

Statement of financial position

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Read first: **Business finance: needs and sources**, **Cash-flow forecasting and working capital**

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What you need to know

By the end of this topic you should be able to:

1. **The main parts of a statement of financial position.** Know what assets, liabilities and equity are, and sort assets and liabilities into their main groups: non-current assets, current assets, current liabilities and non-current liabilities, with examples of each.
2. **Read a simple statement of financial position and make deductions from it.** Use the figures to say what the business owns, how it is financing its activities (owners' money, long-term borrowing or short-term debts), whether it can pay its short-term debts, how things have changed from one year to the next, and how it could raise finance from what it already has, such as by selling inventory.

You will **not** be asked to draw up a statement of financial position. You will be asked to define its terms, classify items, use figures from an extract, and explain what they tell a manager, owner or lender.

Understand it

What a statement of financial position is

A **statement of financial position** is a financial statement that shows the value of a business's assets, liabilities and equity at one particular date. Its old name is the **balance sheet**, and you may still see that name in older books.

The words "at one particular date" matter. An income statement covers a period, usually a year. A statement of financial position is a snapshot of what the business owns and owes on one day, such as 31 December 2025; a day later the figures are different.

It answers three questions:

- **What does the business own?** Its assets.
- **What does it owe to people outside the business?** Its liabilities.
- **How much belongs to the owners?** Its equity: what is left of the assets once all the debts are paid.

Assets: what the business owns

An **asset** is an item of value that the business owns. Assets are split by how long the business expects to keep them.

Non-current assets are items of value owned by the business that it expects to keep and use for more than one year. They are the things the business works with, not things it sells:

- land and buildings: a factory, shops, offices, a warehouse;
- machinery and equipment: ovens, computers, tools;
- vehicles: delivery vans, lorries, company cars, fishing boats, buses;
- fixtures and fittings: shelving, counters, display cabinets;
- shares the business owns in another business (investments).

Current assets are items of value owned by the business that it expects to turn into cash or use up within one year. They move round all the time as the business trades:

- **inventory**: raw materials, unfinished goods and finished goods waiting to be sold;
- **trade receivables**: money owed **to** the business by customers who bought on credit and have not yet paid;
- **cash**: cash in the till and money in the bank account.

The same kind of item can be in different groups in different businesses. A car is a non-current asset for a plumber who drives it to jobs, but inventory (a current asset) for a car showroom that is trying to sell it. Ask: **will the business keep it and use it for years, or turn it into cash soon?**

Liabilities: what the business owes

A **liability** is a debt the business owes to someone outside it. Liabilities are split by when they must be repaid.

Current liabilities are debts the business owes that must be repaid within one year:

- **trade payables**: money the business owes **to** its suppliers for goods bought on credit;
- **bank overdraft**: money taken out of the bank account beyond what was in it;
- **short-term loans** repayable within the year;
- tax that is owed but not yet paid.

Non-current liabilities are debts the business owes that are repaid over more than one year:

- **long-term bank loans**, for example a five-year loan for new machinery;
- **mortgages** on land or buildings;
- **debentures** (long-term loans to a company from investors).

Two pairs are easy to mix up. **Trade receivables** are owed **to** the business, so they are an asset; **trade payables** are owed **by** the business, so they are a liability. And an **overdraft** is a current liability even though it is "money in the bank": the business owes it to the bank and can be asked to repay it at short notice.

Equity: what the owners have put in

Equity is the money put into the business by its owners plus the profit it has kept (retained profit); it equals total assets minus total liabilities. In a limited company it is called **shareholders' equity** or shareholders' funds: the money raised by selling shares (share capital) plus the profits kept in the business (reserves). For a sole trader or partnership it is called the owner's or partners' **capital**.

Equity is not cash in a drawer. It tells you how much of the assets were paid for by the owners rather than by lenders and suppliers: if the business sold every asset and paid every debt, the owners would get what is left. Dividends are something different: they are the share of a company's profit paid **out** to its shareholders, which reduces the profit kept in the business.

