Final Admitting Examination

Module 11

Advanced Financial Accounting Solutions

August2013

Note answer 1 (b) is shown first and then followed by 1(a)

Answer 1 (b)

An analysis of foreign exchange Gains/(Losses) arising out of the inclusion of Family Inns UK Ltd in the Group Accounts of Hotel Ireland Ltd

	Controlling	**Non Controlling**	
	Interest	**Interest**	**Group**
Opening net assets Fx loss W/N 1	(€561,569)	(€140,392)	(€701,961)
Net Profit for year Fx loss W/N 2	(€30,882)	(€7,721)	(€38,603)
Goodwill Fx Loss W/N 3	(€1,255)		(€1,255)
Total Foreign exchange (losses)/Gains	**(€593,706)**	**(€148,113)**	**(€741,819)**

W/N 1

Exchange Gain/(Losses) arising on translation of Opening Net Assets of Family Inns UK Ltd -using the exchange rate at the acquisition date- with their subsequent translation using the exchange rate at 31/12/12 .

		Controlling		**Non Controlling**		
		Interest		**Interest**		**Group**
		80%		20%		100%
Share Capital	£	1,200,000	£	300,000	£	1,500,000
Retained Profits	£	2,380,000	£	595,000	£	2,975,000
Net Assets at 30/09/12 UK £	**£**	**3,580,000**	**£**	**895,000**	**£**	**4,475,000**
Exchange Rate at date of purchase	£	0.75	£	0.75	£	0.75
Net asset at Acq date in €euros	€	4,773,333	€	1,193,333	€	5,966,667
Exchange rate at 31/12/12	£	0.85	£	0.85	£	0.85
Opening Net Asset in €euros at 31/12/12	€	4,211,765	€	1,052,941	€	5,264,706
Exchange loss	**(€**	**561,569)**	**(€**	**140,392**)	**(€**	**701,961**)

Question 1 (b) continued

W/N 2- computation of exchange rate arising from translating post acquisition profit for the three months ended 31/12/12 of Family Inns UK Ltd using the average exchange rate and translating it using the year end exchange rate .

	Controlling	Non Controlling	
	Interest	**Interest**	**Group**
Profit for 3 months ended 31/12/12 in £UK	£ 420,000	£ 105,000	£ 525,000
Average exchange rate during year	£ 0.80	£ 0.80	£ 0.80
Profit for 3 months ended 31/12/12 in €euro	€ 525,000	€ 131,250	€ 656,250
Exchange rate at 31/12/12	£ 0.85	£ 0.85	£ 0.85
Profit for year end 31/12/12 at closing rate	€ 494,118	€ 123,529	€ 617,647
Exchange loss ie. Avg rate cf with C.R.	**(€ 30,882)**	**(€ 7,721)**	**(€ 38,603)**

W/N 3

<u>Exchange Gain /Loss arising on Goodwill from: translating</u>

Goodwill at date of acquisition exchange rate i.e. 30/09/12 and exchange rate at 31/12/12

Consideration in Sterling	£	3,588,000	
divided by exchange rate at 30/09/12	£	0.75	
equals		equals	
Consideration in euros per B/S in question	€	4,784,000	
compared with			
Controlling interest in Net Asset per W/N1	€	4,773,333	
Thus Goodwill at purchase date--->	€	10,667	
Goodwill restated y/e exchange rate £0.85			
[€10,667 x £0.75] divided by £0.85	€	9,412	<answer (d) (i)
Loss arising	(€	1,255)	

Note answer to question (c)(i) in relation to the amount of goodwill that would appear on the Group Balance Sheet at year end is also answered ie. €9,412

