	Parts:		When will be tested?
part 1	Basics of accounting		
		fin vs mgmt accounting	midterm test 1
		ac cycle	midterm test 1
		ac documents	midterm test 1
		double entry	midterm test 1
		accruals	midterm test 1
part 2	Conceptual framework		
		role of framework	midterm test 1
		role of IFRS	midterm test 1
		fin statements	midterm test 1
		ac policies, estimates, errors	midterm test 1
part 3	Assets		
		PPE	midterm test 1 (will be confir
		Intangible assets	midterm test 2
		Right-to-use asset (lease)	midterm test 2
		Current assets	midterm test 2
part 4	FI		midterm test 2
part 5	Liabilities		
		Provisions	midterm test 2
part 5	Equity		midterm test 2
part 6	Deferred tax		midterm test 2
part 6	FX		midterm test 2

Note: topics for both midterm tests will be also included into final exam

No. of lecture class
lecture 1

lecture 2, lecture 3

lecture 4, lecture 5
-med later)

lecture 6, lecture 7

lecture 7

lecture 7, lecture 8
lecture 8

Part I. Basics of accounting

1 fin vs management accounting

Comparison between financial and management accounting Chapt

	Financial Accounting	Management Accounting
Purpose	Record historic transactions	• assist in controlling the busin operations • planning how the business wi develop • making decisions between alternatives
Audience	External parties – particularly shareholders, lenders and regulators	Internal management and owner the organisation
Legal requirements	• prepare financial statements (in accordance with legal requirements) • prepare accounts for tax authorities	• No legal requirement to prep • No set format for presentatic

Comparison between financial and management accounting (cont.) Chapt

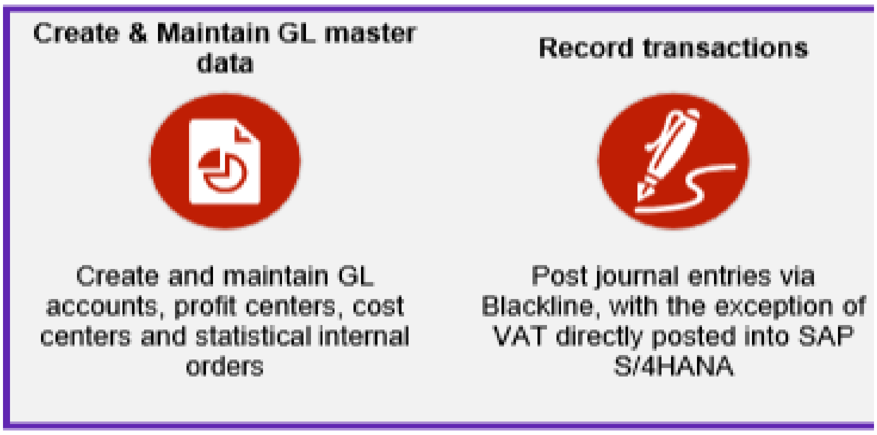
	Financial Accounting	Management Accounting
Format	Must conform to accounting and legal requirements	Presented in such a format as to b easily understood by managers
Perspective	Historic performance (i.e. backwards looking only)	Both future perspective (for planning and decision-making) an historic perspective (for control)
Nature of Information	Almost entirely financial	Both financial and non-financial
Frequency of Preparation	Usually once a year	As often as necessary – daily, weekly preparation or monthly, depending upon the needs of managers.

2 accounting cycle and double entry book keeping

- preparation of fin statements
  - transactions recorded in subledger accounts (e.g.
  - subledger accounts are balanced and closed off in
  - trial balance extracted from GL accounts
  - year-end adjustments made and GL accounts clos
  - trial balance used to prepare financial statements
- books of primary entry (records in subledgers) - are used to update GL ac
  - sales day book
  - purchases day book
  - cash book (cash receipts, cash paymens, petty cas
  - journals
- control accounts (records in general ledger) - are used to prepare trial ba
  - reconciliation (rec)
    - recs - means of checking
    - how to prepare a rec:

suspense accounts (incomplete records)

end-to-end period close includes:



3 accounting documents

Quotation	A written offer to provide goods or services at a particular price. No transaction has taken place yet and therefore nothing is recorded in the accounts.
Sales order	An order note for goods required by a customer.
Purchase order	An order note for goods required from a supplier
Goods received note	A list of goods received from a supplier. Prepared by the recipient business.
Goods despatched note	A list of goods sent to a customer. Prepared by the seller.
Invoice	A demand for payment sent to a customer.
Statement	A document sent to a customer listing all transactions between the business and that customer.
Credit note	A note sent to a customer who returns goods or overpays This reduces the amount owed by that customer.
Debit note	A note sent to a supplier to whom goods have been returned. It is in effect a request for them to issue a credit note.
Remittance advice	A document sent to a supplier alongside any payment sent to them. It details which invoices are being paid.
Receipt	A note to confirm that payment has been received.

