CHAPTER NINE

FINAL ACCOUNTS: STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

CHAPTER OUTLINE

- Statement of comprehensive income
- Revenue and capital expenditures
- Format for statement of comprehensive income

Learning Objectives:

At the end of this chapter, the student should be able to:

- Differentiate between revenue and capital expenditures
- Identify items treated in Statement of Profit or Loss and other comprehensive income and statement of financialposition.
- Explain the relationship between subsidiary books, ledger, trial balance and final accounts.
- Calculate the cost of goods sold.
- Determine gross profit and net profit.
- Prepare statement of comprehensive income.

9.1. STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME: This is a report prepared to determine the profit or loss of an entity at the end of an accounting period. The summary of the income earned is recorded and compared with the expenses incurred. Recall that there is a difference between income earned and income received; so also between expenses incurred and expenses paid. If in doubt, then refer to the realization principle earlier discussed in this book. The difference between the income earned and expenses incurred is the profit or loss of the business for the period. Expenses as mentioned above are of two types: revenue expenditure and capital expenditure.

9.2. REVENUE AND CAPITAL EXPENDITURES

(a) Revenue Expenditures: These are expenditures incurred whose benefits are consumed within an accounting period. They are mostly made for the day to day running of the business. Some of these revenue expenditures are more direct in nature as they affect cost of goods sold and therefore, are used to determine the gross profit of the business while those that are indirect in nature such as rent, rate, electricity, e.t.c are used to determine the net profit of the business.

In the treatment or preparation of statement of comprehensive income, only revenue expenditure is used. It is equally worthy of note that there are some non-revenue expenditures which may be expensed in the statement. Such expenditure includes immaterial or insignificant value expenditure such as the purchase of calculator, ruler, e.t.c. Though the benefit of such item may not be consumed in one accounting period, the business still writes it off as expense within one accounting period due to its small value as emphasized in materiality convention. In some entities, the management sets what is known as **materiality limit** so that all items whose costs are less than that limit, even when used for more than one accounting period, should be expensed in the year of acquisition.

(b) Capital expenditures: Theses are expenditures that are capital intensive in nature, used to procure assets that the business entity will use for more than one accounting period. Such expenditures are capitalized to the statement of financial position and not expensed in statement of comprehensive income. Since the assets purchased are used over a number of years to generate income, the cost is therefore recognized systematically over the number of years for which the associated benefits are consumed. This is in line with the matching concept.

Having explained the difference between the capital and revenue expenditures, we can go on to have a wider discussion of the statement of comprehensive income. One primary aim of every business is to make profit. The book keeping process is necessitated because the businessman would

want to record every transaction relating to the business so as to determine how fruitful the business is at the end of the period. The book-keeping process provides the necessary information from which the businessman will be able to calculate profit earned or loss incurred by the business. The account which is primarily aimed at determining the profit or loss of the business is called Statement of Comprehensive Income, formerly known as Trading, Profit and Loss Account before the introduction of the International Financial Reporting Standard (IFRS). To prepare the statement of comprehensive income, the first task is to determine the gross profit i.e. turnover less cost of goods sold. The reader needs to understand the interplay of variables required to determine the cost of goods sold. It is computed as follows:

Opening stock		X
Add Purchases	X	
Carriage Inwards	<u>X</u>	X
Total goods Available		X
Less: Closing stock		<u>(X)</u>
Cost of goods sold		X

To complete the double entry principle, the sales account is closed by debiting the sales account and crediting the trading account while the purchases account is credited with the balance therein and trading account debited. At this point, the closing value of the assets which was determined during the end of the period stock taking has no existing account; hence a new stock account is opened and debited with the value of the closing stock. The closing stock is brought into the calculation of the gross profit which is affected in the Trading Account, hence the credit entry for the closing stock should be in the Trading Account to complete the double entry principle. Note however, that the effect of crediting the trading account with the closing stock is a deduction from the purchases account which currently is directly deducted from the purchases in the trading account.

9.3. FORMAT FOR STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE

It is now ripe to draw up the statement of profit or loss and other comprehensive income by transferring all revenues to the credit side of the account and all expenses incurred for the year to the debit side of the statement of profit or loss and other comprehensive income (if "T" format is adopted). At this level, we may not throw the full weight of the International Financial Reporting Standards as we will be looking at this statement as one prepared for internal use. The first part of the statement shows the trading activities aimed at determining the gross profit i.e. the excess of sales over the cost of goods sold. We may equally try to show the differences between the former presentation of the trading, profit and loss account and the current way of presenting the statement of profit or loss and other comprehensive income. The two formats will be displayed below, adopting the vertical format.

The last part of the statement of profit or loss and other comprehensive income is aimed at determining the net profit of the business.

See the format of statement of profit or loss and other comprehensive income (for internal use). Vertical format:

Obollo Enterprises'

Statement of profit or loss and other Comprehensive Income for the year ended 31st December, 2009.

	₦	₦
Turnover (Sales)		X
Less Sales Returns	(X)	
Less Cost of sales:		
Opening Stock	X	
Add: Purchases	X	
Less Purchase Returns	(X)	
Add Carriage Inwards	X	
Cost of goods Available	XX	
Closing Stock	(X)	
Cost of Goods Sold	X	
Wages	X	
Cost of Sales		(X)
Gross Profit		XXX
Add Other Incomes:		
Interest Received	X	
Discount Received	X	
Decrease in provision for bad debt	X	X
		XXX

Less expenses:		
Salaries		X
Rent and rates		X
Carriage Outwards		X
Depreciation		X
Printing & Stationery		X
Discount Allowed		X
Advertising		X
		(XX)
Net Profit		XXX.