Question 1 **Answer 1 (a)**	**Post Acq. 3 months to 31/12/12**		**Family Inns UK Ltd**	**Hotels Ireland Ltd**	
Income statement	**£Subsidiary**		**€Subsidiary**	**Parent**	**Group**
Revenue/ Sales	£2,000,000	£0.80	€2,500,000	€18,000,000	€20,500,000
Cost of sales	(£500,000)	£0.80	(€625,000)	(€10,800,000)	(€11,425,000)
Gross Profit	£1,500,000		€1,875,000	€7,200,000	€9,075,000
Operating expenses	(£750,000)	£0.80	(€937,500)	(€6,000,000)	(€6,937,500)
Operating Profit	£750,000		€937,500	€1,200,000	€2,137,500
Exchange gain on loan **W/N 4**				€562,824	€562,824
Finance costs	(£125,000)	£0.80	(€156,250)	(€59,800)	(€216,050)
Profit before tax	£625,000		€781,250	€1,703,024	€2,484,274
Taxation	(£100,000)	£0.80	(€125,000)	(€142,525)	(€267,525)
Profit for the year	£525,000		€656,250	€1,560,499	€2,216,749
Other comprehensive income					
Foreign exchange gains[see1(a)]			(€740,564)	(€1,255)	(€741,819)
Total Comprehensive income	£525,000		(€84,314)	€1,559,244	€1,474,930
Profit and loss for year					
Attributable to controlling %			€525,000	€1,559,244	€2,085,499
Non Controlling interest			€131,250		€131,250
			€656,250	£1,559,244	€2,216,749
Total Comprehensive income					
Attributable to controlling %			(€67,451)	€1,559,244	€1,491,793
Non Controlling interest			(€16,863)	n/a	(€16,863)
			(€84,314)	€1,559,244	€1,474,930

W/N 4 Exchange gain on Loan to Hotels Ireland Ltd.

Loan	£3,588,000	£0.75	€4,784,000	
Loan	£3,588,000	£0.85	€4,221,176	<answer (d) (ii)
Thus Exchange gain			€562,824	

Note the loan represents a monetary item the exchange gain or loss in relation to which is included under a suitable heading such as finance charges in the Income Statement of Hotels Ireland Ltd and Group . It is not necessarily required to be listed separately but it is done so here because of its significance [about 30% of Profit] and to highlight its separate treatment from Gains or Losses arising on Net Investment in Family Inns UK Ltd whose amounts appear under Other Comprehensive Income.

Question 1 continued
Answer to (d) (ii) Loan amount on B/S is €4,221,176 as set out in per W/N 4

Group Statement of Changes in Equity of Hotels Ireland Ltd for year ended 31/12/12
Answer 1(c)

	Share	Share		Retained	Fx currency	Controlling
	Capital	Premium	Revaluation	Profits	Trans Reserve	Interest Total
At 31/12/11	€1,000,000	€ 500,000	€1,150,000	€16,525,000		€19,175,000
Acquisition of NCI						
Comprehensive income				€2,085,499	(€593,706)	€1,491,793
Dividends				(€300,000)		(€300,000)
At 31/12/12	**€1,000,000**	**€500,000**	**€1,150,000**	**€18,310,499**	**(€593,706)**	**€20,366,793**

Note the SOCE should include the attributable portions of non controlling interest i.e NCI. For reasons of “space” the non controlling interest is shown separately below together with the summary totals of controlling interest

	Controlling	Non Controlling
	Interest total	Interest total
At 31/12/11	€19,175,000	
Acquisition of NCI		€1,193,333
Comprehensive income	€1,491,793	(€16,863)
Dividends	(€300,000)	
At 31/12/12	**€20,366,793**	**€1,176,471**

The amount of non controlling interest [minority interest] that would appear on the Balance Sheet is thus €1,176,471

W/N 5 Analysis of Non Controlling interest

Non Controlling interest 20%		
At acquisition date 30/09/12	W/N 1	€1,193,333
Share of profit for year	Answer (b)	€131,250
Exchange gain /losses W/N	Answer 1(a)	(€148,113)
Balance at 31/12/12		**€1,176,471**

note
Share profit €131,250 less exchange losses (€148,113) equals (€16,863) in SOCE

Question 1-continued
Group Balance Sheet of Hotels Ireland as at 31/12/12 [not asked for]