Book of prime entry	Transaction type
Sales day book (SDB)	Credit sales
Purchases day book (PDB)	Credit purchases
Sales returns day book (SRDB)	Returns of goods sold on credit
Purchases returns day book (PRDB)	Returns of goods purchased on credit

5 accruals and prepayments

arises when moment of impact on P/L and mome

Cash flow now	Cash flow later

Income statement now		Accrual
Income statement later	Prepayment	

Accrued expense

Db

Cr

Accrued income

Db

Cr

Prepaid expense

Db

Cr

Prepaid income (aka deferred income)

Db

Cr

er 1

ess

ill

's of

oare

on

er 1

oe

d

customer accounts, vendor accounts)

to control/general ledger (GL) accounts (e.g. debtor account, creditor account etc.)

ed off

ccounts

h)

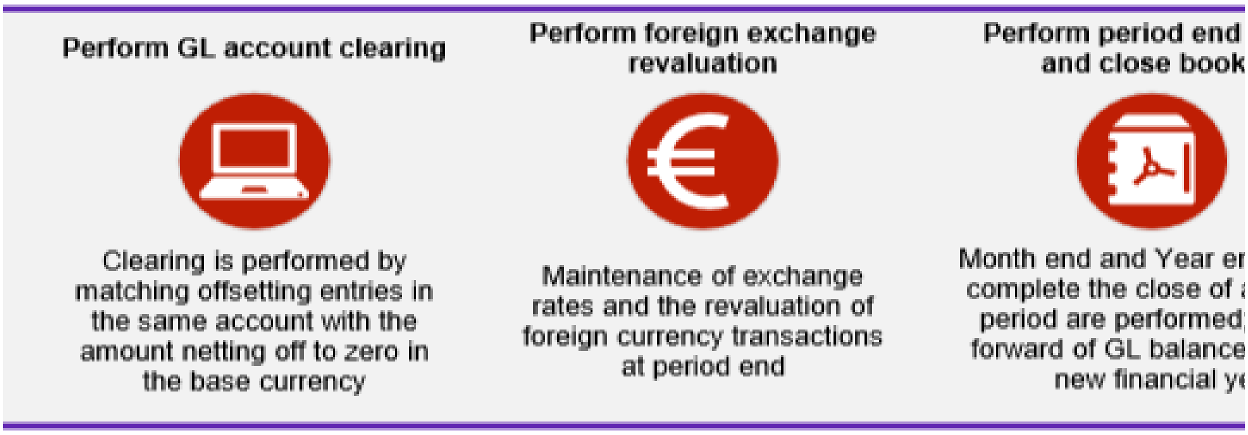
alance

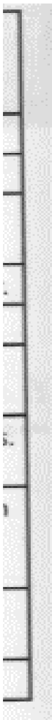
that balancee on the control (GL) account agrees with balance on the ledger account

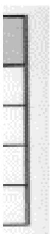
take breakdowns at transaction level of all records from related subledger accounts

compare total amount from breakdown and GL cummulative balance

if two total amount do not reconcile, investigate the variance

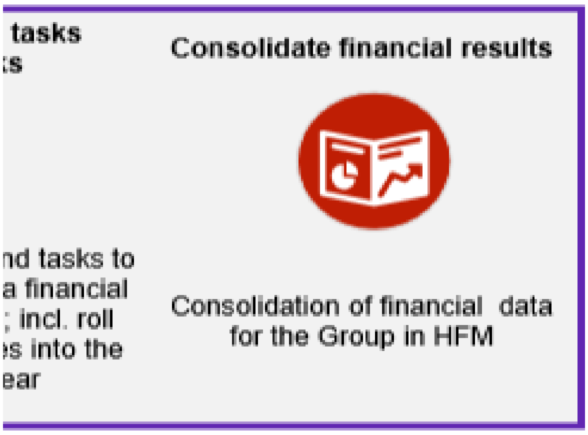






nt of actual cas are not the same:

	release		
Expense (P/L)		Db	Accued expense (B/S)
Accued expense (B/S)		Cr	Invoice received or credit note issu
Accued income (B/S)		Db	Invoice issued or debit note issued
Income (P/L)		Cr	Accued income (B/S)
Prepaid expense (B/S)		Db	Expense (P/L)
Expense (P/L)		Cr	Prepaid expense (B/S)
Income (P/L)		Db	Deferred income (B/S)
Deferred income (B/S)		Cr	Income (P/L)


