
Chapter 14

Service Firms

Higher Level

2012

New Era Gym

100 Marks

Step by step approach

STEPS INVOLVED

- | | |
|--------|---|
| Step 1 | Prepare a statement of the company's reserves (profit and loss balance) |
| Step 2 | Calculate the profit/loss from the shop for the year ended. |
| Step 3 | Prepare a profit and loss account for the year ended. |
| Step 4 | Prepare a balance sheet. |
| Step 5 | Some sort of Theory. |

Step 1 - Prepare a statement of the company's reserves (profit and loss balance)

This is where you look at the start of the question and from the list given identify the assets and liabilities. You will have to complete a working to calculate the correct figure for Buildings and grounds, Equipment, and furniture to include the accumulate depreciation. The number of years to be calculated will be given in the question. You will also have to include the following which students usually leave out -

1. Investment Income - You might have to calculate the figure for investments.
2. Bank - the opening back figure will have to be included. If this figure is on the debit side, it is an asset but if it is on the credit side it is a liability.
3. Loan - You might have to calculate the figure for the loan. Have a look at the payment section in the question and see if they have given you the loan figure or the loan plus the interest figure. If it is the loan plus the interest figure the loan will have to be calculated.
4. The interest figure - Take the loan figure (calculate above) and take it away from the figure in the payment section.

These figures (1-4 above) should be included and are where students lose marks.

Part 1

Identify if the items at the start of the question if they are an asset or liability. Place an A over the item you think is an asset and a L under the item you think is a liability.

Assets	Liabilities
Buildings and grounds at cost (W)	Creditors for Suppliers
Equipment at cost (W)	Client fees paid in advance
Vehicles at cost (W)	Issued Capital
Stock in shop	Loan
Stock of heating oil	Interest
Investment Income	
Contract cleaning prepaid	
Bank	

Remember not to include Authorized capital as this is the amount of money, we can issue but have only issued €450,000. Remember the next step is to do the workings for each of the items that has a W (This will usually be the same for each question)

Part 2

The next part to the question is to do the working for the following -

- | | | |
|----------------------|--------------|-------------|
| 1. Buildings | 3. Equipment | 5. Vehicle |
| 2. Investment Income | 4. Loan | 6. Interest |

Working 1 - Accumulate Depreciation

Buildings

€520,000 * 2%	Need 3 years Depreciation as per the question
= €10,400 Dep Per Year	€10,400 * 3 = €31,200

Need to reduce the buildings by €31,200 (Accumulated Depreciation)

€520,000	
<u>(€31,200)</u>	
€488,800	SoR

Equipment

€75,000 * 10%	Need 3 years Depreciation as per the question
= €7,500 Dep Per Year	€7,500 * 3 = €22,500

Need to reduce the Equipment by €22,500 (Accumulated Depreciation)

€75,000

(€22,500)

€52,500 **SoR**

Vehicles

€60,000 * 20%

Need 3 years Depreciation as per the question

= €12,000 Dep Per Year

€12,000 * 3 = €36,000

Need to reduce the Equipment by €48,000 (Accumulated Depreciation)

€60,000

(€36,000)

€24,000 **SoR**

Working 2 - Investment Income

We are given the Investment figure at the start of the question (€40,000) so we don't have to calculate it. We only need to calculate -

1. the figure yearly figure for the P & L (A)
2. the investment income due for the BS CA

€40,000 * 5%

= **€2,000** Yearly **P & L (A)**

€1,100

€900 **BS CA**

Working 3 - Loan

In this question they are given you the Loan figure (€30,000). This means you only have to calculate -

1. the interest figure.
2. the interest figure of this year P & L (L).
3. the interest figure for next year BS CL.

Total Amount	€36,000	as per the question
Loan	<u>€30,000</u>	as per the question
	€6,000	Interest

€6,000 / 15

= €400 Per month

€400 * 3 Months = €1,200 P & L (L)

€400 * 12 Months = €4,800 SoR

Now that we have all the workings completed and the figures needed, we can now complete the Statement of Reserve

Statement of Capital and Reserve for New Era Gym and Health Centre Ltd on 01.01.11

Assets		
Buildings (w1)	488,800	
Equipment (w1)	52,500	
Furniture (w1)	24,000	
Stock Shop	3,600	
Stock Heating Oil	1,800	
Investment	40,000	
Contact Cleaning	300	
Bank	6,500	617,500
Liabilities		
Creditors	1,500	
Member Fees Prepaid	5,000	
Issued Capital	350,000	
Loan (w3)	30,000	
Interest (w3)	4,800	(391,300)
Reserves 01.01.2008		226,200

Step 2 - Calculate the profit/loss from the shop for the year ended.

The next step is to prepare a profit and loss account for the shop. Highlight all the words that says shop including the start of the question, the receipts and payments account and the end of the question. You will have to complete some workings for the expense section of the profit and loss account

Highlight the following.