	£Subsidiary		€Subsidiary	Parent	Total
Non Current Assets					
Hotel buildings	£ 5,200,000	£0.85	€ 6,117,647	€ 13,400,000	€ 19,517,647
Family Inns UK				€ 4,784,000	
Goodwill [net of Fx loss €1,255]					€ 9,412
Current Assets					
Inventories	£ 900,000	£0.85	€ 1,058,824	€ 4,900,000	€ 5,958,824
Receivables	£ 150,000	£0.85	€ 176,471	€ 6,100,000	€ 6,276,471
Cash in bank	£ 22,000	£0.85	€ 25,882	€ 47,675	€ 73,557
Total Assets	**£ 6,272,000**		**€ 7,378,824**	**€ 29,231,675**	**€ 31,835,910**
Equity					
Ordinary Share Capital NV €1	£ 1,500,000	£0.75	€ 2,000,000	€ 1,000,000	€ 1,000,000
Share premium				€ 500,000	€ 500,000
Pre-acquisition	£ 2,975,000	£0.75	€ 3,966,667		€ -
Post acquisition	£ 525,000	Bal Fig->	(€ 84,314)	€ 17,222,675	
Exchange gain on UK loan				€ 562,824	
Retained Profits					€ 17,716,793
Revaluation	‘			€ 1,150,000	€ 1,150,000
Equity attributable to owners	£ 5,000,000		€ 5,882,353	€ 20,435,499	**€ 20,366,793**
Non Controlling interest					€ 1,176,471
Non Current Liabilities					
Bank Loans				€ 1,200,000	€ 1,200,000
5% UK Loan				€ 4,221,176	€ 4,221,176
Deferred Tax	£ 262,000	£0.85	€ 308,235	€ 425,000	€ 733,235
Current Liabilities					
Trade and other payables	£ 870,000	£0.85	€ 1,023,529	€ 2,800,000	€ 3,823,529
Tax Liabilities	£ 140,000	£0.85	€ 164,706	€ 150,000	€ 314,706
Total Equity & Liabilities	**£ 6,272,000**		**€ 7,378,824**	**€ 29,231,675**	**€ 31,835,910**

Note only the extreme left and right columns would be published.
The additional headings of pre-acquisition and post acquisition profits and gain on UK Loan are included only for analysis/ study purposes.

Question 2 answer to (a)

Industry Energy Ltd Statement of Comprehensive Income y/e 30/06/13

Revenue **W/N 1**	€ 9,250,000	€ 111,000	€ 9,361,000	3.00
Cost of sales **W/N 2**			(€ 4,862,050)	9.50
Gross Profit			**€ 4,498,950**	0.50
Selling and distribution **W/N 2**		€ 1,865,000		1.00
Administration expense **W/N 2**		€ 1,324,700		4.00
			(€ 3,189,700)	
Operating profit			**€ 1,309,250**	
Share of profit of associates **W/N 10**	€ 6,300	(€ 1,500)	€ 4,800	2.00
Finance charges				
Debenture interest			(€ 5,000)	1.00
Profit before tax			**€ 1,309,050**	
Taxation [€3,600 +€22,000]			(€ 25,600)	1.00
Profit for the year			**€ 1,283,450**	0.25
Other comprehensive income **W/N 7**	Actuarial losses		(€ 170,000)	1.00
Total Comprehensive income for the year			**€ 1,113,450**	0.25

Question 2 answer (c)

Statement of changes in Equity of Industry Energy for year ended 30/06/13

	Share Capital	**Share Premium**	**Retained Profits**	**Total**
Balance at 30/06/12	€ 750,000	€75,000	€ 600,000	€ 1,425,000
Prior year adjustment-contract 1	‘	‘	€ 13,200	€ 13,200
Restated at 30/06/12	€ 750,000	€ 75,000	€ 613,200	€ 1,438,200
Issued during the year per Qn	€ 250,000	€ 125,000		€ 375,000
Share option **W/N 8**	€ 7,200			€ 7,200
Profit for the year			€ 1,113,450	€ 1,113,450
Dividends	‘	‘	(€ 20,000)	(€ 20,000)
Balance at 30/06/13	**€ 1,007,200**	**€ 200,000**	**€ 1,706,650**	**€ 2,913,850**

The company has proposed to pay an ordinary dividend of €0.02 per share totaling €40,000

(a) per W/N 1 Profit on contract 1 occurring year ended 30/06/12 had not been accounted that year

Question 2 -answer (b)