Consolidate financial results
Consolidation of financial data for the Group in HFM

profit redu

ued to customer (payable) (B/S)

0 impact on P/L when actual expense/income is received

l to vendor (receivable) (B/S)

release of amounts from B/S into P/L

	Expense					Income	
accrued		prepaid			accrued		prepaid
currentliability		profit incre	current asset	profit incre	current asset		profit redu

currentliability

Part II. Conceptual framework

1 Conceptual framework (evidence from IFRS)

Role of Conceptual framework

Conceptual framework can be seen as frame for evaluati

Past history of standard setting bodies thoughout the wo

such standards were often not consistent wit

such standards were intenrally not consistent

standards were produced on 'fire fighting' ba

the same theoretical issues were revised mar

Lack of conceptual framework resulted in creation of rul

Aims of conceptual framework are:

being a basis for evaluation of existing accounting practi

promotion of harmonization if accounting standards by r

assist acountants in dealing with accounting transactions

2 IFRS

IFRS - can be seen as common language for financial reporting which

Advantages of adoption of IFRS

IFRS are widely accepted as a set of high-quality and tran

They were produced in cooperation with other internatio

Companies using IFRS have an enhanced status and repu

International Organization for Securities Commissions (IO

Companies that own foreign subsidiaries will find it easie

Companies that use IFRS will find their results are ore ea

Note! Accounting standards alone cannot provide regulatory framev

IFRS themselves

local company law

local securities exchange regulations

EU directives

local GAAP

Structure of IFRS

IFRS Foundation

IFRS Advisory Council

International Accounting Standards Board (IA

IFRS Interpretations Committee (IFRIC)

Standard setting process

setting the agenda - IASB will add projects to its agenda

project planning - working party is established

development and publication of discussion paper (DP) - i

development and publication of exposure draft (ED) - it i

development and publication of IFRS - when al issues fro

procedures after IFRS is issued - IASB monitors the applic

3 Fin statements

information presented in fin statements - quality characteristics

Information presented in FS should be **useful**

it should be able to influence economic decis

it should be faithful - complete, neutral, free

Usefulness of information presented in FS is enhanced b
- comparable
- complete
- verifiable
- provided on timely basis
- and in compehesive way
- faithful presentation
- free from error (accuracy)

principles/assumptions for preparation of fin statements
- going concern - company will continue its business activi
- accrual/matching - expenses and incomes should be reco
- consistency - methodology for preparation of fin stateme
- materiality - correct level of aggregation of transactions
- substance over form - items recorded in fin statements s
  - where assets are 'sold' at prices that are grea
  - when an asset is leased and used by lessee de
  - in consolidations despite the fact that the pa
  - in case of consignment inventory if risks and
  - a sale and repurchase of maturing goods - wh
- prudence - expenses recorded in fin statements shuld no

elements of fin statements
- asset - resource controlled by the entity as a result of pa
- liability - present obligation arising from past events and
- equity - residual interest in assets after deducting from t
- income - increases in economic benefits in form of enha
- expense - decreases in economic benefits in form of dec

reporting of elements of fin statements
- recognition criteria for elements - an item can be recogn
  - meets the definition of particular element
  - it is probable that any future economic bene
  - item's cost or value can be measured reliably
  - recognition of such items (i.e. assets or liabili
    - that is relevant - If the probability
    - that results in benefits exceeding
- measurement basis for elements (i.e. amounts at which
  - according to methodology how to calculate a
    - at cost (historical evaluation) - all
      - current cost - what the
    - at value (current evaluation) - not
      - fair value (aka market
        - info input c
        - info input c
        - info input c
      - value in use (or fulfilm
      - current cost - it is repl
  - according to application
    - carrying amount (book value) - an

