SOLUTIONS TO END-OF-CHAPTER QUESTIONS CHAPTER 2

DEVELOP YOUR UNDERSTANDING

Question 2.1

Resources that are assets

Apply the four criteria to show why the resources in the question are assets of entities and so are recognised on the statement of financial position.

(a) Motor vehicles purchased by an entity

- Does the entity control the resource? Yes, by virtue of purchasing the motor vehicles and registering them in the company's name at the DVLA.
- Is there a past event giving rise to control of that resource by the entity? Yes, the purchase of the vehicles.
- Will future economic benefits flow to the entity from that resource? Yes, the motor vehicles can be used to deliver goods to customers, be used by sales reps to visit customers to generate more sales or for any other business purpose that will result in increasing profits, cash and the inflow of economic benefits.
- Can the cost or value of the asset be measured reliably in monetary terms? Yes, the cost of the motor vehicles can be readily determined from the purchase documents and the cash paid from the bank.

(b) Inventory received from suppliers

- Does the entity control the resource? Yes, by virtue of the contract signed or verbal agreement with suppliers for the supply of goods to the entity.
- Is there a past event giving rise to control of that resource by the entity? Yes, the delivery of the inventory by suppliers and the receipt of that inventory by the entity (legally, title to the goods passes on receipt by the customer).
- Will future economic benefits flow to the entity from that resource? Yes, the inventory can be used in production to produce more goods for sale or, in the case of retail businesses, the inventory can be sold at a higher price to customers and so produce economic benefits in the form of cash flow and profit.
- Can the cost or value of the asset be measured reliably in monetary terms? Yes, the cost of the inventory can be readily determined from the invoices from the suppliers and by the cash paid from the bank to suppliers for the goods delivered.

(c) Cash and cash equivalents

- Does the entity control the resource? Yes, the entity controls the cash through the presence of the cash on company premises or as a result of the cash being deposited into the entity's bank account.
- Is there a past event giving rise to control of that resource by the entity? Yes, the receipt of cash in exchange for goods or services sold and deposited in the bank.
- Will future economic benefits flow to the entity from that resource? Yes, the cash can be used to purchase more goods for use in production or for resale or to repay liabilities upon which interest is being charged thereby saving interest and increasing cash resources in the future still further.
- Can the cost or value of the asset be measured reliably in monetary terms? Yes, cash can be measured in terms of the amount of physical cash on the business's premises or by reference to the bank statements if the cash is in the bank.

Resources that are NOT assets

Applying the four criteria to show why the resources in the question are NOT assets of an entity and why they are no longer/not recognised on the statement of financial position of entities.

(a) Redundant plant and machinery

- Does the entity control the resource? Yes, by virtue of purchasing the plant and machinery in the past and using it in the business in the past to produce goods for sale.
- Is there a past event giving rise to control of that resource by the entity? Yes, the purchase of the plant and machinery in the past.
- Will future economic benefits flow to the entity from that resource? No, the plant and machinery is now redundant and will not produce any more goods or result in a cash receipt when it is sold or scrapped, so there are no more economic benefits associated with this piece of plant and machinery. If there are disposal costs for this plant and machinery, you might even be able to make out a case that a liability now exists in relation to this plant and machinery. There would then be an outflow of economic benefits and the obligation to pay these disposal costs exists and is unavoidable.
- Can the cost or value of the asset be measured reliably in monetary terms? Yes, the cost of the plant and machinery can be readily determined from the purchase documents and the cash paid from the bank.

Result: while the resource meets three of the four criteria, it fails on the third criterion (no future economic benefits) and so the asset, which would have been previously recognised by the entity on its statement of financial position, is now derecognised and is removed from property, plant and equipment.

(b) Trade receivable that will not be recovered

- Does the entity control the resource? Yes, by virtue of delivering goods/providing services to the customer and the customer taking delivery of those goods/services and assuming the obligation to pay for them.

- Is there a past event giving rise to control of that resource by the entity? Yes, the delivery of the goods/services to the customer.
- Will future economic benefits flow to the entity from that resource? No, the customer will not pay the invoice because of its bankruptcy and so no future economic benefits will flow to the entity from this trade receivable.
- Can the cost or value of the asset be measured reliably in monetary terms? Yes, the sales invoice from the entity to the customer can be used to measure the value of the trade receivable reliably.

Result: while the resource meets three of the four criteria, it fails on the third criterion (no future economic benefits) and so the asset, which would have been previously recognised by the entity on its statement of financial position, is now derecognised and is removed from trade receivables.