Why it balances

Everything a business owns had to be paid for in one of two ways: with money from its owners, or with money it still owes to others. So the two sides are always equal:

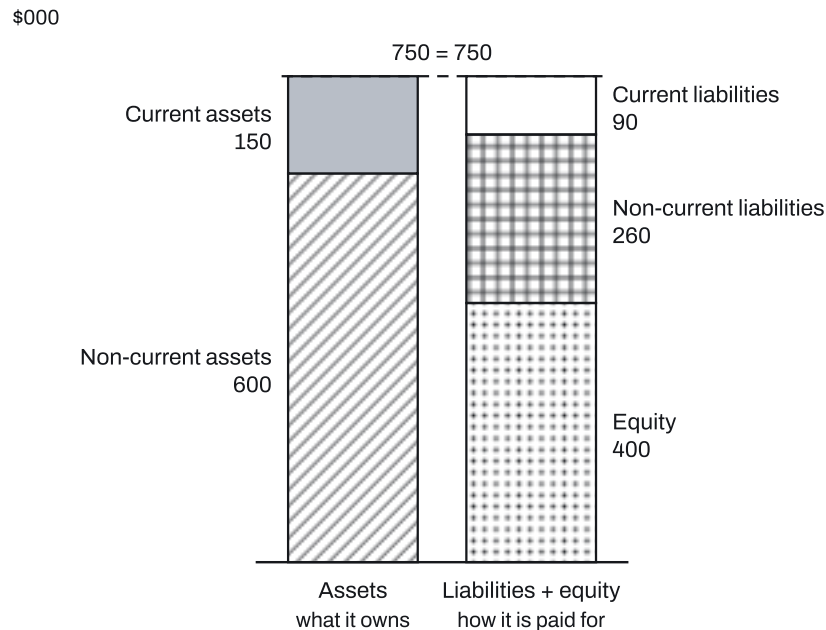
total assets = total liabilities + equity

and therefore

equity = total assets – total liabilities.

Here is a simple statement for a furniture maker that is a private limited company.

Furniture company, statement of financial position at 31 December 2025	\$000
Non-current assets: factory building 400, machinery 150, delivery vans 50	600
Current assets: inventory 70, trade receivables 50, cash 30	150
Total assets	750
Current liabilities: trade payables 55, overdraft 35	90
Non-current liabilities: bank loan repayable over 8 years	260
Total liabilities	350
Equity: share capital 250, retained profit 150	400
Total liabilities + equity	750



The left bar shows what the company owns; the right bar shows where the money for it came from. They are the same height because every dollar of assets was paid for either by the owners or by someone the company still owes. Check: $750 = 350 + 400$.

What you can deduce from it

Reading the statement means turning figures into sentences about the business. For the furniture company:

- **What it owns.** Most of its assets are non-current: 600 of 750 thousand dollars, mainly the factory. That is normal for a manufacturer.
- **How it finances its activities.** Of the \$750 000 of assets, \$400 000 was paid for by the owners (equity), \$260 000 by a long-term bank loan and \$90 000 by short-term debts. More than half comes from the owners, so the company is not heavily reliant on borrowing, but it does have a large loan to repay over the next 8 years, with interest each year.
- **Whether it can pay its short-term debts.** Compare current assets with current liabilities. Here current assets of \$150 000 are bigger than current liabilities of \$90 000, so **working capital** = $150 - 90 = 60$ thousand dollars. When current liabilities are bigger than current assets, working capital is negative and the business may struggle to pay its suppliers and bank on time. (The current ratio, current assets ÷ current liabilities, compares the same two figures; here $150 \div 90 = 1.67$. Ratios are covered in "Analysis of accounts".)
- **How things have changed.** One statement on its own says little about direction. Put two years side by side and ask: which lines grew, which fell, and how was any new asset paid for? Example 2 does this.

Always quote the figures: "non-current liabilities rose from \$40 million to \$60 million", not "it has a lot of debt".

Raising finance from what the business already has

The statement also shows where a business could find money without borrowing more or selling more shares:

- **Sell some inventory.** A shop holding more stock than it needs can sell off the extra, or simply buy less for a while. Inventory turns into cash. Total current assets do not change at that moment (inventory down, cash up by the same amount if sold at cost), but the business now has cash it can spend.
- **Collect trade receivables faster.** Asking customers who owe money to pay sooner turns receivables into cash.
- **Sell non-current assets** it no longer needs, such as a spare van or an unused building. This can raise a large sum, but the asset is gone if it is needed later.

The statement shows which of these internal sources (see "Business finance") are possible and how big they could be.

How transactions change the statement

Because it always balances, every transaction changes at least two figures. A few worth knowing:

Transaction	What changes	Working capital
Takes out a 5-year bank loan and spends it on a machine	non-current liabilities up; non-current assets up by the same amount	no change
Sells inventory at cost for cash	inventory down, cash up: current assets the same	no change
Uses cash to pay off part of the overdraft or pay a supplier	current assets down; current liabilities down by the same amount	no change
Uses cash to buy a non-current asset (a new van)	current assets down; non-current assets up	falls
Buys inventory on credit	inventory up; trade payables up	no change
Owners buy new shares and the cash is kept	cash up; equity up	rises

The rule behind the last column: working capital changes only when a transaction has a current item on one side and a non-current item or equity on the other.

