# SOLUTION FINANCIAL REPORTING NOV 2010

**SOLUTION 1**

(a) Obra

Consolidated Income Statement for the year ended 31 December 2009

| | GHS'000 |
|---|---|
| Revenue (170,000 + (84,000 x 6/12) – 16,000 intra-group sales) | 196,000 |
| Cost of sales (w (i)) | (144,000) |
| Gross profit | 52,000 |
| Distribution costs (4,000 + (4,000 x 6/12)) | (6,000) |
| Administrative expenses (12,000 + (6,400 x 6/12)) | (15,200) |
| Finance costs (600 + (800 x 6/12)) | (1,000) |
| Profit before tax | 29,800 |
| Income tax expense (9,400 + (2,800 x 6/12)) | (10,800) |
| Profit for the year | 19,000 |
| Attributable to: | |
| Equity holders of the parent | 18,600 |
| Non-controlling interest (((6,000 x 6/12) – (1,600 URP + 400 depreciation)) x 40%) | 400 |
| | 19,000 |

(b) Consolidated Statement of Financial Position as at 31 December 2009

| | GHS'000 |
|---|---|
| Assets | |
| Non-current assets | |
| Property, plant and equipment (81,200 + 25,200 + 4,000 – 400 (w (i))) | 110,000 |
| Goodwill (w (ii)) | 9,000 |
| | 119,000 |
| Current assets (w (iii)) | 43,600 |
| Total assets | 162,600 |
| Equity and liabilities | |
| Equity attributable to owners of the parent | |
| Equity shares of GHS1 each ((20,000 + 19,200 ) w (ii)) | 39,200 |
| Retained earnings (w (iv)) | 71,400 |
| | 110,600 |
| Non-controlling interest (w (v)) | 12,200 |
| Total equity | 122,800 |
| Non-current liabilities | |
| 10% loan notes (8,000 + 6,000) | 14,000 |
| Current liabilities (16,400 + 9,400) | 25,800 |
| Total equity and liabilities | 162,600 |

Workings (figures in brackets in GHS'000

(i) Cost of sales

| | GHS'000 |
|---|---|
| Obra | 126,000 |
| Nkwa (64,000 x 6/12) | 32,000 |
| Intra-group sales | (16,000) |
| URP in inventory | 1,600 |
| Additional depreciation (2,000/5 years x 6/12) | 400 |
| | 144,000 |

The unrealised profit (URP) in inventory is calculated as (GHS16 million – GHS10.4 million) x 40/140 = GHS1,600,000.

**(ii) Goodwill in Nkwa**

| | GHS'000 | GHS'000 |
|---|---|---|
| Investment at cost | | 19,200 |
| Shares (8,000 x 60% x 2/3 x GHS6) | | |
| Less – Equity shares of Nkwa (8,000 x 60%) | (4,800) | |
| - pre-acquisition reserves (10,000 x 60% see below) | (6,000) | |
| - fair value adjustment (4,000 x 60%) | (2,400) | (13,200) |
| Parent's goodwill | | 6,000 |
| Non-controlling interest's goodwill (per question) | | 3,000 |
| Total goodwill | | 9,000 |

**The pre-acquisition reserves are**:

| | |
|---|---|
| At 31 December 2009 | 13,000 |
| Earned in the post acquisition period (6,000 x 6/12) | (3,000) |
| | 10,000 |

**Alternative calculation for goodwill in Nkwa**

| | |
|---|---|
| Investment at cost (as above) | 19,200 |
| Fair value of non-controlling interest (see below) | 11,800 |
| Cost of the controlling interest | 31,000 |
| Less fair value of net assets at acquisition (8,000 + 10,000 + 4,000) | (22,000) |
| Total goodwill | 9,000 |

**Fair value of non-controlling interest (at acquisition)**

| | |
|---|---|
| Share of fair value of net assets (22,000 x 40%) | 8,800 |
| Attributable goodwill per question | 3,000 |
| | 11,800 |

(iii) **Current assets**

| | GHS'000 | GHS'000 |
|---|---|---|
| Obra | 32,000 | |
| Nkwa | 13,200 | |
| URP in inventory | (1,600) | |
| | 43,600 | |