(c) A highly skilled workforce

- Does the entity control the resource? Yes, to the extent that the entity controls the workforce while they are working for the organisation, but the entity is powerless to stop individual workers leaving and joining another company, taking all their skills and knowledge with them.
- Is there a past event giving rise to control of that resource by the entity? Yes, each member of the workforce signed their contract.
- Will future economic benefits flow to the entity from that resource? Yes, the highly skilled workforce will produce goods/services and hence sales and profits for the company into the future.
- Can the cost or value of the asset be measured reliably in monetary terms? No: it is not possible to measure the cost of an employee to the business reliably.

Result: while the resource meets two of the four criteria, it fails on the other two criteria (lack of control and no reliable monetary measure) and so the asset, which would never have been previously recognised by the entity on its statement of financial position, still cannot be recognised.

› Question 2.2

Oxford Academicals Football Club Limited

This is a further application of the criteria to determine whether entities can recognise assets on their statement of financial position or not. Looking at the four criteria:

- The football club controls the resources, the players, through the contracts that they signed.
- As the club holds the players' registrations and has contracts with the players that they will play exclusively for Oxford Academicals, other football clubs can legally be prevented from employing the club's players in their teams.
- There is a past event, the signing of the contracts by the players and, in the case of those players whose contracts were bought from other clubs, cash paid.
- All the players should produce future economic benefits for the club as spectators will pay to watch the team play, there will be monetary rewards for end of season league position and trophies won and, when the players become surplus to requirements, lose form or fall out with the manager, their contracts can be sold to other clubs for a transfer fee or used in player for player swaps.

- In the case of the players whose contracts have been bought, there is a reliable measurement of their cost, the transfer fees of £25 million. In the case of players developed by the club, there is no reliable measure of their cost or value.

Result: the contracts of the bought in players meet all the criteria for asset recognition, so they can be recognised on the statement of financial position at a cost of £25 million. The internally developed players cannot be recognised as assets on the statement of financial position as they only meet three out of the four criteria. This may seem unfair and even illogical, but this is how the accounting rules work.

The player registrations that can be recognised on the statement of financial position will be classed as intangible non-current assets. The players will normally be signed on contracts that exceed 12 months (once a player has one year or less to run on their contract, then these registrations should become intangible current assets as the assets will be used up within one year).

As accounting information is meant to be useful and to help users of accounts make economic decisions, it is quite likely that there will be a note in the accounts explaining that not all player registrations are recognised on the statement of financial position but that the current value of the players not so recognised is estimated by the directors to be so many £million. In this way, an additional disclosure will help users understand all the player resources controlled by Oxford Academicals Football Club.

Question 2.3

Alma Limited: statement of financial position at 30 April 2018

ASSETS	**£000**	**Note**
Non-current assets		
Intangible assets	—	1
Property, plant and equipment	6,500	2
	6,500	
Current assets		
Inventories	1,000	
Trade receivables	1,750	
Cash and cash equivalents	10	
	2,760	
Total assets	**9,260**	3
LIABILITIES		
Current liabilities		
Short-term borrowings	1,000	4
Trade payables	1,450	
Taxation payable	540	
	2,990	
Non-current liabilities		
Long-term borrowings	1,000	5
Total liabilities	**3,990**	6
Net assets	**5,270**	7
EQUITY		
Called up share capital	1,000	
Share premium	1,500	
Retained earnings	2,770	
Total equity	**5,270**	8

Notes

1. There are no intangible assets in Alma so the total here is zero.
2. (Plant and machinery) £2,000 + (land and buildings) £4,500 = £6,500.
3. Total assets = non-current assets + current assets, so £6,500 + £2,760 = £9,260.
4. (Bank loan due within 12 months) £200 + (bank overdraft: overdrafts are repayable on demand, so due within the next 12 months) £800 = £1,000.
5. Long-term borrowings: the bank loan due seven years after the statement of financial position date on 30 April 2025.
6. Total liabilities = current liabilities + non-current liabilities, so £2,990 + £1,000 = £3,990.

7. Net assets: total assets – total liabilities = £9,260 – £3,990 = £5,270.
8. Total equity: share capital + share premium + retained earnings = £1,000 + £1,500 + £2,770 = £5,270.