Start of the question

Stock in shop (Opening Stock)

Receipt and Payments

Shop receipts (Receipts)

Purchases - Shop (Payments)

End of the Question

Closing Stock - Shop

Adjustment (iv) Salaries (w)

Adjustment (vi) - Light and Heat (w)

Adjustment (vi) - Insurance (w)

Adjustment (vi) - Telephone (w)

We need to do workings from adjustment (iv) taken into account what they are telling us as per the question.

Working 4 - Wages

€20,000 * 40%	Amount	€84,300	As per the question
= €8,000 P & L (Shop)	Less Shop	<u>(€8,000)</u>	See working 5
		€76,300	P & L (L)

Working 5 - Light and Heat

Amount	€3,300	As per the question.	
Less Shop	<u>€300</u>	Adjustment (vi)	P & L Shop
	€3,000		
Add Oil 01.01	<u>€1,800</u>	Start of the question.	
	€4,800		
Less Oil 31.12	<u>€400</u>	End of the question.	BS CA
	€4,400	P & L (L)	
Add Electricity 31.12	<u>€340</u>	End of the question.	BS CL
	€4,740	P & L (L)	

Working 6 - Insurance

Amount	€6,200	As per the question.	
Less shop	<u>€900</u>	Adjustment (vi)	P & L Shop
	€6,000	P & L (L)	

Working 7 - Telephone

Amount	€1,400	As per the question.	
Less shop	<u>€400</u>	Adjustment (vi)	P & L Shop
	€1,000	P & L (L)	

Now we have all the working completed for Part b we can now prepare the Profit and Loss account for the Shop.

Trading Profit and Loss for New Era Gym and Health Centre Ltd on 31.12.11

Sales		42,000
Less Cost of Sales		
Opening Stock	3,600	
Add Purchases	26,000	
	29,600	
Less Closing Stock	1,600	28,000
Gross Profit		14,000
<u>Less Expenses</u>		
Wages (w4)	8,000	
Light & Heat (w5)	300	
Insurance (w6)	900	
Telephone (w7)	400	9,600
Profit		4,400

This profit will be included in the Part C - Profit and Loss account under Assets.

Step 3 - Prepare a profit and loss account for the year ended.

The next step is to complete the profit and loss account. Here you need to work down through each item in the receipt and payment account. The receipts are an asset and the payment is a liability. You will also have to look the adjustments and complete workings for calculate the correct figure -

Receipts

Bank	This has been entered in the SoR account as part of Part A
Client fees	An adjustment will be needed (See Working 8)
Interest on investments	See working 2.
Shop receipts	Used for P & L for the shop. Include if a profit was made.
Balance 31/12/2011	This is the bank overdraft and goes in the BS CL

Working 8 - Client Fees

We need to look at the start of the question to see if there are any member/client fees due or prepaid. Look at the end of the question to see if there are any member/client fees due or prepaid. And have a look to see if there are any dishonored cheques.

01.01.xx	Due	Less	31.12.xx	Due	Add
01.01.xx	Prepaid	Add	31.12.x	Prepaid	Less
Amount	€320,000		Receipts section.		
01.01.16 Prepaid	<u>€5,000</u>		Start of the question.		
	€325,000				
31.12.16 Prepaid	<u>(€5,500)</u>		End of the question.		BS CL
	€319,500				
31.12.16 Due	<u>€600</u>		€2700 + €950 (Cheque Dishonored)		BS CA
	€320,100		P & L (L)		

Remember

Any items that at the end of the question will probably go in the Balance sheet as well.

Profit and Loss account for New Era Gym and Health Centre Ltd for year ended 31.12.11		
Assets		
Client Fees (w8)	€320,100	
Investment Income (w2)	€2,000	
Shop Profit	€4,400	€337,300

Payments

Laundry	Use the figure as per the question.
Telephone and Broadband	See working 7.
Wages and Salaries	See working 4.
Loan Interest	See working 3.
Equipment	See working 9.
New Extension	See working 9.
New Vehicle	See working 9.
Contract Cleaning	An Adjustment will be needed (See Working 10)
Light and Heat	See working 5.
Insurance	See working 6.
Purchase - Shop	Used for P & L for the shop. Include if a profit was made.
Purchases - Suppliers	See working 11.
Loss on Vehicle	See working 9.

Working 9 - Depreciation**Equipment**

Amount	€75,000	as per the question.
Equipment	<u>€20,000</u>	as per the question
	€95,000	BS TA

€95,000 * 10%

= €9,500 P & L (L)

Accumulate Depreciation

Amount	€22,500	As per working 1.
This year	<u>€9,500</u>	As per above
	€32,000	BS TA (Dep)

Buildings

Amount	€520,000	See the start of the question.
New Buildings	<u>€220,000</u>	As per question.
	€740,000	BS TA (Use revalue Figure)
€740,000 * 2%	=	€14,800

Accumulate Depreciation

Amount	€31,200	As per working 1.
This year	<u>€14,800</u>	As per above
	€46,000	BS TA (Dep) (Not needed do to revalue figure)