Statement of Financial Position of Industry Energy Ltd as at 30/06/13

Non Current assets	**W/N 3**		€ 2,099,550
Investment in Vacuous Ltd	**W/N 10**	€ 53,600	
Development costs	**W/N 9**	€ 310,000	
			€ 363,600
Current Assets			
Inventory		€ 286,000	
Contract work in progress	**W/N 1**	€ 8,600	
Trade receivables		€ 35,000	
Amounts due from customers	**W/N 1**	€ 64,000	
			€ 393,600
Assets classified as held for sale	**W/N 4**		€ 400,000
			‘
Total Assets			€ 3,256,750
Equity			
Share Capital [N.V. €0.50 per share]	**SOCE**	€ 1,007,200	
Share Premium	**SOCE**	€ 200,000	
Revaluation		€ -	
Retained Profits	**SOCE**	€ 1,706,650	
Total Equity			€ 2,913,850
Non Current Liabilities			
5% Debentures			€ 100,000
Defined Benefits	**W/N 7**		€ 90,000
Provisions-fines	**W/N 6**		€ 60,000
Current Liabilities			
Payables		€ 40,000	
Amounts due to customers	**W/N 1**	€ 4,000	
Taxation		€ 22,000	
Debenture interest owing		€ 2,500	
Bank overdrawn		€ 24,400	
			€ 92,900
Equity plus Liabilities			**€ 3,256,750**

W/N 1 Long term contracts and the allocation of **Revenues** and Costs to S.C.I & amounts to B/S

	Complete	90%	70%	15%
row		**Contract 1**	**Contract 2**	**Contract 3**
1	**Contract Price/ Total revenue**	€ 120,000	€ 90,000	€ 80,000
2	Cumulative costs incurred to date	€ 90,000	€ 60,000	€ 12,000
3	Further costs estimated to complete contract	€ 8,000	€ 16,000	€ 50,000
4	**Overall profit/(Loss) on Contract**	€ 22,000	€ 14,000	€ 18,000
5	Revenue :% complete x contract price row 1	€ 108,000	€ 63,000	equals cost
6	less previous year 60% x contract price row 1	€ 72,000	**N/A**	**N/A**
7	**Revenue this year** [row 5 minus row 6]	**€ 36,000**	**€ 63,000**	**€ 12,000**
8	Costs % complete x [row 2+row 3]	€ 88,200		
9	Cost previous year 60% x [row 2+ row 3]	€ 58,800	**N/A**	**N/A**
10	**Cost this year** row 8 minus row 9	**€ 29,400**	**€ 53,200**	**€ 12,000**
11	**Profit** [row 7 minus row 10]	€ 6,600	€ 9,800	
12	**Work in progress** [row 2 minus row 6]	€ 1,800	€ 6,800	€ -
13	**Amounts due from customers**	€ 36,000	€ 28,000	
14	**Amounts due to customers**			(€ 4,000)
15	**Previous years profit Prior Yr adjust**	€ 13,200		

Total sales from long term contracts is row 7 €36,000+€63,000 +€12,000 = **€111,000**
Total cost of sales from long term contracts row 10 €29,400+€53,200+€12,000 = **€ 94,600**
Work in Progress on B/S is row 12 € 1,800 +€ 6,800 = **€ 8,600**
Amount due from customers row 13 € 36,000+€28,000 = **€ 64,000**
Amounts due to customers row 15 €4000 = **€ 4,000**

Contract 1- **Prior Profit** :: Prior year revenue €72,000 less prior year costs €58,800 = **€13,200**

<u>**Contract 3 15% complete**</u>
As this contract is less complete than company guidelines for taking profit then only revenue equal to the amounts of costs incurred to date resulting in no profit no loss outcome.
This assumes all costs incurred to date are recoverable under this contract

W/N 2- Analyses of costs by function

		Production	Distribution	Admin
Per Trial balance			€ 1,850,000	€ 1,387,500
Inventory per T/B		€ 260,000		
Contributions to fund	**W/N 7**			(€ 180,000)
Defined benefit costs	**W/N 7**			€ 100,000
Fines minimum	**W/N 6**	€ 60,000		
Purchase per T/B		€ 4,200,000		
Inventory at year end Qn note 1		(€ 286,000)		
Contracts costs	**W/N 1**	€ 94,600		
Share option	**W/N 8**			€ 7,200
Impairment-Machinery	**W/N 5**	€ 64,850		
Premises	**W/N 3**	€ 25,000	€ 15,000	€ 10,000
Machinery	**W/N 3**	€ 153,600	€ -	€ -
Development costs	**W/N 9**	€ 290,000	‘	‘
Totals to SCI		**€ 4,862,050**	**€ 1,865,000**	**€ 1,324,700**

