

Accounting Fundamentals Assessment 1
(LCBB4001)

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Question 1

Income Statement

Income Statement		
Particulars	Amount £000	Amount £000
Revenue		
Sales	30300	
Total Revenue		30300
Less: Cost of Sales	16220	
Gross profit		14080
Operating Expenses		
Distribution expenses	2160	
Administrative Expenses	5965.5352	
Total Operating cost		8125.535
Operating Profit		5954.465
Less: Interest Expenses	480	
Profit Before tax		5474.465
less: taxes		1600
Net Profits		3874.465

Financial Statement

Financial Statement		
	Amount	Amount
Assets	£000	£000
Non-Current Assets		
Land At cost	20000	
Building at cost	16000	
Less: Acc dep	-4580	
Plant at cost	25600	
Less: Acc dep	-7520	
Total Fixed Assets		49500
Current Assets		
Inventory on 31 December 2019	3120	
Bank	320	
Trade Receivables	8240	
Less: bad debt	-0.24	
Less: Allowances	-164.7952	
Total Current Assets		11514.96
Total Assets		61014.96
Liabilities		
Non-current liabilities		
12% debentures	4000	4000

Current Liabilities		
Trade payables	4480	
Outstanding fee	0.5	
Income tax liability	1600	
Outstanding interest	240	
Total Current Liabilities		6320.5
Total Liabilities		10320.5
net Worth		50694.46
Equity and Shareholder Fund		
Ordinary shares	29000	
Share premium	5000	
Retained Earnings	11694.4648	
Revaluation Profit	5000	
Total		50694.46

Working Notes

Workings Note 1:	Retained Earnings
Opening Retained Earnings	8380
Add: profits	3874.4648
Less: Dividends	560

Closing balance	11694.4648
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	Workings note 2	depreciation		
Item	Fixed Assets at cost	Depreciation	Accumulated Depreciation	Carrying value
Building	16000	320	4580	11420
Plant	25600	2560	7520	18080

Workings Note 3	Allowances or Receivables
Tarce receivables	8240
Less: bad debt	-0.24
Closing value	8239.76
Allowance @2%	164.7952
Working Note 4	Administrative Account
Opening administrative	2920
Add: Depreciation	2880

bad debt	0.24
Allowance for bad debt	164.7952
Outstanding interest	0.5
Administrative Expenses	5965.5352
Working Note 5	Interest Expenses
Loan amount	4000
Interest rate	12%
yearly Interest	480
less: paid	240
Outstanding	240

Question 2

Return on Capital Employed

Return on capital Employed			
Particulars	2019	2018	Trend
Operating Profit	23.00	29.70	-23%
Debt	41.90	65.10	-36%
Equity	93.20	80.30	16%
Capital Employed	135.10	145.40	-7%
Return on capital Employed	17%	20%	-17%

Table: Return on Capital Employed of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It indicates the amount of money that a company generates from its owned capital through investment. ROCE for the selected 2019 and 2018 amounted to 17% and 20% respectively. It can be noted that the ratio has decreased for the year 2019 which suggests that the ability of company to take effective and profitable investment decision has declined or that the economy is going through depression due to which the business is unable to improve return from investment. However, for proper and accurate assessment, ROCE should always be double that the interest rate of the business and lower return indicates that the firm is making poor use of its capital resources (Svynarenko, Zhang and Kim, 2019).

Return on Equity

Return on Equity			
Particulars	2019	2018	Trend
Net Profit	12.90	18.30	-30%
Total Equity	93.20	80.30	16%
Return On Equity	0.14	0.23	-39%

Table: Return on Equity of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It is the measure of profitability of a business in relation to its equity. ROE for the business for 2019 and 2018 amounted to 0.14 and 0.23, respectively. Although the rate of REO depends on the industry or sector within which the company is operating, a declining ROE is an indication of poor investment decision and less efficient management in creating profit and increasing shareholder value. Further, if a company aggressively borrows money, it can also cause the money ROE to decline to a significant extent (Haskins, 2017).

Earnings Per Share

Earnings per Share			
Particulars	2019	2018	Trend
Net Profit	12.90	18.30	-30%
Total Number of shares issued	17.80	17.80	0%
Earnings per Share	0.72	1.03	-30%

Table: Earnings per share of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It describes the profit per outstanding share of stock which is usually calculated on an annual basis. The EPS of the business for the year 2019 and 2018 amounted to 0.72 and 1.03 respectively. Most of the time EPS is used to compare with the performance of its competitors or with industry standard. However, a low amount o EPS or declining EPS suggests that the profit per outstanding share of the business is considerably low or declining due to increased competition or onset of inflation within the country. However, low EPS also means that company might have spent a lot of money in the past year (Wu and Lin, 2018).