IMPORTANT ISSUES TO NOTE

1. Closing Stock Valuation: The principle is that the closing stock should be valued at cost or market value, whichever is less.

2. Carriage Inwards: This refers to cost of transport that the business incurs in moving goods bought for resale into the place of business. It is a cost incurred in order to bring the goods into a condition that is necessary for its sale, hence it should be charged to the trading account. It is added to the cost of purchases.

3. Wages: If the wages is in respect of production or factory, it is charged against the trading account but if it is administrative wages, it is charged to profit or loss account. In a situation where wages and salaries form one account, it is debited to profit or loss section.

The International Financial Reporting Standard format of the Statement of Comprehensive Income is thus:

XYZ Company

Statement of Profit or Loss and other Comprehensive Income for the year ended 31 December, 2012

	31/12/11	31/12/12
	₦	₦
Revenue	X	X
Cost of Sales	(X)	(X)
Gross Profit		

Other Income	X	X
Distribution Costs		
Administrative expenses	(X)	(X)
Other Expenses	(X)	(X)
Finance Costs	(X)	(X)
Profit Before Tax	X	X
Income Tax expense	(X)	(X)
Profit for the year from continuing operations	X	X
Loss for the year from discontinuing operations	(X)	(X)
Profit for the year	X	X
Other/comprehensive income		
Exchange difference from translation of foreign operations	X	X
Available for sale financial assets	X	X
Cash flow hedges	X	X
Gains on property revaluation	X	X
Actuarial gains (losses) on defined benefit pension plans	X	X
Share of other Comprehensive income of associates	X	X
Income tax relating to components of other comprehensive income	(X)	(X)
Other comprehensive income for the year net of tax	X	X
Total comprehensive income for the year	X	X

(Culled from IFRS for Dummies, page23).

Note that the format above is a comprehensive one for companies which can be modified to suit any other business entity.

In the standard under the revised IAS 1, one can split the statement of profit or loss and other comprehensive income into two separate statements showing:

1. The income statement itself and
2. A statement starting with profit (or loss) for the year from continuing operation (or loss for the year from discontinuing operation as the case may be) and then disclosing the separate components of other comprehensive income (with any gain or loss taken directly to the equity section of the statement of financial position. (culled from IFRS for dummies). Detailed discussion of IFRS requirement will be considered in advanced stage of this course.

Illustration 9.1.

From the following trial balance of Chibuike Enterprises, you are required to draw up a statement of Profit or Loss and other Comprehensive Income for the year ended 31st December, 2011.

	Dr	Cr
	₦	₦
Sales		53,000
Purchases	30,000	
Carriage Outward	100	
Electricity	200	
Salaries and Wages	2,500	
Insurance	50	
Building	5,000	
Fixtures	10,000	
Debtors	500	
Creditors	200	
Bank balance	5,000	
Carriage Inwards	100	
Motor Vehicles	10,000	
Capital		10,000
Return outwards		250
	63,450	**63,450**

Solution 9.1.

Chibuike Enterprises'

Statement of Profit or Loss and other Comprehensive Income for the year ended 31st December, 2011.

	₦	₦
Sales		53,000
Less cost of Sales:		
Purchases	30,000	
Less Return Outwards	(250)	
Carriage Inwards	100	

Cost of Goods Sold		(29,850)
Gross Profit		23,150
Less Expenses:		
Carriage Outwards	100	
Electricity	200	
Salaries and Wages	2,500	
Insurance	50	(2,850)
Net Profit		20,300

Going through the trial balance at the end of the preparation of the statement of comprehensive income, one will realize that there are some items left untouched such as capital, buildings, fixtures and other assets and liabilities. Such items are not treated in the statement of comprehensive income but exclusively in the statement of financial position.

Illustration 9.2

The following trial balance was extracted from the books of Anambra, a sole proprietor, whose business is known as Anambra enterprises as at December 31, 2016.

	Dr ₦'000	Cr ₦'000
Capital		224,000
Motor Van	80,000	
Inventory	65,000	
Balance at bank	49,600	
Purchases	640,000	
Sales		892,000
Trade Receivables	116,000	
Trade Payables		66,240
Rent and Rates	22,432	
Salaries	140,160	
General Expenses	17,888	
Motor Expenses	10,240	
Discount Allowed	16,160	
Discount Received		15,840
Insurance	7,840	
Bad Debts	12,160	
Drawings	20,000	
	1,198,080	1,198,080

The following matter is to be taken into account:

I. Trade inventories as at December 31, 2013 was ₦80,640,000

Required:
Prepare the income statement for the year ended December 31, 2016.

Solution 9.2

Anambra's
Statement of Profit or Loss and other Comprehensive Income for the Year Ended 31 December, 2016.

	₦'000	₦'000	₦'000
Sales			892,000
Less: Cost of Sales			
Opening Inventory		65,600	
Add: Purchases		640,000	
		705,600	
Less: Closing Inventory		80,640	624,960
Gross Profit			267,040
Add discount received			15,840
			282,880
Less expenses:			
Salaries		140,160	
Rent & Rates		48,000	
General Expenses		17,888	
Motor Expenses		10,240	
Discount Allowed		16,160	
Insurance		7,840	
Bad Debts		12,160	252,448
Net Profit			**30,432**