W/N 3 Analyses of Non Current Assets

	Premises	Machinery	Total
Opening balance at cost	€ 2,500,000	€ 1,500,000	€ 4,000,000
Additions			€ -
Reclassification **W/N 4**	(€ 500,000)	‘	(€ 500,000)
Total cost value at 30/06/13	€ 2,000,000	€ 1,500,000	€ 3,500,000
Accum. Depreciation 30/06/12	€ 500,000	€ 732,000	€ 1,232,000
Reclassification **W/N 4**	(€ 100,000)		(€ 100,000)
Income statement y/e 30/06/13	€ 50,000	€ 153,600	€ 203,600
Impairment **W/N 5**	‘	€ 64,850	€ 64,850
Accum. Depreciation 30/06/13	€ 450,000	€ 950,450	€ 1,400,450
Net Book value 30/06/12	€ 2,000,000	€ 768,000	€ 2,768,000
Net Book value 30/06/13	€ 1,550,000	€ 549,550	**€ 2,099,550**

Premises :Depreciation straight line: €2,500,000 x 2% =€50,000 . Note commitment to sell some of the buildings did not take place till 29/06/13 ie. after full year's depreciation .

Allocated of depreciation cost as follows:50% to Production €25,000 ; 20% to Distribution €10,000 and the balance 30%i.e €15,000 to administration

Machinery Depreciation 20% RB i.e. NBV [€1,500,000-€732,000] X 20%=€153,600 all to production

W/N 4 Asset available for sale

IFRS 5 A firm commitment entered into by board. Asset must be stated at the lower of its carrying amount and the fair value less costs to sell. In this case the year end carrying value is the lower amount

W/N 5 Impairment of machinery

Assets tested for impairment IAS 36 should be by comparing its carrying amount and recoverable amount. The recoverable amount is the higher of the NRV and the value in use.

Carrying amount is €614,400 ie.[€1,500,000 -(€732,000 +€153,600)
N.R.V. per question €330,000
Value in use €549,550 i.e. €145,000 x 3.79 [5 year annuity factor of 10%]

Comparison is between €614,400 and €549,550 [higher of NRV and Value in Use] =€64,850

W/N 6- Legal requirement to install carbon reduction emission filters

IAS 37 At the balance sheet date there was no present obligation to incur costs of €200,000 to install the filters. Post Balance Sheet there was invitation to suppliers of same to tender but not specific contract so that unless there was an actual contract by 30/06/14 there might still be no present obligation at that subsequent B/S date.30/06/14.
The issues of the fines is difficult to assess without sight of the legislation. On a prudence basis €60,000 should be provided though it could be argued otherwise.

W/N 7 Computation and analysis of amounts charged to income statement in respect of the defined benefit contribution and the increase in liability arising.

	Assets	Liability	SCI	
Values at 30/06/12	€ 900,000	€ 900,000	€ -	
Interest costs 10%		€ 90,000	€ 90,000	
Current service cost		€ 170,000	€ 170,000	
Contribution by				
Company	€ 180,000			
Employees	€ 60,000		(€ 60,000)	
Benefits paid out	(€ 120,000)	(€ 120,000)	€ -	
Return on plan of assets	€ 100,000	‘	(€ 100,000)	
Expected closing balance	€ 1,120,000	€ 1,040,000	**€ 100,000**	**SCI**
Actuarial gains/losses)	€ 80,000	(€ 250,000)	**€ 170,000**	**OCI**
Values at 30/06/13	€ 1,200,000	€ 1,290,000	**€ 90,000**	**B/S**

The charge to the statement of comprehensive income SCI is €100,000 whilst the charge to the Other Comprehensive income OCI is €170,000
The total charges to Income statement is thus €270,000 whilst the amounts paid by the board on is €180,000 leaving an increase outstanding liability of **€90,000**
Note the opening balances there was zero difference between Plan of assets values and obligations and then the nil balance in the Trial balance.