Gross Profit

Gross Profit Margin			
Particulars	2019	2018	Trend
Gross Profit	191.80	186.90	3%
Sales	501.30	486.80	3%
Gross Profit Margin	38%	38%	0%

Table: Gross Profit Margin of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

Gross profit denotes the amount of money that a business generates from after covering for cost of goods sold. High gross profit suggests that the company's sales is significantly high compared to its COSG which is making the company more capable of retaining profit. The Gross profit for both the years were consistent at 38% indicating that the company making strong and consistent profit which have not been affected by increasing competition. Also, the rate of profit is significantly higher which denotes that the that the sales stream of the business is strong. Strong sales indicate that the demand for the services and products of the company is higher than usual (Farfan et al., 2017).

Asset Turnover

Assets Turnover			
Particulars	2019	2018	Trend
Sales	501.30	486.80	3%
Total Assets	286.10	293.80	-3%
Average total assets	289.95	289.95	0%
Assets Turnover	1.73	1.68	3%

Table: Asset Turnover ratio of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It describes the profit that total assets of the business generate through its effective and efficient utilization. As can be seen from the calculation, assets turnover of the company for 2019 and 2018 amounted to 1.73 and 1.68. It is evident that the turnover has marginally increased for 2019 which can be due to the improvement in the utilization of assets or updating the fixed assets of the company that have improved the productivity of the business to considerable extent. It also suggests that the company is able to effectively generate sales for its owned assets despite facing fierce competition and that the business would be able to sustain itself for longer time span (Lee and Lee, 2018).

Stock Holding Period

Stock Holding period			
Particulars	2019	2018	Trend
Cost of Goods sold	309.50	299.90	3%
Inventory	38.80	41.10	-6%
Average inventory	39.95	39.95	0%
Stock Holding period	47.11	48.62	-3%

Table: Stock Holding Period of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It shows the number of days on average that a business holds its inventory before selling it into the market and replacing it with new ones. A decreasing period is a good indication and suggests that the stock is being sold much faster and hence the holding period of inventory have been reduced and vice versa. For the business, the holding period for 2019 and 2018 amounted to 47.11 and 48.62, respectively. It denotes that the holding period has marginally declined and hence it can be interpreted that the products of the business were sold at a faster pace in 2019 which can be due to increase in demand and increase in production level or both (Nurfadilah and Daryanto, 2018).

Debtors Collection Period

Debtors Collection period			
Particulars	2019	2018	Trend
Sales	501.30	486.80	3%
Debtors	114.90	114.70	0%
Average debtors	114.80	114.80	0%
Debtors Collection period	83.59	86.08	-3%

Table: Debtors Collection Period of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It represents the average time a company takes to collect all its outstanding debts and liabilities. Usually, all receivables are collected within 20 days of facilitating credit sales. For the company, the collection period for 2019 and 2018 were 83.59 and 86.08 which is considerably higher than the industry sector. It means that the business is extending its credit policy to attract more customers to its business and to increase the sales and demand of its products, However, the risk of bad debts is also higher in longer credit facility and the customer can become bankrupt and the amount of credit sales won't be able to be recovered.

Current ratio

Current ratio			
Particulars	2019	2018	Trend
Current Assets	153.90	156.50	-2%
Current Liabilities	151.00	148.40	2%
Current ratio	1.02	1.05	-3%

Table: Current Ratio of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It describes the ability of business to pay all its short-term debts using its current assets. Usually, ratio higher than one is preferred by investors as it denotes that the marketable assets of the business are higher than all its short-term debts. Current ratio of the company for 2019 and 2018 stood out at 1.02 and 1.05, respectively. It indicates that the company is capable for covering its short-term obligations without raising external source of funding (Goud and Kumar, 2019).

Gearing ratio:

Gearing Ratio			
Particulars	2019	2018	Trend
Debt	41.90	65.10	-36%
Capital Employed	135.10	145.40	-7%
Gearing Ratio	0.31	0.45	-31%

Table: Gearing Ratio of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It compares some of owner's equity to debts or funds borrowed by a firm. The gearing ratio of the company for 2019 and 2018 were 0.32 and 0.45. It suggests that the debts of the company are lower the capital employed by the business, and hence the company is more inclined towards internal source of funding (Ernawati, Handojo and Murhadi, 2018).

Interest Coverage:

Interest Coverage			
Particulars	2019.00	2018.00	Trend
Operating Profit	23.00	29.70	-23%
Interest Cost	0.20	3.50	-94%
			#DIV/0!
Interest Coverage	115.00	8.49	1255%

Table: Interest Coverage Ratio of Jerry plc for the year 2018 and 2019

(Source: Created by Author)

It highlights the ability of the business to pay for its interest costs using the operating income of the company. For the company is question, the interest coverage for 2019 and 2018 were 115 and 8.49 respectively. The company coverage ratio has increased to a significant extent. It is since the interest cost of the business fell down to 0,20 from 3.50 of 2017 which enabled the company to improve its ability to cover its interest expenses (Wu and Lin, 2018).