Who uses it, and for what

Managers, owners and outsiders all read the statement of financial position, for different reasons. The ways it can be used:

- to show **what the business owns** (the value of its assets);
- to show **what it owes** (the value of its liabilities);

- to show **how it finances its activities**: how much from owners, from long-term loans, from short-term debts;
- to show **what the business is worth** (its equity);
- to calculate **working capital** and liquidity ratios such as the current ratio, to judge whether it can pay its short-term debts;
- to **support a loan application** or attract investors: a bank wants to see what the business already owes and which assets could be used as security;
- to **compare** with earlier years, or with competitors.

The statements a company publishes

A public limited company must publish its accounts every year. The main financial statements in them are the **income statement**, the **statement of financial position**, the **statement of cash flows** and the **statement of changes in equity**. A cash-flow forecast is a plan for the future used inside the business, not a published statement. Profit, revenue or assets are items **in** a statement, not statements themselves.

Key facts and formulas

This topic has no formula list in the exam. "Learn it" means you must remember it.

Fact or formula	Status
Statement of financial position: a financial statement that shows the value of a business's assets, liabilities and equity at one particular date	Learn it
Non-current assets: items of value owned by the business that it expects to keep and use for more than one year (land, buildings, machinery, vehicles, fixtures)	Learn it
Current assets: items of value owned by the business that it expects to turn into cash or use up within one year (inventory, trade receivables, cash)	Learn it
Current liabilities: debts the business owes that must be repaid within one year (trade payables, overdraft, short-term loans)	Learn it
Non-current liabilities: debts the business owes that are repaid over more than one year (long-term bank loans, mortgages, debentures)	Learn it
Equity: the money put into the business by its owners plus the profit it has kept (retained profit); it equals total assets minus total liabilities	Learn it
Total assets = non-current assets + current assets	Learn it
Total liabilities = current liabilities + non-current liabilities	Learn it
Total assets = total liabilities + equity	Learn it

Fact or formula	Status
Equity = total assets – total liabilities	Learn it
Working capital = current assets – current liabilities	Learn it
Current ratio = current assets ÷ current liabilities	Learn it

How to do it

We have tagged 10 questions on this topic (2022–2025), all 20-mark structured questions on Paper 1. Five of them have parts of more than one type, so the counts add to 16.

Question type	Questions
Define a statement of financial position term	6
Identify examples of assets or liabilities	2
Classify items as current asset or current liability	2
Outline or identify uses of a statement of financial position	2
Explain how liabilities or a high level of debt affect a business	2
Calculate a total from listed items	1
Identify the financial statements a company must publish	1

The mark scheme codes are **k** (knowledge: a correct point), **app** (application: a detail from the case), **an** (analysis: a developed consequence) and **eval** (evaluation: a justified judgement).

Part	Marks	What earns them
"Define"	2	a full definition; a partial one gets 1
"Identify" or "State"	1 each	a correct item; only the first answers asked for are marked
"Calculate"	2	the right answer with units; the right method with a wrong answer gets 1
"Outline"	4	each point: k + app
"Explain"	6	each point: k + app + an
(e) "Do you think ...?"	6	2 k + 2 an + 2 eval; a general question, so no app

1. Define a statement of financial position term (6 questions)

A 2-mark part (a) or (b). Each definition has **two ideas**, and you need both for 2 marks:

Term	Idea 1	Idea 2
Non-current assets	owned by the business	kept for more than one year
Current assets	owned by the business	turned into cash or used up within one year
Current liabilities	debts the business owes	repaid within one year
Statement of financial position	shows assets, liabilities and equity	at one particular date
Equity	money put in by the owners plus retained profit	equals total assets minus total liabilities

1. **Write the definition in one sentence** that contains both ideas, using the wording in "Key facts and formulas".
2. **Say "one year" or "12 months"**, never just "short-term" or "a short time".
3. **Don't give examples instead of a definition.** An example can follow, but it earns nothing on its own.