Question 2 continued

W/N 8 Share option at end of four year period. Expected drop out 20%

150 options x 400 employees x €0.60 value at date of grant equals €36,000
Only 80% expected to fulfill condition thus €36,000 x 80% equals €28,800
Closing balance at the end of the first year of four years is €28,800 /4 years =€7,200

Expense- Administration	€7,200	
Equity		€7,200 closing balance 30/06/13

W/N 9- Development Costs IAS 38

Internally generated goodwill	€ 200,000	P38/ IAS38	W/off
Professional fees arising from bring asset to its working condition	**€ 80,000**	P28 b /IAS 38	Asset
Cost of testing whether asset is performing functionally	**€ 120,000**	P28 c /IAS 38	Asset
Cost of introducing new product through promotion and advt.	€ 90,000	P29a /IAS 38	w/off
Purchases of materials including import duties of	**€ 110,000**	P27 a / IAS 38	Asset
Total per Trial Balance	€ 600,000	€ 290,000	

Note internally generate goodwill regardless of how computed is not recognized because the unreliability of the valuation process.
The development expenditure capitalised is €80,000+€120,000+€110,000=€310,000

W/N 10 30**% Investment in Vacuos Ltd - associate company**

6 Month post acquisition thus total profit for year is €42,000 x 6/12 months x 30% =€6,300

€6,300 less impairment of goodwill €1,500 =€4,800

Note goodwill was
Net assets at acquisition date ie.
share capital €80,000 + Pre-acquisition profits €70,000 =€150,000 x 30% =€45,000

Cost of investment €50,000 less share of Net assets €45,000 equals **Goodwill €5,000**

Balance sheet amount is

Investment in Associate	€ 50,000
Post acquisition profits	€ 6,300
Dividend received	(€ 1,200)
Impairment of goodwill	(€ 1,500)
As at 30/06/13	**€ 53,600**

Question 3

Preliminary workings

Leasing

	Open Balance	**10%**	**Repayment**	**Close Balance**
(a)Year 1	€300,000	€30,000	(€79,139)	€250,861
(a)Year 2	€250,861	€25,086	(€79,139)	€196,808
Year 3	€196,808	€19,681	(€79,139)	€137,349
Year 4	€137,349	€13,735	(€79,139)	€71,945
Year 5	€71,945	€7,194	(€79,139)	€0

Note only the first two rows are necessary to determine C.L. and N.C.L. €196,808

Adjustments [not necessary to set out. Included for information only]

	Dr	Cr
	€	€
Asset-Machine	300,000	
Loan		300,000
Accum. Depreciation [over 5 years]		60,000
Income Statement	60,000	
Loan a/c interest -see above year 1		30,000
Income statement interest	30,000	
Repayment-Cost of sales-I/S		79,139
Loan	79,139	
Reversal of lease payment and charging it directly to loan account		
Revaluation	700,000	
Non current asset premises		700,000

Summarising the adjustments

	[←---------------Equity------------→]		[←-----Net Liabilities------------→]	
	Income statement	Revaluation	Non Current Assets	Non Current (Liabilities)
Machine/Loan			300,000	(300,000)
Repayment reversal	79,139			79,139
Depreciation	(60,000)		(60,000)	
Loan interest	(30,000)			(30,000)
Revaluation reduction	‘	(700,000)	(700,000)	‘
	(10,861)	(700,000)	(460,000)	(250,861)
Non C.L [see above]				(196,808)
C.L.				(54,053)

Question 3-continued

Note this answer in relation to the computation of ratios is an abridged version. The formal answer would have required the following format

Name of Formula	**Formula**	**2012**	**2011**
??	??	?? x 100 =??% ??	?? x 100 =??% ??
Example			
Current Ratio	C.A. to C.L.	€955,851 =1.38 to 1 €694,411	€702,740 =0.97 to 1 €724,415
After adjustment for €54,053		€955,851 = 1.28 to 1 €748,464	

(a)

Liquidity :The ability of an entity to meet day to day demands for cash

The main impact on Liquidity is the increase in current Liabilities by €54,053

Liquidity ratios

Current Ratio		1.38 to 1	0.97 to 1
After extra CL loan	€54,053	1.28 to 1	
Quick asset ratio		0.67 to 1	1.179 to 1
after extra CL loan	€54,053	0.62 to 1	

