SOLUTION ADVANCED FINANCIAL REPORTING NOV 2010

SOLUTION 1

FOFIE GROUP OF COMPANIES
COSOLIDATED CASH FLOW STATEMENT FOR THE YEAR
ENDED DECEMBER 31, 2009

	GHS	GHS
Net profit before tax		2,533,000
Adjustment for:		
Depreciation		850,000
Profit on disposal		(600,000)
Interest receivable		(135,000)
Interest payable		95,000
Loss on disposal		125,000
Pre-tax profit on joint venture (275,000 + 100,000)		(375,000)
Operating profit before working capital changes		2,493,000
Movements in working capital items		966,800
Interest received	130,000	
Interest paid	(45,000)	
Dividend paid to minority interest	(155,000)	
Dividend received from joint venture	50,000	
Taxation paid	(575,000	(595,000)
Net cash from operating activities		2,864,800
Cashflows from investing activities:		
Puchase of property, plant & equipment (1,900,000 – 150,000)	(1,785,000)	
Proceeds from sale of fixed assets	975,000	
Proceeds from disposal of subsidiary less cash & bank balances of subsidiary (610,000 - 40,000 + 375,000)	(275,000)	
Purchase of interest in joint venture	(125,000)	
Net cash used in investing activities		(1,210,000)
Cashflows from financial activities:		
Repayment of borrowed funds	(3,000,000)	
Proceeds from issue of shares	2,285,000	
Net cash used in financing activities		(715,000)
Increase in cash & cash equivalents		939,800
Cash & cash equivalents at jan 1, 2009		14,486,600
Cash & cash equivalents at December 31, 2009		15,426,400

Workings

	GHS
Movement in working capital items	
As given	991,800
Adjustment for WC items of subsidiary:	
Stocks	(300,000)
Debtors	(200,000)
Prepayments	(50,000)
Trade Creditors	450,000
Accruals	75,000
	966,800

Dividend paid to minority interest	
Balance sheet movement	200,000
Profit for the year	375,000
Sale of subsidiary (20% of 2,100,000)	(420,000)
	155,000

Tax paid	
As given	155,000
Tax on joint venture	100,000
Tax on subsidiary sold	125,000
Tax on profit	(955,000)
	(575,000)

Sale of fixed assets	
As given	7,925,000
Transferred to joint venture	(1,000,000)
Fixed assets of subsidiary sold	(1,550,000)
Sale & leaseback	(5,000,000)
Profit on sale	600,000
	975,000

SOLUTION 2

a) Z-score = 0.012*0.36827 + 0.014*23.2368 + 0.033*31.55268 + 0.0006*2282 + 0.999*1.292
= 0.0044 + 0.3253 + 1.0412 + 13.693 + 1.291
= 16.3539

b) Tasty Breweries Limited is very much unlikely to collapse in the next six months.

Workings:

1. **Income Statement**:

	GHS	GHS
Sales (750,490/1.15)		652,600
Cost of sales:		
Opening stock	40,100	
Add: Purchases (460,690/1.15)	400,600	
	440,700	
Less: Closing stock	48,260	392,440
Gross profit		260,160
Less: Selling, general & admin exps.		100,800
Profit before interest & tax		159,360
Interest (24,000*12/100)		2,880
Profit after tax		156,480
Taxation		39,120
Retained profit		117,360

2. **Income Surplus Account**

	GHS
Balances b/f	86,200
Add: profit for year	117,360
	203,560

3. **Balance Sheet**

	GHS	GHS
Property, plant & equipment		330,500
Intangible assets		23,400
		353,900
Current Assets		
Inventory	48,260	
Receiveables	73,200	
Babnk/Cash	29,700	
	151,160	
Current Liabilities		
Payables	69,500	
VAT/NHIS (97,890 – 60,090)	37,800	
Interest payable	2,880	
Taxation	39,120	
Net Current Assets		1,860
Net Assets		149,300
Less: 12% Medium-Term Loan		24,000
		331,760
Financed By:		
Stated Capital		50,000
Capital Surplus		78,200
Income Surplus		203,560
		331,760

4 **Others**

a. Total Assets = 353,900 + 151,160 = 505,060

b. Market value of equity = 156,480* 3.5 = 547,680

5. X_1 = Net working capital/total assets *100
= 1,860/505,060 *100
= 0.36827

6. X_2 = Retained earnings/total assets *100
= 117,360/505,060 *100
= 23.2368

7. X_3 = Profit before interest & tax/total assets *100
= 159,360/505,060 *100
= 31.55268

8. X_4 = Market value of equity/book value of debt securities *100
= 547,680/24,000 *100
= 2,282

9. X_5 = Sales/total assets *100
= 652,600/505,060 *100
= 1.291

(b) Capital Maintenance Concept
(Any 4 of the five listed)

The concept of capital maintenance is concerned with how an entity defines the capital that it seeks to maintain. Several alternative interpretations of this concept have been offered, some of which are as follows:-

1 THE MONEY AMOUNT CONCEPT
This is reflected in Historical Cost Accounting. The aim of this concept is to maintain financial capital money terms, therefore, measurement of periodic profit should ensure that the monetary value of the shareholders' equity is maintained intact. It assumes that, money is stable.