(iv) **Consolidated Retained Earnings**

| | |
|---|---|
| Obra per statement of financial position | 70,800 |
| Nkwa's post acquisition profit | |
| (((6,000 x 6/12) – (1,600 URP + 400 depreciation)) x 60%) | 600 |
| | 71,400 |

(v) **Non-controlling interest (in statement of financial position)**

| | |
|---|---|
| Net assets per statement of financial position | 21,000 |
| URP in inventory | (1,600) |
| Net fair value adjustment (4,000 – 400) | 3,600 |
| | 9,200 |
| 23,000 x 40% = | 3,000 |
| Share of goodwill (per question) | 12,200 |

**SOLUTION 2**

(a) Angel Ltd

| | GHS | GHS |
|---|---|---|
| Income surplus at 1 January 2005 | | 52,500 |
| Write back of “provision” plant overhaul | | 6,000 |
| | | 58,500 |
| Profit for the year to 31 December 2005 | 47,500 | |
| Add back lease rentals | 3,200 | |
| Lease interest | (800) | |
| Depreciation – Freehold (2% x 130,000) | (2,600) | |
| - Leasedhold (25% x 11,200) | (2,800) | |
| - Non-Leased Plant (110,000 x 20%) | (22,000) | |
| Loss on investment property (15,000 – 12,400) | (2,600) | |
| Write-down of stock (6,000 – 3,600) | (2,400) | |
| Unrecorded trade creditors | (500) | |
| Write back of provision for plant overhaul | 6,000 | |
| Increased in deferred tax (22,500 – 18,700) | (3,800) | |
| Loan note interest ((7,200/4)/2) | (900) | |
| Restated profit for 2005 | | 18,300 |
| Income surplus at 31 December 2009 | | 76,800 |

(b) Statement of Financial Position

| | GHS |
|---|---|
| Non-Current Assets | |
| Freehold property (126,000 – 2,600) | 123,400 |
| Plant (110,000 – 22,000) | 88,000 |
| Leased plant (11,200 – 2,800) | 8,400 |
| Investment property (15,000 – 2,600) | 12,400 |
| | 232,200 |
| Current Assets | |
| Inventory (60,400 – 2,400) | 58,000 |
| Trade debtors | 31,200 |
| Bank | 13,800 |
| Total assets | 103,000 |
| | 335,200 |
| Equity & Liabilities | |
| Equity & Surplus | |
| Ordinary share capital | 150,000 |
| Income surplus | 76,800 |
| Capital surplus | 10,000 |
| | 236,800 |
| Non-current Liabilities | |
| Deferred tax | 22,500 |
| Finance lease | 5,600 |
| 8% Loan (14,100 + 300) | 14,400 |
| | 42,500 |

| | |
|---|---|
| Current Liabilities | |
| Trade creditors (47,400 + 500) | 47,900 |
| Finance lease interest | 800 |
| Accrued loan interest | 600 |
| Finance lease obligation | 2,400 |
| Taxation | 4,200 |
| | 55,900 |
| Total equity and liabilities | 335,200 |

**SOLUTION 3**

(a) Kaba Ltd

Income Statement for the year ended 31st December 2009

| | ACCRA GHS | HOHOE GHS | TOTAL GHS |
|---|---|---|---|
| Sales | 96,000 | 36,000 | 132,000 |
| Less cost of goods sold: | | | |
| Opening stock | 7,200 | 2,400 | 9,600 |
| Add purchases | 78,000 | - | 78,000 |
| Goods received | (6,600) | 6,000 | |
| Goods available for sale | 78,600 | 8,400 | 87,000 |
| Less closing stock | 9,000 | 480 | 9,480 |
| | 69,600 | 7,920 | 77,520 |
| Gross profit | 26,400 | 28,080 | 55,260 |
| Branch adjustment a/c | 780 | - | |
| | 27,180 | 28,080 | 55,260 |
| Less expenses | - | - | |
| Rent | 2,400 | 600 | 3,000 |
| Wages | 4,800 | 840 | 5,640 |
| Sundry expenses | 2,400 | 360 | 2,760 |
| Depreciation | 1,200 | 24 | 1,224 |
| | 10,800 | 1,824 | 12,624 |
| Net profit | 16,380 | 26,256 | 42,636 |