Bella Limited: statement of financial position at 30 April 2018

ASSETS	**£000**	**Note**
Non-current assets		
Intangible assets	—	1
Property, plant and equipment	28,100	2
	28,100	
Current assets		
Inventories	700	
Trade receivables	3,000	
Cash and cash equivalents	825	3
	4,525	
Total assets	**32,625**	4
LIABILITIES		
Current liabilities		
Short-term borrowings	400	5
Trade payables	4,000	
Taxation payable	1,100	
	5,500	
Non-current liabilities		
Long-term borrowings	10,000	6
Total liabilities	**15,500**	7
Net assets	**17,125**	8
EQUITY		
Called up share capital	5,000	
Share premium	7,500	
Retained earnings	4,625	
Total equity	**17,125**	9

Notes

1. There are no intangible assets in Bella Limited so the total here is zero.
2. (Plant and machinery) £9,500 + (land and buildings) £17,100 + (motor vehicles) £1,500 = £28,100.
3. (Cash at bank) £800 + (cash in hand) £25 = £825.
4. Total assets = non-current assets + current assets, so £28,100 + £4,525 = £32,625.
5. Bank loan due within 12 months of the statement of financial position date.

6. Long-term borrowings: the bank loan due seven years after the statement of financial position date on 30 April 2025.
7. Total liabilities = current liabilities + non-current liabilities, so £5,500 + £10,000 = £15,500.
8. Net assets: total assets – total liabilities = £32,625 – £15,500 = £17,125.
9. Total equity: share capital + share premium + retained earnings = £5,000 + £7,500 + £4,625 = £17,125.

Carla Limited: statement of financial position at 30 April 2018

ASSETS	£000	Note
Non-current assets		
Intangible assets	600	1
Property, plant and equipment	15,900	2
	16,500	
Current assets		
Inventories	800	
Trade receivables	2,750	
Cash and cash equivalents	15	
	3,565	
Total assets	**20,065**	3
LIABILITIES		
Current liabilities		
Short-term borrowings	1,550	4
Trade payables	1,750	
Taxation payable	800	
	4,100	
Non-current liabilities		
Long-term borrowings	1,500	5
Total liabilities	**5,600**	6
Net assets	**14,465**	7
EQUITY		
Called up share capital	2,500	
Share premium	4,500	
Retained earnings	7,465	
Total equity	**14,465**	8

Notes

1. (Goodwill) £400 + (trademarks) £200 = £600.
2. (Plant and machinery) £3,750 + (land and buildings) £10,200 + (motor vehicles) £1,950 = £15,900.
3. Total assets = non-current assets + current assets, so £16,500 + £3,565 = £20,065.

4. (Bank loan due within 12 months) £300 + (bank overdraft: overdrafts are repayable on demand, so due within the next twelve months) £1,250 = £1,550.
5. Long-term borrowings: the bank loan due seven years after the statement of financial position date on 30 April 2025.
6. Total liabilities = current liabilities + non-current liabilities, so £4,100 + £1,500 = £5,600.
7. Net assets: total assets – total liabilities = £20,065 – £5,600 = £14,465.
8. Total equity: share capital + share premium + retained earnings = £2,500 + £4,500 + £7,465 = £14,465.

Deborah Limited: statement of financial position at 30 April 2018

ASSETS	**£000**	**Note**
Non-current assets		
Intangible assets	350	1
Property, plant and equipment	14,250	2
	14,600	
Current assets		
Inventories	750	
Trade and other receivables	3,200	3
Cash and cash equivalents	558	4
	4,508	
Total assets	**19,108**	5
LIABILITIES		
Current liabilities		
Short-term borrowings	—	6
Trade payables	5,600	
Taxation payable	—	7
	5,600	
Non-current liabilities		
Long-term borrowings	—	6
Total liabilities	**5,600**	8
Net assets	**13,508**	9
EQUITY		
Called up share capital	3,000	
Share premium	5,000	
Retained earnings	5,508	
Total equity	**13,508**	10

Notes

1. (Goodwill) £250 + (trademarks) £100 = £350.
2. (Plant and machinery) £4,250 + (land and buildings) £8,750 + (motor vehicles) £1,250 = £14,250.