2 THE FINANCIAL CAPITAL CONCEPT
The objective of this concept is to maintain capital of the entity in real terms by constantly updating the historical cost assets for changes in the value of money. This concept purports to show the shareholders' that their capital kept pace with general inflationary pressure during the financial period, by measuring profits in such a way as to take into account changes in the price level. Real capital is money capital that has beend adjusted to maintain it general purchasing power, using a general index eg. Retail price index

3 THE OPERATING CAPABILITY/PHYSICAL CAPITAL CONCEPT
This concpet of capital maintenance asserts that profit is a residual after provision has been made to replace the resources exhausted in the course of operation. It measures the operating or productive capacity or service potential of the entity. It takes into account changes in the

prices of commodities specific to the entity, either directly or by using specific price index to measure changes in the prices ofr similar commodities.

4 THE DISPOSABLE WEALTH CONCEPT

The disposable wealth concept suggests that the maintenance of capital should be viewed from the prospective of the realizable value of the assets of the entity; accordingly, the measurement of periodic profit is required to take into account changes in the realizable value of the net assets attributable to the shareholders' equity.

5 THE INVESTMENT PURCHASING POWEWR/ECONOMIC VALUE CONCEPT

This concept defines the assets of an entity in terms of their potential earning power. The potential earning power is expressed as the present value of all cash flows to be generated in the future.

"The last three concepts (3 – 5) are all employed under the current Cost Accounting systems while item 2 is used under the Current Purchasing Power Accounting"

(c) Revenue from "**sale of Goods**" shall be recognised when all the following conditions have been satisfied:-

(i) The entity has transferred to the buyer significant risk and rewards of ownership to the foods;

(ii) The entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;

(iii) The amount of revenue can be measured reliably;

(iv) It is probably that the economic benefit associated with the transaction will flow to the entity; and

(v) The cost incurred or to be incurred in respect of the transaction can be measured reliably.

The out come of a transaction involving "**rendering of service**" can be estimated reliably when:-

(i) The amount of revenue can be measured reliably;

(ii) It is probable that the economic benefit associated with the transaction will flow to the entity;

(iii) The stage of completion of the transaction at the end of the reporting period can be measured reliably; and

(iv) The cost incurred for the transaction and the cost to complete the transaction can be measured reliably.

SOLUTION 3

(a)

Capital Redemption Account

	GHS		GHS
Patents	300,000	Preference Shares	175,000
Plant & Machinery	300,000	Ordinary Shares	750,000
Inventories	70,000	Land & Buildings	100,000
Trade & Others	220,000	Warranties	40,000
Income Surplus	300,000	Investment	20,000
Capital Suplus	105,000	Provision for reconstriction	200,000
		Damages/claims	10,000
	1,295,000		1,295,000

(b)

SOS Television Limited

Statement of Financial Position as at 30th September, 2008

	GHS	GHS
Non-Current assets		
Land and Buildings		900,000
Plant and Machinery		285,000
		1,185,000
Current Assets		
Inventories	480,000	
Other Receivables	360,000	
Bank and Cash	285,000	
Investment	210,000	
	1,335,000	
Current Liabilities		
Trade & Other payables	392,500	
Provision for warranties	110,000	
	502,500	
Net Current Assets		832,500
Non-Current Liabilities		
15% debentures		(500,000)
		1,517,500
Financed By:		
Stated Capital		
Ordinary shares		750,000
20% Cumulative Preference Shares		525,000
Income Surplus		137,500
Capital Surplus		105,000
		1,517,500

WORKINGS

SOS TELEVISION LIMITED
STATEMENT OF PROFIT EARNED FROM 1ST APRIL TO 30TH SEPTEMBER, 2010

	GHS	GHS
Addition to Networth:		
Bank and cash balances	40,000	
Trade debtors	80,000	
Stock	50,000	
Creditors	20,000	
		190,000
Less: Depreciation		
(0.1 x 300,000 x 6/12)	15,000	
Debenture interest		
(0.15 x 500,000 x 6/12)	37,500	52,500
NET PROFIT		137,500