Variations you will meet:

- **Define "non-current assets"** (0450/12/O/N/24 Q3, part (a)): the mark scheme required both "owned by the business" and "for more than one year" for 2 marks; either idea alone earned 1.
- **Define "current liabilities"** (0450/13/O/N/23 Q2, part (a); 0450/12/M/J/22 Q1, part (a)): debts repaid within a year, or before the date of the next statement of financial position, for 2; "money owed by a business" was partial (1). Lesson: name the time limit (12 months), because "short-term" alone is too loose, and keep it apart from non-current liabilities and current assets.
- **Define "current assets"** (0450/12/M/J/23 Q4, part (b)): owned by the business **and** used or turned into cash within one year (or before the next statement of financial position) for 2; "in the business for less than a year" or "assets owned" alone was partial (1). Lesson: put both ideas in one sentence, give the time as one year, and remember an asset is owned, never owed.
- **Define "statement of financial position"** (0450/12/O/N/22 Q1, part (b)): assets and liabilities (or assets, liabilities and equity) **at a particular date** for 2; "what a business owns and owes" or "shows assets and liabilities" was partial (1). Lesson: the date is what lifts 1 mark to 2; it is the balance sheet under its newer name, not an income statement or cash-flow forecast.
- **Define "shareholders' equity"** (0450/11/M/J/22 Q3, part (a)): any of money invested by the company's owners, share capital plus reserves, or total assets minus total liabilities earned 2; "money raised from selling shares" was partial (1). Lesson: equity is the owners' stake, while dividends are profit paid out to them.

2. Identify examples of assets or liabilities (2 questions)

1 mark per item; only the first answers asked for are marked.

1. **Check which group is asked for:** non-current asset, current asset, current liability or non-current liability.

2. **Give a single, specific item:** "machinery", "delivery vans", "overdraft". Not "money" or "things the business owns".
3. **When two of the same group are asked for, make them clearly different.** "Factory" and "building" are too close; "factory" and "delivery vans" are not.

Variations you will meet:

- **One non-current asset and one current liability for an electrical goods retailer (0450/11/O/N/25 Q2, part (b)):** accepted non-current assets included machinery, equipment, land, buildings or shops, and vehicles; accepted current liabilities were an overdraft, a short-term loan or trade payables.
- **Two examples of non-current assets for a garden products business (0450/12/M/J/22 Q1, part (b)):** land or buildings, machinery or equipment, fixtures and fittings, vehicles, or investments in another business. Lesson: stick to items kept for years (not inventory or cash), and make the two clearly different.

3. Classify items as current asset or current liability (2 questions)

A 4-mark "State whether each of the following ..." with four items, 1 mark each.

1. For each item ask: **does the business own it, or owe it?** Owns: asset. Owes: liability.
2. Then ask: **within one year?** Everything in these questions is current; the trap is direction (to or from the business), not time.

Receivables, inventory and cash are current assets; payables and an overdraft are current liabilities.

Variations you will meet:

- **Trade receivables, trade payables, overdraft and inventory (0450/12/O/N/24 Q3, part (c)):** receivables and inventory are current assets; payables and the overdraft are current liabilities.
- **Overdraft, trade receivables, trade payables and cash in bank (0450/11/M/J/22 Q3, part (c)):** the same idea with cash instead of inventory.

4. Outline or identify uses of a statement of financial position (2 questions)

"Identify four ways" (1 each, no case): list four different uses from "Who uses it, and for what". Make each one a different idea: "calculate working capital" and "calculate the current ratio" are both credited, but "see what it owes" and "see its debts" are the same point.

"Outline two ways the information might be useful" (k + app each), with an extract:

1. **Pick a use** (k): shows what it owns; shows what it owes; shows how it is financed; shows its value (equity); calculate working capital or the current ratio; support a loan application; compare over time or with competitors.
2. **Back it with a figure** (app) worked out from the extract, using a different one for each way. With non-current assets, current assets, current liabilities and non-current liabilities given, you can work out total assets (NCA + CA), working capital (CA – CL), the current ratio (CA ÷ CL), total liabilities (CL + NCL) and equity (total assets – total liabilities).

For a removal company with an extract (\$000) of non-current assets 340, current assets 45, current liabilities 60 and non-current liabilities 150: "It can be used to calculate working capital (k), which is $45 - 60 = -15$, so $-\$15\,000$ (app)." "It shows the value of what the business owns (k): total assets of $340 + 45 = 385$, that is $\$385\,000$ (app)."

Variations you will meet:

- **Outline two ways an extract is useful to an electrical goods retailer (0450/11/O/N/25 Q2, part (c)):** the extract (\$ million) was non-current assets 120, current assets 70, current liabilities 110 and non-current liabilities 75. Figures the mark scheme accepted as application included total assets \$190 million, current liabilities \$110 million, working capital $-\$40$ million, a current ratio of 0.63:1 or 0.64:1 and equity of \$5 million, as well as the 10 vehicles it needs finance for. "Assess liquidity" was credited when no specific ratio was named.
- **Identify four ways the information can be used, for a clothing retailer (0450/13/O/N/24 Q4, part (c)):** credited ways were calculating working capital, the current ratio or the acid test ratio; showing how activities are financed; showing what it owns; showing what it owes; supporting a loan application; showing what the business is worth; and comparing over time or with competitors.