Kaba Ltd

Statement of Financial position as at 31st December 2009

| | ACCRA | HOHOE |
|---|---|---|
| | GHS | GHS |
| Fixed assets | | 150,000 |
| Less depreciation | | 1,224 |
| | | 148,776 |
| Current Assets | | |
| Stock | 10,260 | |
| Debtors | 22,800 | |
| Bank | 84,000 | |
| | 117,060 | |
| Current Liabilities | | |
| Creditors | 24,000 | |
| | | 93,060 |
| | | 241,836 |
| Capital | | 199,200 |
| Add net profit | | 42,636 |
| | | 241,836 |

Workings

Stock Adjustment Account

| | GHS | | GHS |
|---|---|---|---|
| Profit & loss a/c | 780 | Bal b/f | 1,200 |
| Mark-up on closing stock c/f | 120 | | |
| Mark-up on goods in transit c/f | 300 | | |
| | 1,200 | | 1,200 |

Consolidated Opening Stock

| | GHS | GHS |
|---|---|---|
| Head office | | 7,200 |
| Branch | 2,400 | |
| Less profit margin (1/4 x 2,400) | 600 | |
| | | 1,800 |
| | | 9,000 |

Consolidated Closing Stock

| | GHS | GHS |
|---|---|---|
| Head office | | 9,000 |
| Branch (cost) | | 360 |
| Good in transit | 1,200 | |
| Less profit margin (¼ x 1,200) | 300 | |
| | | 900 |
| | | 10,260 |

(b) (i) Exploration and evaluation assets are expenditure for exploration and evaluation mineral resources that are recognised as assets while

Exploration and evaluation expenditures are expenditures incurred by an entity in connection with the exploration for and evaluation of mineral resources.

(ii) Initial Cost of Exploration and Evaluation Assets

| | GHS |
|---|---|
| Acquisition of rights to explore | 20,000 |
| Topographical expenses | 30,000 |
| Geochemical and Geophysical Studies | 5,000 |
| Exploratory Drilling | 4,000 |
| Trenching | 2,000 |
| Sampling | 500 |
| | 61,500 |

**SOLUTION 4**

SAND AND STONE PARTNERSHIP

REALISATION ACCOUNT

| | GHS | | GHS |
|---|---|---|---|
| Land & Buildings | 1,450,000 | Stokosis Ltd | 5,000,000 |
| Motor vehicles | 945,000 | Creditors (discount) | 50,000 |
| Fixtures | 200,000 | Capital – Stone | 315,000 |
| Plant & Machinery | 750,000 | | |
| Office equipment | 175,000 | | |
| Stocks | 345,000 | | |
| Debtors | 290,000 | | |
| Cash – Interest on loan | 20,000 | | |
| Capital – Sand | 714,000 | | |
| Capital - Stone | 476,000 | | |
| | 5,365,000 | | 5,365,000 |

BANK ACCOUNT

| | GHS | | GHS |
|---|---|---|---|
| Cash transfer | 50,000 | Balance b/d | 75,000 |
| Stokosis Ltd | 600,000 | Creditors | 150,000 |
| | | Loan - Sand | 400,000 |
| Capital - Stone | 199,000 | Capital – Sand | 224,000 |
| | 849,000 | | 849,000 |

Partnership Capital Accounts

| | Sand GHS | Stone GHS | | Sand GHS | Stone GHS |
|---|---|---|---|---|---|
| Realisation (motor) | | 315,000 | Balance b/f | 1,800,000 | 1,200,000 |
| Stokosis Ltd | | | Current a/c | 350,000 | 200,000 |
| Ordinary shares | 2,400,000 | 1,600,000 | Realisation a/c | 714,000 | 476,000 |
| 8% Debentures | 240,000 | 160,000 | | | |
| Bank a/c | 224,000 | | Bank a/c | | 199,000 |
| | 2,864,000 | 2,075,000 | | 2,864,000 | 2,075,000 |