Vehicle

Vehicles	
€60,000	€60,000
€48,000	€48,000 (BS TA)
€108,000	€108,000

Acc Dep Vehicle	
€42,000	€36,000
€4,800 (BS TA)	€10,800 (P * L (L))
€46,800	€46,800

Disposal	
€60,000	€8,000
	€42,000
	€10,000 (P & L (L))
€60,000	€60,000

Depreciation this year

€60,000 * 20% * 6/12 =	€6,000
€48,000 * 20% * 6/12 =	<u>€4,800</u>
	€10,800

Vehicle Sold

01.01.2008 - 31.12.2008	12
01.01.2009 - 31.12.2009	12
01.01.2010 - 31.12.2010	12
01.01.2011 - 01.07.2011	<u>6</u>
	42 Months

$$\begin{aligned} & \text{€40,000} * 20\% * 42/12 \\ & = \text{€42,000} \end{aligned}$$

Working 10 - Contract Cleaning

Amount	€3,400	As per the question.	
Add Prepaid 01.01	<u>€300</u>	Start of the question.	
	€3,700		
Less Prepaid 31.12	<u>€700</u>	Adjustment (iv)	P & L (L)
	€3,000	BS CA	

Working 11 - Purchases - Suppliers

Amount	€34,600	As per the question.	
Less Creditors 01.01	<u>€1,500</u>	See the start of the question.	
	€33,100		
Add creditors 31.12	<u>€2,000</u>	See the end of the question	BS CL
	€35,100	P & L (L)	

Liabilities		
Laundry	€3,000	
Telephone (w7)	€1,000	
Wages & Salaries (w4)	€76,300	
Loan Interest (w3)	€1,200	
Dep Equipment (w9)	€9,500	
Dep Buildings (w9)	€14,800	
Dep Vehicles (w9)	€10,800	
Contract Cleaning (w10)	€3,000	
Light and Heat (w5)	€4,740	
Insurance (w6)	€5,300	
Purchases - Suppliers (w11)	€35,100	
Loss on Vehicle (w9)	€10,000	€174,740

Profit and Loss account for New Era Gym and Health Centre Ltd for year ended 31.12.11		
Assets		
Client Fees (w8)	€320,100	
Investment Income (w2)	€2,000	
Shop Profit	€4,400	€337,300
Liabilities		
Laundry	€3,000	
Telephone (w7)	€1,000	
Wages & Salaries (w4)	€76,300	
Loan Interest (w3)	€1,200	
Dep Equipment (w9)	€9,500	
Dep Buildings (w9)	€14,800	
Dep Vehicles (w9)	€10,800	
Contract Cleaning (w10)	€3,000	
Light and Heat (w5)	€4,740	
Insurance (w6)	€5,300	
Purchases - Suppliers (w11)	€35,100	
Loss on Vehicle (w9)	€10,000	€174,740
		€157,040
Add Reserves 01.01.13		€226,200
Profit and Loss 31.12.13		€377,960

Step 4 - Prepare a balance sheet.
Working 12 - Revaluation Reserve

New Value	€850,000	As per the question.	BS TA
Cost	<u>€740,000</u>	See working 9.	
Increase in value	€110,000		
Increase in Value	€110,000	See working 11.	
Accumulated Dep	€31,200	See working 9.	
This year Dep	<u>€14,800</u>	See working 9.	
	€156,000	BS FB	

Balance Sheet for for New Era Gym and Health Centre Ltd as at year ended 31.12.11			
Fixed Asset	Cost	Ac Dep	NBV
Buildings (w12)	€850,000	€0	€850,000
Equipment (w9)	€95,000	€32,000	€63,000
Vehicle (w9)	€48,000	€4,800	€43,200
	€993,000	€36,800	€956,200
Financial Assets			
5% Investments (w2)			€40,000
			€996,200
Current Assets			
Closing stock (Shop)		€1,400	
Closing Stock (Oil)		€600	
Cleaning Prepaid (w10)		€500	
Client Fees Due (w8)		€800	
Income Due (w2)		€900	
		€4,200	
Creditors due within one year			
Creditors (Suppliers) (w11)	€2,000		
Client Fees Prepaid (w8)	€5,500		
Electricity Due (w5)	€340		
Bank Overdraft	€108,600	€116,440	(€112,240)
			€883,960
Finance by	Authorized	Issued	
Capital	€400,000	€350,000	
Profit and Loss		€377,960	€727,960
Revaluation reserve (w12)			€156,000
			€883,960

Step 5 - Some sort of Theory.

The company now wishes to purchase equipment for the new extension. Advise the company on how to fund the expected cost of €150,000.

My advice to the company would be:

Sell investments	€40,000
Sell remaining shares	€50,000
Borrow	€60,000

The company would be well able to pay back the loan quickly as the accounts show that it had a surplus €151,760 in 2011 and the company is generating enough cash. Although it owes the bank €108,600 it has paid out amounts up to €310,000 on non-recurring and non-trading items.