5. Explain how liabilities or a high level of debt affect a business (2 questions)

A 6-mark "Explain two ways / problems" part: for each, k + app + an.

1. Pick two different effects (k):

- **interest:** more borrowing means more interest each year, which raises expenses and cash outflows;
- **harder to borrow more:** lenders worry whether the business can repay, so they may refuse, charge more, or ask for more security (collateral);
- **repayment and risk:** more debt has to be repaid, so the risk of not being able to pay rises, which can lead to cash-flow and liquidity problems and, at worst, closure.

2. Apply each (app) with a different case detail: the figure for the loan or liabilities, the type of business, what it is trying to do.

3. Develop each (an): say what happens next because of it. Interest is a cash payment, so "less cash for paying suppliers"; refusal of a loan means "it cannot buy the new equipment it needs to grow".

Example for a ferry operator whose long-term loans rose to \$80 million: "It must pay interest (k) on the \$80 million of loans (app), which raises its expenses and cash outflows every year, leaving less cash for running costs such as fuel (an)."

Answer the question asked: the **effects** of the debt. Reasons why the business borrowed, or how it could reduce its debt, earn nothing here.

Variations you will meet:

- **Two ways an increase in non-current liabilities might affect a multinational clothing maker (0450/11/M/J/24 Q3, part (d)):** its non-current liabilities rose from \$300 million to \$400 million. The mark scheme credited paying interest on the \$400 million, which increases expenses or cash outflows; finding it

harder to raise more finance, or needing more collateral, because lenders worry about repayment; and having more debt to repay, which increases financial risk.

- **Two problems of a high level of debt for a fishing business (0450/13/O/N/22 Q1, part (d)):** its extract showed a \$200 000 bank loan and a \$20 000 overdraft. The mark scheme credited difficulty arranging more finance (so it may not be able to expand), high interest on the bank loan increasing expenses and cash outflows, struggling to meet repayments and so liquidity problems, and higher financial risk so the bank may not lend more. Lesson: stick to effects, quote the loan figure, and carry each effect on to what it does to the business.

6. Calculate a total from listed items (1 question)

A 2-mark "Calculate the value of ... Show your working."

1. **Sort every item** into its group before adding anything. Cross out what does not belong: assets when liabilities are asked for, long-term items when current ones are asked for.
2. **Write the working:** the items, the sum, then the answer.
3. **Give the units** of the table: if it says \$000, 35 means \$35 000.

For a printer listing trade receivables 12, inventory 18, trade payables 25, bank overdraft 9 and a 5-year bank loan 70 (\$000): current liabilities = $25 + 9 = 34$, so **\$34 000**. The loan is non-current; receivables and inventory are assets.

Variation you will meet:

- **Current liabilities of a fishing business (0450/13/O/N/22 Q1, part (b)):** from trade payables 60, trade receivables 50, overdraft 20 and bank loan 200 (\$000), the answer was trade payables + overdraft = \$80 000 for 2 marks; the right method with a wrong answer earned 1. Lesson: leave the bank loan out, and always write the working.

7. Identify the financial statements a company must publish (1 question)

A 2-mark "Identify two ...", 1 mark each, first two answers only.

- Give two of: **income statement, statement of financial position, statement of cash flows, statement of changes in equity**. Older names (profit and loss account, balance sheet) were also accepted.

Variation you will meet:

- **Two statements a public limited company must publish each year (0450/11/M/J/22 Q3, part (b)):** any two of the four above; a cash-flow forecast was not accepted. Lesson: name whole statements, not lines inside one.

Worked examples

Example 1

Lim and Ortiz run a dental practice as a partnership. These are some of its balances at 30 June 2025.

Item	\$
Dental chairs and equipment	180 000
Car used for home visits	25 000
Dental supplies in store	8 000
Money owed by patients' insurance companies	15 000
Cash in bank	12 000
Money owed to suppliers	9 000
Bank overdraft	6 000
Bank loan repayable over 6 years	90 000

(a) Define "non-current liabilities". **[2]**

(b) Sort the eight items into non-current assets, current assets, current liabilities and non-current liabilities, and give the total of each group. **[4]**

(c) Calculate the partners' capital (equity). Show your working. **[2]**

(a) Debts the business owes (1) that are repaid over more than one year (1).