STOKOSIS LTD

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2009

| | GHS | GHS |
|---|---|---|
| Non-Current Assets | | |
| Goodwill | | 1,160,000 |
| Land & building | | 1,450,000 |
| Plant and machinery | | 750,000 |
| Fixtures | | 200,000 |
| Office equipment | | 175,000 |
| Motor vehicles | | 630,000 |
| | | 4,365,000 |
| Current Assets | | |
| Stocks | 345,000 | |
| Debtors | 290,000 | |
| | 635,000 | |
| Current Liabilities | | |
| Bank overdraft | 600,000 | |
| | | 35,000 |
| | | 4,400,000 |
| Long-Term Liabilities | | |
| 8% Debentures | | 400,000 |
| | | 4,000,000 |
| Represented By: | | |
| Stated Capital | | 4,000,000 |

**SOLUTION 5**

(a) Ratio

| | Ratio | Basis | Computation | Answer |
|---|---|---|---|---|
| (1) | Return on Capital Employed | Profit before tax & Interest x 100<br>Capital employed | 422 x 100<br>1,270 | 33.23% |
| (2) | Net Assets Turnover | Sales times<br>Net Assets | 4,850 time<br>1,270 | 3.8 times |
| (3) | Gross Profit Margin | Gross Profit x 100<br>Sales | 1,110 x 100<br>4,850 | 22.89% |
| (4) | Net Profit (before tax) Margin | Net Profit (before tax) x 100<br>Sales | 372 x 100<br>4,850 | 7.67% |
| (5) | Current Ratio | Current Assets : 1<br>Current Liabilities | 1,190 : 1<br>1,000 | 1.19:1 |
| (6) | Acid Test Ratio | Current Assets – Stock : 1<br>Current Liabilities | 640 : 1<br>1,000 | 0.64:1 |
| (7) | Stockholding Period | Stock x 365<br>Cost of Sales | 550 x 365<br>3,740 | 54 days |
| (8) | Debtors Collection Period | Debtors x 365<br>Sales | 640 x 365<br>4,850 | 48 days |
| (9) | Creditors Payment Period | Creditors x 365<br>Cost of Sales | 700 x 365<br>3,740 | 68 days |
| (10) | Debt/Equity Ratio | Debt x 100<br>Equity | 600 x 100<br>670 | 89.55% |
| (11) | Dividend Yield | Dividend per Share x 100<br>Net Price | 0.15 x 100<br>6 | 2.5% |
| (12) | Dividend Cover | Net profit after tax times<br>Dividend | 192 times<br>180 | 1.07<br>times |

(b) Report

Analysis of Microchip Ltd financial performance compared to industry average for the year to 31 December 2008.

To : The Board
From: Financial Controller
Date: 20 January, 2009

Introduction

These reports present an analysis of the financial performance of Microchip Ltd juxtaposing to the industry averages.

Profitability

The return on capital employed of Microchip is imprecise being more than 50% higher than the industry average. The company is employing its assets more efficiently and effectively in generating sales as net assets turnover of 3.8 times is double the industry average. However, gross profit margin and net profit margin of Microchip are comparatively lower than the industry averages. This implies that net assets turnover contributes significantly to return on capital employed against net profit margin.

Liquidity

Here Microchip shows real cause for concern. Its current and quick ratios are much worse than the industry average, and indeed far below expected norms. Current liquidity problems appear due to high levels of trade creditors and a high bank overdraft. The high level of stock constitutes to the poor acid test ratio and may be indicate of further obsolete stock. The trade debtors collection figure is reasonable, but at 68 days, Microchip takes longer to pay its creditors than competitors. Whilst this is a source of 'free' finance, it can damage relations with suppliers and may lead to a curtailment of further credit.

Gearing

Microchip gearing is more than twice the level of the industry average. The company is making an overall return of 34.6%, but only paying 8% interest on its loans notes. The gearing level may become a serious issue if Microchip becomes unable to maintain the finance costs. The company already has an overdraft and the ability to make further interest payments could be in doubt.

Investment Ratios

Despite reasonable profitability figures, Microchip's dividend yield is poor compared to the sector average. From the extracts of the changes in equity it can be seen that total dividends are GHS180 million out of available profit for the year of only GHS192 million, hence the very low dividend cover. It is worthy to note that the interim dividend was GHS120 million and the final dividend only GHS60 million. Perhaps this indicates a worsening performance during the year, as normally final dividends are higher than interim dividend.

Conclusion

The company compares favourably with the industry average figures for profitability, however, the company's liquidity and gearing position is quite poor and gives cause for concern.

Yours faithfully,

Financial Controller