

## PRINCIPLES OF ACCOUNTS

### ADVANCED LEVEL

#### OBJECTIVES

The examination aims to test the candidates' abilities to:

1. demonstrate knowledge of accounting procedures and practices and an understanding of accounting principles on which they are based;
2. apply such knowledge and understanding to familiar and novel situations;
3. analyse data and present information in an appropriate accounting form; and
4. evaluate a given scenario with reasoned explanations and make recommendations based on accounting information and principles.

#### THE EXAMINATION

The examination will consist of two papers of three hours each. Each paper will have two sections: Section A consisting of two compulsory questions of 30 marks each, and Section B a choice of two out of three questions of 20 marks each. The content of the syllabus will be tested on both papers.

#### THE SYLLABUS

Candidates are encouraged to keep abreast of the latest accounting developments in Hong Kong. Any accounting definition or practice made obsolete by a new or revised standard effective for annual periods beginning before 1 January 2009 will not be accepted in the examination.

##### *Syllabus*

##### *Explanatory Notes*

#### **I. THE ACCOUNTING SYSTEM**

1. Purposes of financial reporting
  - (a) Users and their information needs
  - (b) An introduction to the regulatory framework of accounting

*Syllabus**Explanatory Notes*

- |    |                                    |  |
|----|------------------------------------|--|
| 2. | Accounting principles and concepts | (c) Uses and limitations of conventional financial statements  |
|    |                                    | (a) Meanings and implications of ‘true and fair view’ and ‘substance over form’  |
|    |                                    | (b) Meaning, importance, functions and shortcomings of:<br>entity, going concern, stable monetary unit, historical cost, accrual,<br>prudence, consistency, objectivity, timeliness, materiality, uniformity,<br>relevance, disclosure |
| 3. | Books of accounts and records      | (a) Double-entry book-keeping  |
|    |                                    | (b) Books of original entries  |
|    |                                    | (c) Ledgers and their classifications  |
|    |                                    | (d) Information technology applications in accounting systems  |
| 4. | Control systems                    | (a) Trial balance  |
|    |                                    | (b) Control accounts and their reconciliation with personal ledgers  |
|    |                                    | (c) Bank reconciliation statement  |
|    |                                    | (d) Types of errors and their correction   |

**II. FINANCIAL ACCOUNTING**

1. Preparation of final accounts for the following types of business:
  - sole proprietorship
  - partnership
  - limited companies
  - non-trading organisations

*Syllabus**Explanatory Notes*

- |    |   |   |
|----|---|---|
| 2. | Balancing day adjustments relating to the preparation of final accounts | <ul style="list-style-type: none"> <li>(a) Prepayments and accruals for revenue and expenses</li> <li>(b) Allowance for doubtful debts</li> <li>(c) Depreciation               <ul style="list-style-type: none"> <li>(i) Causes</li> <li>(ii) Methods:   Straight-line<br/>                  Reducing-balance<br/>                  Sum-of-the-years-digits<br/>                  Units of production</li> <li>(iii) Disposal of property, plant and equipment</li> </ul> </li> </ul>  |
| 3. | Accounting for changes in partnership                                   | <ul style="list-style-type: none"> <li>(a) Valuation and accounting treatments of goodwill</li> <li>(b) Admission and/or retirement of partner(s)</li> <li>(c) Dissolution of partnership (Piecemeal realisation is not required)</li> </ul>  |
| 4. | Accounting for limited liability company                                | <ul style="list-style-type: none"> <li>(a) Types and raising of capital<br/>(Issues payable by instalments and forfeiture of shares are excluded)</li> <li>(b) Limited company taking over a sole proprietorship or a partnership<br/>(Pre-incorporation profit is not required)</li> <li>(c) Consolidated accounts (one subsidiary and acquisition method only)               <ul style="list-style-type: none"> <li>▪ minority interest</li> <li>▪ goodwill arising on consolidation (including the basic accounting treatment of subsequent impairment)</li> <li>▪ pre-acquisition and post-acquisition profits</li> <li>▪ inter-company transactions: trading of goods, property, plant and equipment; borrowing; dividend received/receivable; remittances<br/>(Accounting treatment for preference shareholding in subsidiary is not required)</li> </ul> </li> <li>(d) Published accounts (Interpretation and explanation only)</li> </ul> |