(b) Non-current assets: equipment and car, $180\,000 + 25\,000 = 205\,000$ dollars (1).

Current assets: dental supplies (inventory), money owed by insurers (trade receivables) and cash, $8\,000 + 15\,000 + 12\,000 = 35\,000$ dollars (1).

Current liabilities: money owed to suppliers (trade payables) and the overdraft, $9\,000 + 6\,000 = 15\,000$ dollars (1).

Non-current liabilities: the 6-year bank loan, \$90 000 (1).

(c) Total assets = $205\,000 + 35\,000 = 240\,000$; total liabilities = $15\,000 + 90\,000 = 105\,000$. Equity = total assets – total liabilities (1) = $240\,000 - 105\,000 = 135\,000$ dollars (1).

Part (a) earns 2 for both ideas; part (b) 1 per correct group with its total; part (c) 1 for the method and 1 for the answer. Total 8 marks. The money owed by insurers is a trade receivable, owed **to** the practice, so it is an asset even though the word "owed" appears.

Example 2

A bus company is a public limited company. During 2025 it bought a fleet of new electric buses. An extract from its statements of financial position is shown (\$ million).

	2024	2025
Non-current assets	90	125
Current assets	30	25
Current liabilities	20	30
Non-current liabilities	40	60
Equity	60	60

(a) Calculate how much the company's total assets rose from 2024 to 2025, and show where the money for the rise came from. [3]

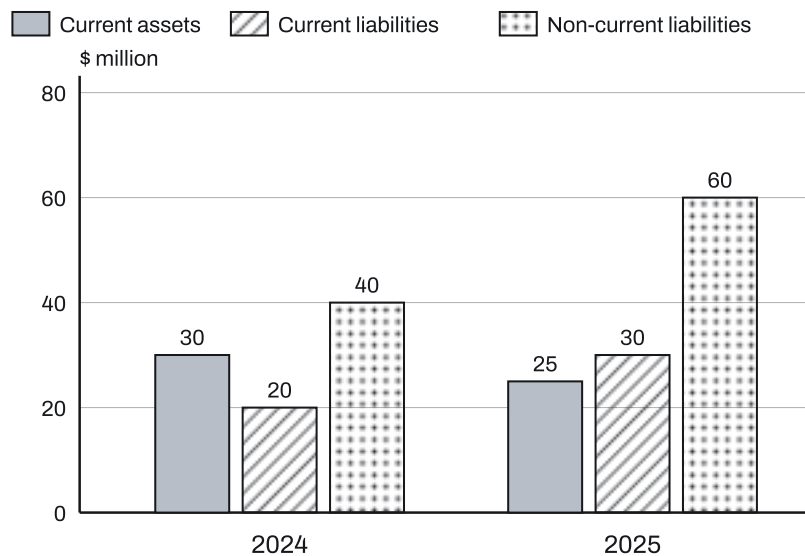
(b) Explain two deductions the directors could make from the changes between 2024 and 2025. [6]

(a) Total assets were $90 + 30 = 120$ in 2024 and $125 + 25 = 150$ in 2025, so they rose by $150 - 120 = 30$, that is \$30 million (1). Current liabilities rose by $30 - 20 = 10$ and non-current liabilities by $60 - 40 = 20$ million dollars (1). Equity did not change, so the whole rise was financed by liabilities: $10 + 20 + 0 = 30$ million dollars (1).

(b) Deduction 1: the new buses were paid for mainly by borrowing (k). Non-current assets rose by $125 - 90 = 35$ million dollars, while non-current liabilities rose by $60 - 40 = 20$ million dollars and equity did not change at all (app). So the shareholders put in no new money, and the company now has \$20 million more in long-term loans to repay, with interest every year that adds to its expenses and cash outflows (an).

Deduction 2: its liquidity has become worse (k). Current liabilities of \$30 million are now bigger than current assets of \$25 million, so working capital has fallen from $30 - 20 = 10$ million dollars to $25 - 30 = -5$ million dollars (app). If its short-term debts all fell due, it could not pay them from its current assets, so it may have to delay paying suppliers, which could damage its credit reputation and make suppliers less willing to offer credit (an).

Part (a) earns 1 for the rise in total assets, 1 for the changes in liabilities and 1 for showing they add up (3); part (b) earns k + app + an for each deduction ($3 + 3 = 6$). Total 9 marks.