Profitability: The ability to grow an entity through profits thereby increasing its Equity

Any Profit before interest

This will increase by €19,139 ie. reversal of lease payment of €79,139 less additional depreciation charge of €60,000

Any Profit after interest

This will fall by €10,861 i.e. plus €19,139 above less lease interest of €30,000

Capital employed - Equity plus Non Current Liabilities

This will fall by €514,053 as follows

Increase in non Current Liabilities [with reference to Lease]	€196,808
Reduction in current profit [€60k Dep+€30k interest plus add back of €79,139]	(€ 10,861)
Reduction in revaluation surplus by	(€700,000)
Net Change is thus	(€514,053)

Profitability ratio- continued ;[only two asked for]

Gross Profit to Sales		18.00%	20.00%
adjusted for extra depreciation	(€60,000)	16.76%	
Operating profit/Sales		8.00%	8.00%
adjusted for extra depreciation and add back of loan repayment	€19,139	8.39%	
Return on Capital Employed			18.50%
PbIT/ Equity + Long term loans		18.83%	
Adjusted to Profit before interest & tax	€19,139	26.32%	
C/employed adjusted for profit, NCL and revaluation	(€514,053)		

Efficiency : minimising inputs to achieve given outputs
As only trade payables are dealt with in these formulae then ratios are not affected by adjustments. **Only two ratios asked for**

Efficiency Ratios			change	
Inventory days	45	days	50%	30
Receivable Days	35	days	6%	33
Payable days	30	days	(14%)	35
Turnaround	50		79%	28

Investor returns [**only two asked for]**
Investor will look for returns that can be a composite of dividends and capital gains.
Return sought will take account of financial risk or gearing and business risk.
Shareholder funds will decrease by €110,861 i.e reduction in available profit of €10,861 and reduction in revaluation surplus of €100,000

Return on S/holder funds			20.08%	16.29%
	adjusted	(€10,861)	30.18%	
Revaluation & Profit w/down		(€710,861)		
Earnings per share			€0.202	€0.16
	adjusted	€10,861	€0.197	
Gearing	NCL / Equity +NCL		2.18%	1.80%
	adjusted	€196,808 / (€514,053)	15.63%	

Memorandum

The board of Failte Products
From J. Snodgrass

Date

Subject : A review of the financial statements of the company for the last two years with particular reference to the issue of addressing current funding requirements.

Points to include though others may be equally acceptable.
Some reference to a failure to incorporate regular valuations of the premises and the incorrect treatment of finance lease-as such omissions might suggest that the financial statements may not be prepared in accordance with GAAP.. should be included in the report

Both liquidity ratios are operating below the ideal standards of 2:1 and 1:1

Despite Gross Profit margin falling , Operating margins were maintained due to a reduction in operating expenses as percentage of sales.

Inventory has increased by 50% from 30 days to 45 days. Had it remained at 30 days this would have resulted in an increase cash of €163,472 [[15/365 days] x€3,977,820].

Had Receivables collection been maintained at 28 days this would have resulted in cash inflow of €93,000 approx [[7/365] x €4,851,000] assuming all sales were for credit

Payables credit was reduced from 35 days credit to 30 days which has result in an increased outflow of €54,490 say €55,000 [5/365 days x €3,977,820]
The revised/increased gearing [1.80% to 11.26%] may deter the bank from further funding.

Proposal

Inventory - if maintained per last year would result in a cash increase of	€163,.000 rounded
Assuming no unidentified obsolete inventory	
Receivables-if maintained per last year would result in cash increase cash of	€ 93,000
Assuming no unidentified bad debts and all sales are for credit.	
Payables-if maintained per last year would reduce cash outflow by	€ 55,000 rounded
Assume C.O.S approximates to Purchases and all for credit	€311,000
However there was a “once off” cash inflow from sale of machinery	(€208,000)
NBV €128,000 plus profit of €80,000 on sale	
Payout of dividends [Freeze future payments ?]Improve cash flow by]	€300,000
Potential increase in cash flow- all other things being equal	€403,000
Current overdraft	(€367,466)
Projected incremental cash inflow	€ 36,534
Assuming no projected capital expenditure needs.	