3. (Trade receivables) £2,950 + (tax repayable: cash will be coming into the business so this is a receivable, hence the title of this total is now trade *and other* receivables) £250 = £3,200.
4. (Cash at bank) £550 + (cash in hand) £8 = £558.
5. Total assets = non-current assets + current assets, so £14,600 + £4,508 = £19,108.
6. There are no short- or long-term borrowings in Deborah, so a zero figure is recorded against these headings.
7. Taxation payable: this year there is a tax repayment due so this is recorded as a receivable rather than a payable, so there is zero taxation payable.
8. Total liabilities = current liabilities + non-current liabilities, so £5,600 + £Nil = £5,600.
9. Net assets: total assets – total liabilities = £19,108 – £5,600 = £13,508.
10. Total equity: share capital + share premium + retained earnings = £3,000 + £5,000 + £5,508 = £13,508.

Eloise Limited: statement of financial position at 30 April 2018

ASSETS	£000	Note
Non-current assets		
Intangible assets	950	1
Property, plant and equipment	21,600	2
	22,550	
Current assets		
Inventories	900	
Trade and other receivables	3,900	3
Cash and cash equivalents	212	4
	5,012	
Total assets	**27,562**	5
LIABILITIES		
Current liabilities		
Short-term borrowings	—	6
Trade payables	5,800	
Taxation payable	—	7
	5,800	
Non-current liabilities		
Long-term borrowings	—	6
Total liabilities	**5,800**	8
Net assets	**21,762**	9
EQUITY		
Called up share capital	4,500	
Share premium	9,000	
Retained earnings	8,262	
Total equity	**21,762**	10

Notes

1. (Goodwill) £500 + (trademarks) £450 = £950.
2. (Plant and machinery) £5,000 + (land and buildings) £15,000 + (motor vehicles) £1,600 = £21,600.
3. (Trade receivables) £3,100 + (tax repayable: cash will be coming into the business so this is a receivable, hence the title of this total is now trade *and other* receivables) £800 = £3,900.
4. (Cash at bank) £200 + (cash in hand) £12 = £212.
5. Total assets = non-current assets + current assets, so £22,550 + £5,012 = £27,562.
6. There are no short- or long-term borrowings in Eloise Limited, so a zero figure is recorded against these headings.
7. Taxation payable: this year there is a tax repayment due, so this is recorded as a receivable rather than a payable so there is zero taxation payable.
8. Total liabilities = current liabilities + non-current liabilities, so £5,800 + £Nil = £5,800.
9. Net assets: total assets – total liabilities = £27,562 – £5,800 = £21,762.
10. Total equity: share capital + share premium + retained earnings = £4,500 + £9,000 + £8,262 = £21,762.

›Question 2.4

Maria: statement of financial position at 31 October 2018 and 7 November 2018

	Statement of financial position at 31 October 2018 £	Increase £	Decrease £	Statement of financial position at 7 November 2018 £
Non-current assets				
Property, plant and equipment	**15,000**			**15,000**
Current assets				
Inventory	20,000	2,500[4]	1,200[3]	21,300
Other receivables	3,000			3,000
Cash and cash equivalents	500	2,000[3]	300[5]	2,200
	23,500			**26,500**
Total assets	**38,500**			**41,500**
Current liabilities				
Bank overdraft	7,000	3,500[1]	10,000[2]	500
Trade and other payables	8,000	2,500[4]	3,500[1]	7,000
Taxation	3,000			3,000
Total liabilities	**18,000**			**10,500**
Net assets	**20,500**			**31,000**
Capital account				
Balance at 31 October 2018	**20,500**	10,000[2]	300[5]	**31,000**
		800[3]		

Notes

1. Paying trade payables from the bank account will increase the overdraft by £3,500. Money has been paid out of the bank account thereby increasing the amount owed to the bank while reducing the amounts owed to trade payables by the same amount.
2. £10,000 paid into the bank account by Maria will increase the balance in her capital account by £10,000 (this is the owner's own money introduced into the business) and reduce the bank overdraft by £10,000. Less money is owed to the bank but more money is now owed to Maria.
3. Cash goes up by £2,000 as this is money flowing into the business. As inventory has been sold in the first week of November, the inventory will decrease by £1,200. This leaves a difference of £800 which is profit on the sales made (sales made – the cost of making those sales). Profit is added to the capital account. Any profit retained in the business during the year is added to the capital account as this profit belongs to and is owed to the business's owner.
4. New inventory purchased by the business means that the value of inventory will increase by £2,500. As the inventory was purchased on credit from suppliers (trade payables), trade payables will also increase by £2,500 as more money is now owed to them.
5. The £300 taken out of the business represents a repayment of money owed by the business to the owner. Therefore, the capital account is reduced by £300: the business owes Maria £300 less than it did before this transaction. The £300 was taken out in cash, so cash reduces by £300.