Question 3

a) Three Different User Groups of Company Accounts

The different types of user groups of company accounts are the owners of the company, the management of the company, and the government.

Owners

The owners within the company serve the purpose of providing financial information to the company in the context of the stocks. This information is especially important for the company for preparing the financial statements. It also helps in progressing with the process of stock holding. If the company is facing adverse situations, then they can decide to sell their stocks. This decision can further be modified by selling more stocks or reducing the selling of

stocks. This will help the company in gaining financial stability (Timbata and Park, 2018). This is also indicative of the performance of the company which is also associated with the owners and the investors. This financial information helps in enhancing the investment aspects of the company.

Management

Management of the company helps in running the daily business activities of the company. It plays an important role in creating a strong relationship with the owners and the investors of the company. The financial decisions of the company are made more sound with the enhancement in its efficiency (Abdullahi and Abubakar, 2017). These decisions are also related to the use of raw materials, the balance sheet, earnings, and performances. It also relates to the evaluation of the targets which are said by the organizational departments for accomplishing the set goals and the objectives. This information is indicative of the analysis which helps in analysing the financial statements.

Government

The government also shows interest in the company's business activities. Different rationales lead to the development of an interest in the financial aspects of the company. The earnings of the company represent its financial status and ensure that it can gain a strong position in the operating marketing economy (Minnis and Shroff, 2017). Moreover, it is the responsibility of the company to avoid changes in inaccurate documents and comply with the policies and regulations. It is also important to comply with these regulations because it ensures that the company and its business activities are being performed accordingly decreasing the scope of conflicts and interruptions in the future.

b) Advantages and Disadvantages of Financial Reporting Regulatory Regime:

A regulatory financial reporting regime is especially important for the company. It has one of the significant impacts on the principles and the business activities of the organization. There are certain accounting standards which are also included in the financial reporting regime. There are certain benefits and the drawbacks related to the same-

Advantages-

The regulated financial reporting regime helps in enhancing the transparency with the organization. It ensures that accounting is conducted uniformly. The companies comply with the policies and the regulations and ensure the maximum accessibility of their products and services. It also supports the organization in dealing with adverse situations like those of the decreasing market share or degrading cash position in the operating economy (Stubbs and Higgins, 2018). This is especially important to ensure that the company has not fallen into the trap of fraudulent activities and practices. These regimes help in avoiding such situations and protecting the interests of the investors and other shareholders.

Disadvantages-

It is inclusive of the maximum wastage of time and effort. These regimes are complex in understanding and thus require effort to analyze them and then take the decisions accordingly. It requires the strength of the workforce as they must monitor and review the financial compliance with similar policies and regimes. Thus, the overall compliance cost of the company is enhanced creating the pressure on the financial resources of the organization. The level of flexibility is also declined because the organizations are required to comply strictly with the norms and thus any interruptions can lead to serious conflicts in the future (Sunder, 2016). The uniqueness of the business model and the practices are required to be linked according to the norms set in the financial reporting regimes. It also adds to the burden of ensuring that the organizations and the employees have the right accounting information for developing the business with minimum challenges and risks.

c) Limitations of Financial Statements

The financial statements are especially important to understand the cash position of the company. However, there are certain limitations associated with the same. Firstly, there are chances that there are personal judgments regarding financial statements. The value of the assets and the liabilities are not represented correctly that is following the accounting standards. There are methods of depreciation, amortization, and others that are not presented in the financial statements and thus acts as an imitation. Another major limitation is the specific period reporting (Jürgens and Erdmann, 2020). The financial statements are prepared in the context of the specific time and thus sets the parameters that cannot be evaluated beyond it. This also has a significant impact on the performance of the company and curbs the process of actual analysis of the products. Moreover, the value of the intangible assets is not represented in the balance sheet. These intangible assets help in creating more sales but are not included in the financial statements. Comparability is another limitation of the financial statements. This

is one of the common practices that the financial statements of one company is compared to another. But due to certain factors, this process is not done properly and the analysis of the same makes it difficult to find the results (Gamayuni, 2019). The financial statements do not discuss the nonfinancial issues which are also important for the growth and the development of the company like social and governmental concerns. The financial statements lack such information (Sunder, S. 2016). The financial statements have the capability of only predicting the success of the organization to a certain period. It does not give the right results in the context of future predictions. There are assumptions made but they are not right in the actual sense. Thus, the financial statements are also linked with certain limitations. It is thus important to verify the financial statements and broaden its approach so that it can deliver more useful information in the context of the company. It is therefore important to consider the importance of these financial statements in the context of the limitations.

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