

Task IM-13.9: Statement of Changes in Equity

MESSINGEN AG is an outdoor-internet dealership in Osnabrück. MESSINGEN AG is founded as a company based on shares on 1.01.20X1 by a share issue of 50,000.00 EUR – 10,000 ordinary shares at 7.00 EUR/share (issue price). In the memorandum of incorporation MESSINGEN AG states that it will apply § 150 AktG that way that additions to the German Legal Reserves account are made until the capital reserves and the German legal reserves together reach an amount of 30 % of the issued capital.

On 2.04.20X1, MESSINGEN AG buys a storage building. The cost of acquisition of the storage building is 620,000.00 EUR, ¼ thereof is for the land. Ignore taxes on property acquisition. Depreciation of the building is along straight line method over 50 years. The property is financed by a bank loan which is 600,000.00 EUR. The bank loan requires interest payments PRT (=pro rata temporis) at a rate of interest of 3 %/a and a pay-off payment of 30,000.00 EUR/a. MESSINGEN AG takes the bank loan on 1.04.20X1. The pay-off is paid at the year end at 30,000.00 EUR.

In the accounting period 20X1, MESSINGEN AG earned a gross profit of 20,000.00 EUR. You have to calculate the profit before and after taxes. The total profit/loss is carried forward to the next accounting period 20X2.

On 2.01.20X2, MESSINGEN AG issues 10,000 preference shares at a nominal value of 5.00 EUR/share. The preference shares are non-redeemable. The share issue does not cause contributions to the capital reserves, as it is par value. The preference shares pay the holders a preference dividend on 31.12. of every year to the extent of 4.00 %/a based on the share's nominal value. For 20X2, MESSINGEN AG's annual meeting decides to pay the preference dividends as scheduled on 31.12.20X2.

In 20X2, MESSINGEN AG earns a **gross** profit of 176,000.00 EUR. MESSINGEN AG decides to declare a dividend of 0.50 EUR/ordinary share. The dividend is paid in 20X3. 40 % of the remaining distributable amount is added to earnings reserves, the other portion is carried forward to the next Accounting period.

Required: Prepare the equity section of MESSINGEN AG's balance sheet for the accounting period 20X2. Disclose the amounts for reserves separately (capital reserves, earnings reserves and revaluation reserves). Set up a statement of changes in equity for the periods 20X1 and 20X2.

Consider § 150 AktG (Translation: Norton Rose Fulbright): (1) A legal reserve shall be created in the balance sheet of the annual financial statements to be prepared pursuant to §§ 242 and 264 of the Commercial Code. (2) The amount to be transferred to such reserve shall be one-twentieth of annual net profit, after deducting any loss carried forward from the previous year, until the legal reserve and the capital reserves pursuant to § 272 (2) sentences 1 to 3 of the Commercial Code in aggregate amount to one-tenth of the share capital or any higher percentage set by the articles. (3) If the legal reserve and the capital reserves pursuant to § 272 (2) sentence 1 to 3 of the Commercial Code in aggregate do not exceed one-tenth or the share capital or any higher percentage set by the articles, such reserves may be used only: 1. to offset an annual net loss to the extent such loss is not covered by profits carried forward from the previous year and cannot be offset by a transfer from other profit reserves; 2. to offset a loss carried forward from the previous year to the extent such loss is not covered by an annual net profit and cannot be offset by a transfer from other profit reserves. (4) 1 If the legal reserve and the capital reserves pursuant to § 272 (2) sentence 1 to 3 of the Commercial Code in aggregate exceed one-tenth of the share capital or any higher percentage set by the articles, such excess may be used: 1. to cover an annual net loss to the extent such loss is not covered by profits carried forward from the previous year; 2. to cover a loss carried forward from the previous year to the extent such loss is not covered by annual net profit; Norton Rose Fulbright – December 2016 77 German Stock Corporation Act 3. for an increase of the share capital from the corporation's reserves under §§ 207 to 220. 2 Such excess may not be used pursuant to Nos. 1 and 2 if at the same time transfers are made from profit reserves for the purpose of payment of dividends.