Working capital: \$10 million in 2024, −\$5 million in 2025

The chart shows the change: in 2025 the striped bar (current liabilities) is taller than the solid bar (current assets), and the dotted bar (long-term debt) has grown by half. The \$35 million of extra non-current assets was financed by \$20 million more long-term loans, \$10 million more current liabilities and \$5 million less in current assets. Total assets rose from \$120 million to \$150 million, and so did total liabilities plus equity.

Example 3

A gym is a private limited company. An extract from its statement of financial position at 31 March 2025 is shown (\$000).

	\$000
Non-current assets	820
Current assets (inventory 15, trade receivables 5, cash 60)	80
Current liabilities (trade payables 40, overdraft 30)	70
Non-current liabilities (bank loan)	300
Equity	530

(a) The gym takes out a 5-year bank loan of \$200 000 and spends all of it on new exercise machines. State how this changes the gym's non-current assets, non-current liabilities and working capital. [3]

(b) Instead, the gym sells \$10 000 of its inventory of sports drinks at cost and uses the cash to repay \$10 000 of its overdraft. Calculate the new current assets, current liabilities and working capital. [3]

(c) Outline two deductions about how the gym finances its activities, using the original figures. [4]

(a) Non-current assets rise by \$200 000, from \$820 000 to \$1 020 000 (1). Non-current liabilities rise by \$200 000, from \$300 000 to \$500 000 (1). Working capital stays at $80 - 70 = 10$ thousand dollars, because no current asset or current liability changed (1).

(b) Current assets: inventory falls by 10 and cash rises by 10, then cash falls by 10 to repay the overdraft, so current assets = $80 - 10 = 70$, that is \$70 000 (1). Current liabilities = $70 - 10 = 60$, that is \$60 000 (1). Working capital = $70 - 60 = 10$, that is \$10 000: unchanged, because both sides fell by the same amount (1).

(c) Most of its assets are paid for by its owners (k): equity of \$530 000 out of total assets of $820 + 80 = 900$ thousand dollars, more than half (app).

It uses long-term borrowing to pay for its non-current assets (k): a bank loan of \$300 000 helps pay for the \$820 000 of equipment and premises (app).

Part (a) earns 1 per change (3); part (b) 1 per figure (3); part (c) k + app for each deduction ($2 + 2 = 4$). Total 10 marks. Check (a): total assets become \$1 100 000 and total liabilities plus equity become $70 + 500 + 530 = 1100$ thousand dollars, so the statement still balances.

Example 4

Do you think a business with a large amount of non-current liabilities is always in a weak financial position? Justify your answer. [6]

Large non-current liabilities mean large interest payments (k). Interest must be paid every year whether or not the business is doing well, so it raises expenses and cash outflows, and in a bad year it could leave too little cash to pay suppliers and staff (an).

Long-term loans can pay for non-current assets that earn money for many years (k). A loan for new machinery is repaid in instalments over the years the machinery is used, and the owners keep full control because lenders do not get a share of the business, unlike when new shares are sold (an).

No, it is not always weak: what matters is what the borrowing paid for and whether the business can afford the repayments, so a business whose loans bought productive assets and whose current assets cover its current liabilities can be strong (eval). It is weak when the debt is large compared with what the owners have put in and working capital is negative, because then lenders may refuse more finance and one bad year could leave it unable to repay (eval).

This is a general question, so there are no marks for application: $2\text{ k} + 2\text{ an} + 2\text{ eval} = 6$.

Common mistakes

- **Writing "short-term" or "a short period" instead of "within one year".** Current means within 12 months; non-current means more than 12 months.
- **Giving only half a definition.** Non-current assets need **owned** and **more than one year**; current assets need **owned** and **within one year**.
- **Leaving out "at a particular date"** when defining a statement of financial position. Without it the answer gets only 1 mark.
- **Confusing the statement with others.** It is not an income statement (profit over a period) or a cash-flow forecast (planned cash in and out). It is the new name for the balance sheet.

- **Confusing equity with dividends.** Equity is the owners' stake in the business; dividends are profit paid out to shareholders.
- **Mixing up assets and liabilities.** Assets are owned; liabilities are owed. Saying assets are "owed to others" is wrong, and so is calling a current asset a current liability. Trade **receivables** are owed **to** the business (asset); trade **payables** are owed **by** it (liability).
- **Giving current assets when non-current assets are asked for**, such as inventory or cash. Two near-identical answers count once.
- **Including the long-term loan in current liabilities.** Sort each item first.
- **Repeating the word in the definition** ("current assets are assets that are current") or giving examples instead of a definition. Neither defines anything.
- **Naming an item instead of a statement**, such as "profit" or "revenue" when asked for a financial statement. They earn nothing.
- **Thinking "accounts" means the bank account.** In questions about using a business's accounts, accounts means its financial statements.
- **Explaining why a business has debt, or how to cut it, when asked for the effects.** Neither answers the question.
- **Saying profit is used to pay interest.** Interest is an expense paid in cash, and it must be paid whether or not the business makes a profit.
- **No figures in application.** Quote the table: "current liabilities of \$110 million", not "it has debts". Each figure you quote can be an application mark.
- **Leaving out the units.** If the table is in \$000 or \$ million, the answer must say so.