Workings

SOS TELEVISION LIMITED
STATEMENT OF BANK AND CASH BALANCES AS AT 30TH SEPTEMBER 2010

	GHS	GHS
Bank and cash balance as per Balance Sheet		150,000
Add:		
Proceeds from sale of investment		210,000
		360,000
Less:		
Liability for damages	40,000	
Accrued debenture interst	75,000	115,000
		245,000
Add Increase in Bank and Cash balances (Six months period)		40,000
Bank and Cash balances as at 31st Septembe, 2010		285,000

SOLUTION 4

a) VALUATION OF COMPANIES

1. Using Net Asset Basis

Net Asset per shares = $\frac{\text{Net Assets avalable to Ordinary Share}}{\text{No of Shares Issue}}$

Net Assets available calculated as follows:

		GHS
Property & plant (10,000 + 1,000)		11,000
Trade Investment		6,000
Net Current Assets (8,250 – 2,000 + 500)		6,750
		23,750
Less Long Term	4,000	
Net tax	250	(4,250)
Net Asset available		19,500

Ordinary shares $\frac{19,500}{5,000}$ = 3.9

2. Using P/E Ratio

MV = P/E x EPS

P/E of Church Ltd = $\frac{PPS}{EPS}$

= $\frac{20}{2}$ = 10 times

Since Anointed Ltd is unquoted they are reducing its P/E to 80% of similar quoted company

80% x 10 = 8 times

Earning per share is calculated either using the closing EPS or average EPS

Using closing EPS

= PBT – Tax

2009 = 8000 -2000

$\frac{6000}{5000}$ = GHS1.20

:. NVP 8 x 1.20 = GHS9.6 per share

3. Using Dividend Valuation Basis

MV = $\frac{do\ (l\ tg)}{r\ -\ g}$

where do = 2009 Dividend of GHS4,000

where = r = 20

g = $4\sqrt{\frac{4000}{2500}}$ - 1 = 12%

g = rb

r = $\frac{8000}{20,000}$ x 100 40%

b = $\frac{6000\ -\ 4000}{6000}$ 0.33

g = 4000 x 0.33 = 13%

You can use 12% or 13%

Using 12% = $\frac{4000(1.12)}{0.20 - 0.12}$

$$= 56,000$$

$$\text{PPS} = 56,000/5000$$

$$= \underline{\underline{11.20}}$$

b) <u>Information required for Accountants' report</u>

1. Accounting Policies
2. Divisional performance, turnover, ……. ……
3. Cost of sales
4. Last five years FISI
5. Market Value of properties, plant & equipment
6. Fixed asset movement
7. Details of surplus movement
8. Any contigent liabilities
9. Post Balance sheet events
10. Ensure that all accounts are audited
11. Details of any significant changes during the past five years.

c) (i) The company's borrowings. If loan covenants have been broken or interest and capital repayments requirements are proving difficult to meet, a quick sale would be the main priority.

(ii) The interest expressed in the business. If several parties appear interested it would be logical to wait and see who is prepared to make the best offer.

(iii) The general economic climate. If the economic outlook is poor, the owners may feel it is important to sell the business before the climate worsens and vice versa.

(iv) The personal circumstances of the shareholders. This can vary from the need for money due to debt, divorcce etc or a wish to retire or move on to other things.

(v) Growth rate – (State of the company) in growing or in a state of decline

(vi) The % shares being sold or off-loaded

SOLUTION 5

a) Development expenditure is recognised as an intangible asset if all of the following can be demonstrated.

- The technical feasibility of completing the intangible asset so that it will be available for use or sale.

- The availability of adequate technical, financial, and other resources to complete the development and to use or sell the intangible asset.

- The intention to complete the intangible asset and use or sell it.

- The ability to use or sell the intangible asset.

- How the intangible asset will genertate probable future economic benefits.

- The ability to measure the expenditure.

b) Amounts to be included

Narration	Total	Comprehensive Income	Financial Position
	GHS	GHS	GHS
Project 1	46,500	6,975	39,525
Project 2	27,480	9,160	18,320
Project 3	40,000	40,000	-
Project 4	40,000	-	40,000
Project 5	32,400	-	32,400
	186,380	56,135	-
Total			130,245
Add: Research Exp		22,220	
Total		78,355	

c) i. Cost Model
The carrying amount of an intangible asset is its cost less accumulated amortization and accumulated impairment losses. Assets classified as held for sale are shown at the lower of fair value less cost to sell and carrying amout.

ii. Revaluation Model
The carrying amount of an intangible asset is its fair value less subsequent accumulated amortization and impairment losses. Assets classified as held for sale are shown at the lower of fair value less cost to sell and carrying amount.

Workings
Project 1 = 9/12 * 1/5 * 46,500 = 6,975