TAKE IT FURTHER

Question 2.5

Andy Limited: statement of financial position at 30 June 2018 and 7 July 2018

ASSETS	Statement of financial position at 30 June 2018	Increase	Decrease	Statement of financial position at 7 July 2018
	£	£	£	£
Non-current assets				
Property, plant and equipment	320,000	20,000[2]		340,000
Current assets				
			2,500[4]	
Inventories	50,000	15,000[5]	7,500[3]	55,000
Trade receivables	75,000	10,000[3]	3,000[1]	82,000
		3,000[1]	2,500[1]	
Cash and cash equivalents	20,000	3,250[4]	10,000[6]	13,750
	145,000			**150,750**
Total assets	**465,000**			**490,750**
LIABILITIES				
Current liabilities				
			7,000[6]	
Trade payables	80,000	15,000[5]	2,500[1]	85,500
Taxation	20,000		3,000[6]	17,000
	100,000			**102,500**
Non-current liabilities				
Bank loan (long-term borrowings)	250,000	20,000[2]		270,000
Total liabilities	**350,000**			**372,500**
Net assets	**115,000**			**118,250**
EQUITY				
Called up share capital	20,000			20,000
Retained earnings	95,000	2,500[3]		98,250
		750[4]		
Total equity	**115,000**			**118,250**

Notes

1. 1 July 2018: the payment of the trade payable reduces both trade payables and cash and cash equivalents by £2,500. 1 July 2018: the receipt of a cheque from a trade receivable reduces trade receivables by £3,000, but increases the cash and cash equivalents balance by the same amount.
2. 2 July 2018: both the bank loan and the property, plant and equipment will increase by £20,000. There are £20,000 more assets and £20,000 more liabilities.
3. 4 July 2018: inventory of £7,500 has been sold, so inventory decreases by this amount. The buyer has agreed to buy the goods for £10,000 and pay in August, so trade receivables increase by £10,000. The profit on the transaction of £2,500 (£10,000 – £7,500) will increase retained earnings.
4. 5 July 2018: similarly, inventory of £2,500 has been sold, so inventory decreases by this amount. The buyer paid cash of £3,250 for the goods and so cash increases by £3,250. The profit on the transaction of £750 (£3,250 – £2,500) increases retained earnings.
5. 6 July 2018: both inventory and trade payables increase by £15,000 as there are more goods in stock and there is a bigger liability due to trade payables for goods supplied.
6. 7 July 2018: taxation payable reduces by £3,000 and trade payables decreases by £7,000 as these two amounts have now been paid and are no longer obligations of Andy Limited. The total payment of £10,000 reduces the balance in the bank account by this amount.

Question 2.6

(a) Frankie Limited: statement of financial position at 31 December 2018

	£000	Note
ASSETS		
Non-current assets		
Intangible assets	1,000	1
Property, plant and equipment	27,800	2
	28,800	
Current assets		
Inventories	2,500	
Trade receivables	4,910	
Cash and cash equivalents	605	3
	8,015	
Total assets	**36,815**	4
LIABILITIES		
Current liabilities		
Short-term borrowings	850	5
Trade payables	6,720	
Taxation payable	1,380	6
	8,950	
Non-current liabilities		
Long-term borrowings	8,500	7
Total liabilities	**17,450**	8
Net assets	**19,365**	9
EQUITY		
Share capital	2,000	
Share premium	4,000	
Retained earnings	13,365	
Total equity	**19,365**	10

Notes

1. Goodwill is an intangible asset, so £1,000,000 is recorded as a non-current asset under this heading.
2. (Land and buildings) £15,500,000 + (fixtures and fittings) £1,670,000 + (plant and machinery) £10,630,000 = £27,800,000.
3. (Cash at bank) £600,000 + (cash in hand) £5,000 = £605,000.
4. Total assets = non-current assets + current assets, so £28,800,000 + £8,015,000 = £36,815,000.
5. Short-term, current borrowings are the borrowings due for repayment within one year of the statement of financial position date, i.e. due for repayment by 31 December 2019, so these borrowings are recorded as current liabilities.
6. Taxation payable is a short-term, current liability.
7. Long-term, non-current borrowings are those due for repayment after more than one year from the statement of financial position date. As 31 December 2027 is nine years after the current statement of financial position date, the £8,500,000 is classified as a non-current liability.
8. Total liabilities = current liabilities + non-current liabilities, so £8,950,000 + £8,500,000 = £17,450,000.
9. Net assets: total assets – total liabilities = £36,815,000 – £17,450,000 = £19,365,000.
10. Total equity: share capital + share premium + retained earnings = £2,000,000 + £4,000,000 + £13,365,000 = £19,365,000.