How to get the marks

- **Define** (2 marks): two ideas in one sentence, such as owned **and** more than one year, or assets and liabilities **at a particular date**. Say "one year" or "12 months".
- **Identify** (1 each): one clear item per line, from the right group, each clearly different. Only the first answers are marked, so don't list extras.
- **Calculate** (2 marks): write which items you are adding or subtracting, the sum, then the answer with units on the final-answer line. The working rescues 1 mark if the answer is wrong.
- **Outline** (k + app): a correct use or point, then a figure or detail from this case that fits it. Work out a figure from the extract (total assets, working capital, equity) rather than copying one line. Analysis is not needed.
- **Explain** (k + app + an): add the consequence with "so" or "which means". For debt questions the consequences are about interest and cash outflows, access to more finance, and the risk of not being able to repay.
- **Deductions** from a table: compare figures (bigger, smaller, rose, fell, by how much) and say what that tells you about the business. Copying the figures without comment earns nothing.
- **Part (e)** (6 marks): general, so no case details are needed. Develop a point on each side, then decide and say **why**, and when the answer would be different.

Quick check

1. For a farm, say whether each item is a non-current asset, current asset, current liability or non-current liability: (a) a tractor; (b) seed in store for next season's planting; (c) money a supermarket owes the farm for vegetables it has received; (d) an unpaid bill from the fuel supplier; (e) a 10-year mortgage on the farmland; (f) the farmland.
2. A student defines current liabilities as "money the business owes". Explain why this earns only 1 mark, and write a definition that earns 2.
3. A hairdresser's statement of financial position shows non-current assets \$48 000, current assets \$12 000, current liabilities \$9000 and non-current liabilities \$21 000. Calculate (a) total assets, (b) total liabilities, (c) the owner's capital and (d) working capital.
4. A gift shop has current assets of \$40 000 and current liabilities of \$32 000. (a) It sells \$5000 of inventory at cost and uses the cash to repay \$5000 of its overdraft. Calculate its new working capital. (b) Instead, it uses \$5000 of cash to buy a new display cabinet. Calculate its new working capital.
5. A printing firm asks its bank for a 5-year loan. Name two figures from its statement of financial position the bank would look at, and say what each tells the bank.

Answers

1. (a) Non-current asset. (b) Current asset (inventory). (c) Current asset (trade receivable). (d) Current liability (trade payable). (e) Non-current liability. (f) Non-current asset.
2. It says the money is owed but not when it must be repaid, so it could be a long-term loan. Full definition: debts the business owes that must be repaid within one year.
3. (a) $48\,000 + 12\,000 = 60\,000$ dollars. (b) $9\,000 + 21\,000 = 30\,000$ dollars. (c) $60\,000 - 30\,000 = 30\,000$ dollars. (d) $12\,000 - 9\,000 = 3\,000$ dollars.
4. (a) Current assets $40\,000 - 5\,000 = 35\,000$ and current liabilities $32\,000 - 5\,000 = 27\,000$, so working capital = $35\,000 - 27\,000 = 8\,000$ dollars, the same as before ($40\,000 - 32\,000 = 8\,000$). (b) Current assets fall to \$35 000 and current liabilities stay at \$32 000, so working capital = $35\,000 - 32\,000 = 3\,000$ dollars: the cash has become a non-current asset.
5. Any two: non-current liabilities, which show how much it has already borrowed long term; non-current assets, which show what it owns that could be used as security for the loan; current assets compared with current liabilities (working capital), which shows whether it can pay its short-term debts; equity, which shows how much the owners have put in themselves.

Past questions to try

- **0450/11/M/J/22 Q3**: parts (a) to (c), defining shareholders' equity, naming published statements and classifying four items.
- **0450/13/O/N/22 Q1**: parts (b) and (d), adding up current liabilities and explaining problems of high debt.
- **0450/11/O/N/25 Q2**: parts (b) and (c), naming items and outlining uses of an extract with figures.