

**PENANG SANGAM HIGH SCHOOL**

**P. O BOX 44, RAKIRAKI**

**LESSON NOTES Week 14**

**SUBJECT: ACCOUNTING**

**YEAR/LEVEL: 12**

**Strand 5: Analysis And Interpretation of Financial Statements**

**Sub-strand 5.1:Analysing Accounting Reports** (Ref: MOE Text Year 12 Accounting pg.134- 151)

**Content Learning Outcome:** Analyse financial reports of a sole proprietor to assess its performance.

Greetings to all my students, this week (week 14) we will continue with our coverage, last week we looked at effects of transactions on working capital (WC) and this week we will see how transactions have effect on the net profit (NP) of the business.

**Lesson Notes**

**Effect of Transactions on Net Profit**

**Net profit is calculated as :**

|   |
|---|
| $NP = \text{Revenue} - \text{Expenses}$ |
|---|

So only when **revenue or expense** is affected by a transaction than net profit will change or else it will have **no effect**. It is also important to note that on the accounting equation ( $A + E + D = L + P + R$ ) only (E, R) changes net profit the other elements changing (A, D, L, P) will have no effect on net profit.

**Thus to summarize:**

|      |               |
|------|---------------|
| NP ↑ | Revenue (R) ↑ |
|      | Expense (E) ↓ |
| NP ↓ | Revenue (R) ↓ |
|      | Expense (E) ↑ |

**Note:** When NP increases then decrease by the **same** amount eventually there will be **no effect**.

**Example:**

Ra bookshop provides following transactions for the month of June, 20202:

1. Cash sales \$200.
2. Paid creditors \$300.
3. Credit purchase \$100.
4. Owner took cash for own use \$50.
5. Bought Van for \$10 000 on account.
6. Debtor paid his account \$150 and was allowed \$20 discount.

**Required:**

Using **periodic inventory system** state the effect of each of the given transactions on the **Net Profit** of the business.

**Solutions:**

| Transaction | Explanation-accounts affected | Net Profit (NP) | Final Effect on the WC            |
|-------------|-------------------------------|-----------------|-----------------------------------|
| 1.          | Cash – CA ↑                   | No effect       | NP will <b>increase</b> by \$200. |
|             | Sales – Rev ↑                 | ↑               |                                   |
| 2.          | Creditors- CL ↓               | No effect       | No effect on NP                   |
|             | Cash – CA ↓                   | No effect       |                                   |
| 3.          | Purchase – Exp ↑              | ↓               | NP will <b>decrease</b> by \$100. |
|             | Creditors- CL ↑               | No effect       |                                   |
| 4.          | Drawings- P ↓                 | No effect       | No effect on NP.                  |
|             | Cash- CA ↓                    | No effect       |                                   |
| 5.          | Van - FA ↑                    | No effect       | No effect on NP.                  |
|             | Creditor- CL ↑                | No effect       |                                   |
| 6.          | Cash- CA ↑                    | No effect       | NP <b>decrease</b> by \$20.       |
|             | Discount Allowed- Exp ↑       | ↓               |                                   |
|             | Debtor- CA ↓                  | No effect       |                                   |

**Class Activity (Teachers own activity):**

Ra supermarket provides the following transactions for the month of May, 2020:

1. Paid rent \$500.
2. Owner took goods for own use \$100.
3. Credit Sales \$400.
4. Cash purchase \$600.
5. Paid Creditors \$300 and received \$50 discount.

**Required:**

Using **periodic inventory system** state the effect of each of the given transactions on the Net profit (NP) of the business.

(Solutions of the above activity will be provided later for reference and marking, please attempt the activities using the lesson notes and example provided)

**(Best wishes for week 14 studies, take care and Stay Safe)**

