

Interpretation of Financial Statements

EXAMINABLE FROM JUNE 2007

Students will be sent by post up to three financial statements approximately four weeks before the examination. The onus is on the students to ensure they have received these statements.

AIM

To ensure students can use company financial information to assess effectively the securities issued by companies.

OBJECTIVES

Students should be able to display an ability to think critically and to communicate effectively by:

- i) analysing, interpreting and comparing company (including group) financial information, considering performance and prospects and evaluating company securities in the light of such analysis;
- ii) demonstrating an understanding of the implications of changes in capital structure;
- iii) demonstrating an awareness of the different types and characteristics of corporate securities and by being able to identify and understand the main financial data which affect their evaluation;
- iv) demonstrating an understanding of accounting terminology and concepts, including an awareness of current accounting issues and problems and their implications for investors;
- v) demonstrating an understanding of the impact of statutory and non-statutory regulation on the presentation and interpretation of financial statements;
- vi) demonstrating an understanding of the impact of Corporate Taxation on the presentation and interpretation of financial statements;
- vii) demonstrating an awareness of the fundamental differences in taxation and accounting practices used in the major overseas countries of investment.

Interpretation of Financial Statements

EXAMINABLE FROM JUNE 2007

NOTE: Students should keep abreast of current issues in financial reporting

ASSESSMENT STRUCTURE

A 3-hour paper divided into three sections:

SECTION A: This section will concentrate on but not be limited to one set of accounts. One compulsory question will be based on the financial statements issued by public companies which students will have been sent for study four weeks prior to the examination. The question will test the students' understanding and ability to interpret financial information, to use financial and accounting ratios and to relate and appreciate the relevance of all the elements of corporate reports. Where appropriate, parts of the question may also incorporate hypothetical events subsequent to the publication of the financial statement. This section will carry 45% of the marks.

SECTION B: One compulsory question and two questions of which students will be expected to answer one. This section may draw on extracts from *ONE OR MORE* of the previously distributed financial statements, or extracts from any other financial statements published in the USA, member states of the EU, Japan and other main international markets and may require students to perform and interpret calculations. This section will carry 35% of the marks.

SECTION C: Up to ten compulsory short answer questions. This section will carry 20% of the marks.

Content

It is emphasised that the intention of the examination is to assess students' analytical and interpretative skills rather than their technical accounting ability. It is also expected that they should have an understanding of standard accounting practices and an awareness of matters currently under discussion.

1. Interpretation of Financial Information

1.1 The effect of accounting practices

Understanding of the effect of accounting practices on the numbers most significant for investment decisions (profit, earnings per share, asset value etc).

1.2 Financial and accounting ratios

Analysis and interpretation of ratios. Understanding of the significance of the main financial and accounting ratios to investors. Presentation of findings in report form for the benefit of an investor.

Interpretation of Financial Statements

EXAMINABLE FROM JUNE 2007

1.3 *Changes in capital structure*

Understanding of the impact of structure changes in capital structure upon the financial condition of a company and upon other securities of the company already in issue. This will cover inter alia, scrip and rights issues, public issues and vendor placings; acquisitions and mergers for cash or securities; schemes of arrangement; the impact of share purchase for cancellation; the issue of convertibles and warrants; capital reduction schemes agreed by the courts.

1.4 *Comparisons of accounting figures*

Ability to compare, contrast and recognise the significance of accounting information for:

- a) companies in different industries;
- b) different companies within the same industry;
- c) the same company over successive accounting periods.

*NOTE: Student are **not** expected to have a detailed knowledge of specialist accounting practices for specific industries, but will be examined upon their ability to understand why comparisons may be valid in some cases and not in others.*

1.5 *Group accounts*

An understanding of the advantages and limitations of presenting group accounts in the form of consolidated accounts.

1.6 *Elements of corporate reports*

Understanding of the relevance of all elements of corporate reports for financial analysis including Chairman's Statement and Directors' Report, Auditors' Report, Statement of Accounting Policies, cashflow statements and other qualitative information provided with the annual report and accounts, prospectuses, interim statements and merger documents.

1.7 *Matters currently under discussion*

Understanding of relevant matters currently the subject of public debate. Students should be familiar with what is being said in the public and professional press and understand the issues involved.

2. **Characteristics of Corporate Securities**

A knowledge of the main classes of securities issued in the UK and the other member states of the EC and the major international markets. An ability to compare and contrast different types of security.

Classes of Securities

Implications of different classes of security upon a company's gearing.

Interpretation of Financial Statements

EXAMINABLE FROM JUNE 2007

3. Accounting Terminology and Concepts

Accounting terminology and a knowledge of accounting concepts and conventions to include the balance sheet, profit and loss account, cashflow statement and notes to the accounts. An understanding of the distinction between capital and revenue, the valuation of assets for accounting purposes and the determination of profit and earnings per share on the nil, net and full distribution bases. An understanding of the significance of the statement of accounting policies in relation to the concept of a true and fair view.

4. Presentation of Financial Statements

Impact of statutory and non-statutory regulation on UK financial statements

An understanding of the effect on the presentation of financial statements of the Companies Acts and non-statutory regulations, including standards and other guidance issued by IASB and stock exchange requirements.

5. Overseas Accounting Practices

An elementary understanding of the effect of the differences in corporate accounting practices, international accounting standards and practices and taxation practices in the USA, EU and other main international markets in interpreting earnings per share, asset value and gearing.

READING LIST

Interpreting Company Reports and Accounts
Sugden D; Gee & Holmes
FT/Prentice Hall