(b) Frankie Limited: statement of financial position at 31 December 2018 and 31 January 2019

ASSETS	Statement of financial position at 31 December 2018 £000	Increase £000	Decrease £000	Statement of financial position at 31 January 2019 £000
Non-current assets				
Intangible assets	1,000			1,000
Property, plant and equipment	27,800	2,500[3]	2,000[8]	28,300
	28,800			**29,300**
Current assets				
Inventory	2,500	12,200[1]	11,450[2]	3,250
Trade receivables	4,910	15,500[2]	6,450[6]	13,960
Cash and cash equivalents	605	1,500[4]	690[5]	1,955
		6,450[6]	8,210[7]	
		2,500[8]	200[9]	
	8,015			**19,165**
Total assets	**36,815**			**48,465**
LIABILITIES				
Current liabilities				
Short-term borrowings	850		200[9]	650
Trade payables	6,720	12,200[1]	8,210[7]	10,710
Taxation payable	1,380		690[5]	690
	8,950			**12,050**
Non-current liabilities				
Long-term borrowings	8,500	2,500[3]		11,000
Total liabilities	**17,450**			**23,050**
Net assets	**19,365**			**25,415**
EQUITY				
Share capital	2,000	500[4]		2,500
Share premium	4,000	1,000[4]		5,000
Retained earnings	13,365	4,050[2]		17,915
		500[8]		
Total equity	**19,365**			**25,415**

Notes

1. Inventory has been acquired, so the value of inventory increases by £12,200,000. As the inventory has not yet been paid for, trade payables (= suppliers) will also increase by £12,200,000 as they are now owed this additional amount for the inventory supplied on credit.

2. Sales have been made on credit to trade receivables (= customers), so trade receivables now owe a further £15,500,000 to Frankie Limited and so increase by this amount. The cost of the goods sold by the company was £11,450,000. As this inventory has now been sold, inventory decreases by £11,450,000 to derecognise the asset that is no longer represented on Frankie Limited's statement of financial position. The difference between the selling price of £15,500,000 and the cost of the inventory sold of £11,450,000 is £4,050,000, which represents the profit on the sales transactions. This profit is added to retained earnings.
3. New plant and machinery has been acquired, so property, plant and equipment increases by £2,500,000. The money used to acquire these new non-current assets has been borrowed, so borrowings must also rise by the same amount. The new borrowings are due for repayment in December 2023, which is more than one year after the end of January 2019, so these new borrowings are added to non-current liabilities.
4. Cash has been raised from the share issue, so cash increases by £1,500,000, the total proceeds of the share issue. As £500,000 of the cash raised relates to the share capital, this balance also increases by £500,000. The remaining £1,000,000 of the cash raised relates to share premium, so this balance increases by this amount.
5. Cash has been paid to the tax authorities, so cash must decrease by £690,000. Now that this liability has been discharged, taxation payable also falls by £690,000 as the obligation has been settled and economic benefits in the form of cash have flowed out of the company to settle the obligation.
6. Trade receivables have paid £6,450,000 of the amounts owed to Frankie, so trade receivables now decrease by this amount to reflect the realisation of this asset through the receipt of cash. Cash will also increase by the same amount as these amounts owed by the trade receivables have now turned into cash.
7. Frankie has discharged obligations owed to trade payables of £8,210,000, so trade payables fall by this amount as the liability has now been paid. As the amounts owed were paid in cash, cash also falls by the same amount to reflect the transfer of economic benefits to settle the obligations to trade payables.
8. The sale of the non-current asset results in the derecognition of the land as the resource is no longer owned or controlled by Frankie. As a result of the sale of the land, property, plant and equipment fall by the original historic cost of the land of £2,000,000. Cash has now been received of £2,500,000, so cash increases by this amount. The difference between the original cost of the land of £2,000,000 and the selling price of £2,500,000 represents a profit on the sale so this £500,000 profit on the transaction is reflected as an increase in retained earnings.
9. The transfer of cash to settle the obligation to short-term borrowings results in a decrease in short-term borrowings of £200,000 to reflect the settlement of the obligation. As the amounts owed were paid in cash, cash also falls by the same amount to reflect the transfer of economic benefits to settle the obligations to short-term borrowings.