Solution:

Income Statement 20X1:

- gross profit is given: -50,000 EUR
- Depreciation in the first year commences on 2.04.20X1 and equals to: $0.75 \times (620,000 \times \frac{3}{4}) / 50 = \mathbf{6,975.00 \text{ EUR}}$.
- Interest equals to: $0.75 \times 600,000 \times 3\% = \mathbf{13,500.00 \text{ EUR}}$.

Income Statement 20X2:

- gross profit is given: 176,000 EUR
- Depreciation equals to: $(620,000 \times \frac{3}{4}) / 50 = \mathbf{9,300.00 \text{ EUR}}$
- Interest equals to: $(600,000 - 30,000) \times 3\% = \mathbf{17,100.00 \text{ EUR}}$.

MESSINGEN AG's STATEMENT of COMPREHENSIVE INCOME for the year ended 31.12.20X1		MESSINGEN AG's STATEMENT of COMPREHENSIVE INCOME for the year ended 31.12.20X2	
	[EUR]		[EUR]
Gross profit	<u>20,000.00</u>	Gross profit	<u>176,000.00</u>
	20,000.00		176,000.00
Materials		Materials	
Labour		Labour	
Depreciation	(6,975.00)	Depreciation	(9,300.00)
Other expenses		Other expenses	
Earnings before int. & taxes (EBIT)	<u>13,025.00</u>	Earnings before int. & taxes (EBIT)	<u>166,700.00</u>
Interest	<u>(13,500.00)</u>	Interest	<u>(17,100.00)</u>
Earnings before taxes (EBT)	(475.00)	Earnings before taxes (EBT)	149,600.00
Income tax expenses	0.00	Income tax expenses	(44,880.00)
Deferred taxes		Deferred taxes	
Earnings after taxes (EAT)	<u>(475.00)</u>	Earnings after taxes (EAT)	<u>104,720.00</u>

The amount added to the Legal reserves equals to $5\% \times (104,720 - 475) = \mathbf{5,212.25 \text{ EUR}}$.

The preference dividend equals to: $50,000 \times 4\% = \mathbf{2,000.00 \text{ EUR}}$.

The ordinary shares' dividend adds up to $0.50 \times 10,000 = \mathbf{5,000.00 \text{ EUR}}$.

Additions to reserves: $40\% \times (104,720 - 475 - 5,212.25 - 2,000 - 5,000) = \mathbf{36,813.10 \text{ EUR}}$.

**Messingen AG's
STATEMENT of CHANGES in EQUITY
as at 31.12.20X2**

	Share capital	Reserves	Retained earnings	total
	[EUR]	[EUR]	[EUR]	[EUR]
as at 1.01.20X1				0.00
Share issue	50,000.00	20,000.00		70,000.00
Profit 20X1			(475.00)	(475.00)
as at 31.12.20X1	50,000.00	20,000.00	(475.00)	69,525.00
Share issue	50,000.00			50,000.00
Profit 20X2			104,720.00	104,720.00
pref Dividend			(2,000.00)	(2,000.00)
ord. Dividend			(5,000.00)	(5,000.00)
Add to legal reserves		5,212.25	(5,212.25)	0.00
Additions to reserves		36,813.10	(36,813.10)	0.00
as at 31.12.20X2	100,000.00	62,025.35	55,219.65	217,245.00

Exhibit 1: Statement of changes in equity

**Messingen AG's
STATEMENT of FINANCIAL POSITION
as at 31.12.20X2**

A		C, L
<i>Non-current assets</i>	[EUR]	<i>Equity</i>
P, P, E		Ord. share capital
Intangibles		Pref. share capital
Financial assets		CRes
		GLRes
		ERes
		RevRes
		Retained earnings
		217,245.00
<i>Current assets</i>		<i>Liabilities</i>
Inventory		Interest bear liab
Accounts receivables		Accounts payables
Prepaid expenses		Provisions
Cash/Bank		Tax liabilities
Total assets	0.00	Total equity and liab.
		434,490.00

Exhibit 2: Balance sheet as at 31.12.20X2 (equity section only)