*Syllabus**Explanatory Notes*

5. Preparation of financial statements from incomplete records

**III. ANALYSIS AND INTERPRETATION OF FINANCIAL STATEMENTS**

1. Cash flow statement
  - (a) Functions
  - (b) Preparation of statement and notes  
(Consolidated cash flow statement is not required)
2. Ratio analysis
  - (a) Calculation of accounting ratios
  - (b) Uses and limitations of ratio analysis
3. Evaluation of profitability, liquidity, management efficiency, investment return, and financial stability

**IV. AN INTRODUCTION TO MANAGERIAL ACCOUNTING**

1. Costing principles and systems
  - (a) Introducing managerial accounting  
(Entries for interlocking cost accounting system are not required)
  - (b) Costing for materials, labour and overheads
  - (c) Preparation of manufacturing account
  - (d) Costing systems: job costing, process costing, and activity-based costing  
(Costing of normal and abnormal losses is required but costing of by-products and waste products is excluded)
  - (e) Marginal costing Vs absorption costing
  - (f) Cost-volume-profit (CVP) analysis (marginal costing only)

*Syllabus**Explanatory Notes*

- |                             |                      |   |
|-----------------------------|----------------------|---|
| 2.                          | Standard costing     | <ul style="list-style-type: none"> <li>(a) Establishing cost standards</li> <li>(b) Preparation of trading and profit and loss account under standard costing system (including treatment of variances)</li> <li>(c) Variance analysis               <ul style="list-style-type: none"> <li>i. Sales - sales price variance and sales volume variance</li> <li>ii. Direct materials - material price variance and material usage variance</li> <li>iii. Direct labour - wage rate variance and labour efficiency variance</li> </ul>               (Analysis of overhead variance and calculation of sales mix and material mix variances are excluded)             </li> </ul> |
| 3.                          | Budgeting            | <ul style="list-style-type: none"> <li>(a) Advantages and uses</li> <li>(b) Fixed Vs flexible budgets</li> <li>(c) Factors to consider in setting and revising budgets</li> <li>(d) Cash budgets</li> <li>(e) Budgeted profit and loss accounts and balance sheets</li> </ul>   |
| 4.                          | Investment appraisal | <ul style="list-style-type: none"> <li>(a) Financial factors affecting investment decisions               <ul style="list-style-type: none"> <li>– ascertainment of future cash flows, payback, and accounting rate of return</li> <li>– net present value and internal rate of return (Calculation of IRR is not required)</li> </ul> </li> <li>(b) Non-financial factors affecting investment decisions</li> </ul>  |
| <b>V. ACCOUNTING THEORY</b> |                      |   |
| 1.                          | Income determination | <ul style="list-style-type: none"> <li>(a) Concepts of revenue and its recognition</li> </ul>   |

*Syllabus**Explanatory Notes*

- |    |  |  |
|----|--|--|
| 2. | Valuation of property, plant and equipment | (b) Concepts of expenses and its measurement<br>(c) Prior-period adjustments   |
| 3. | Valuation of intangible assets             | (a) Distinction between capital and revenue expenditure<br>(b) Valuation concepts and methods: historical cost Vs fair value<br>(Impairment of property, plant and equipment is excluded.)<br>(c) Concepts, reasons and methods of depreciation<br>(d) Accounting for leases (lessee only) |
| 4. | Valuation of inventories                   | (a) Nature and characteristics of intangible assets such as patents, copyrights, franchises, research and development costs, trademark, etc.<br>(b) Valuation concepts and methods<br>(c) Accounting treatment   |
|    |  | (a) Periodic Vs perpetual inventory system<br>(b) Inventory valuation methods (based on historical cost valuation)<br>— specific identification<br>— average cost<br>— first in, first out<br>— last in, first out<br>(c) The lower of cost and net realisable value                       |