- recoverable amount - amount hig
- revalued amount - amount highe

types of statements

- statement of financial position (balance sheet)
    - current/non-current distinction
        - it will be realized/settled within 1
        - it is held for the purpose of tradin
        - it is part of entity's normal operat
- statement of P/L ad other comprehensive income (incom
    - other comprehensive income may include
        - movements in revaluation surplus
        - gains and losses on equity instrum
        - FX differences
    - exceptional items
        - certain material income or expens
        - smaller exceptional items are not
- statement of change in equity
    - reflects changes in components of company's
        - net incomes (profits) or net expen
        - direct contribution or distribution
        - reclasses (transfers) between disff
- statement of cash flow
    - it highlights the key areas where a business h
    - Good cash management ensures a business h
    - Advantages of cash flow statement
        - cash flow balances are a matter o
        - cash flow balances are objective, u
        - users of fin statements can establ
        - users can identify exactly how cas
        - users can assess the ability of busi
    - Operating cash flow
        - Methods for calculating operating
            - direct - information is
                - Cash sales
                - Cash receiv
                - Cash purch
                - Cash paid t
                - Cash expen
                - cash wages
            - indirect - information i
                - Profit befor
                - Adjustmen

                - (Increase)/

(Increase)/(
Increase/(d
Investment cash flow
(Purchase of non-curre
Proceeds from sale of
Interest received
Dividends received (if i
Financing cash flow
Funds raised - through
Borrowings received
(Borrowings repaid)
(Redemption of issued
(finance costs)
Dividends paid (if in ca
consolidated financial instruments
basic terms
parent - a company that has a con
subsidiary - a company that belon
control
what is control?
one compa
it can be ac
it is irreleva
non-controlling interest (NCI) - a n
associate - a company in which an
significant influence - when a com
consolidation adjustments
general rules:
the legal form here is t
fin statements of paren
all group companies sh
there is a single entity
there are some except
a parent sh
parent's se
consolidated statement of financi
steps in consolidation
cost of inve

if parent is
assets and
share capit
retained ea
proforma

total assets

total equity

Notes:

Elimination

Provision fo

Cost of inve

consolidated income statement

steps in consolidation

group inco

group expe

dividend in

profit attrib

goodwill re

proforma

Notes:

product	
product	
product	non-direct
product	non-direct
product	non-direct
non-product	
non-product	
non-product	
non-product	
other	
other	
other	
other	
other	

events after the reporting period (i.e. after year-end)

an event after the reporting period is the eve

types of events and their impact on fin staten

adjusting events - provide additio

non-adjusting events - conditions

accounting policy and accounting estimates

accounting policy - a set of rules (methodolog

change in accounting policy shou

change in policy should be caused

Note! When company applies new accountin

accounting estimate - professional judgemen

change in estimate should be alwa

change in estimate should be acco

correction of prior period error

correction of prior period error is

correction should be done restros

on of existing accounting practices and development of new ones. It forms theoretical basis for determ
orld indicates that absence of conceptual framework results in production of accounting standards tha
h each other particularly in questions of prudence vs accruals basis
: and often prioritized effect of transaction on P/L in compariosn with effect on B/S
sis, often reacting on corporate scandals rather than being proactive in determining best pracice
ny times in successive standards (e.g. R&D expenses)
es-based system of accounting according to which atment of all accounting transactions shuld be delt w

ces and development of new ones
reducing the number of permitted alternative accounting treatments
s for which there is not (yet) an accounting standard

n first firat created for EU-member states, but soon received wide-world adoption.

nsparent global standards intented to achieve consistency and comparability across the globe
onally renowned standard setters with aim of achiving consesnsu and global convergence
ntation
OSCO) recognizes IFRS for listing purposes. This makes it easier and cheaper tp raise finance in internati
er to consolidate fin statements of all members of tho group if all subsidiaries use IFRS.
sily compared with those of other companies that use IFRS.
work, particulary since in many countries they (IFRS) do not have legal standing. Thus regulatory framew

SB)

on requests of IASB staff members and practicing accountants

t is not mandatory step, but it is oftenly used, especially in case if project addresses a major issue. DP e
s mandatory step. It is a draft of future standard. Comments on it are collected and analyzed and if req
m ED are resolved, final standard is subject to approval by IASB.
cation of new standard and any areas that may need clarification and addresses these when standard is

fundamental characteristics

ion of users of such fin statements (**relevance**)
from error and reflect economic substance of the transaction rather than its legal form (**reliability**)

y if such info is also

enhancing characteristics

ty in the foreseable future
ɔrded in PL in the period when they actually happened regardless of recipt/issue of invoice or cash pay
ents cannot change fro period to period (otherwise information presented in such statements will not l
and items should be applied
hould be recorded according to their economic substance and never according to their legal form. Exa
ter or less than their fair values, substance is applied. Ofthen it is really a secured loan.
espite the fact that the lessor is still the legal owner until fully paid, the lessee behaves like owner. So ir
rent owns only 51% of subsidiary, the entire subsidiary is consolidated (i.e. 100% of subsidiary's assets
rewards of for example motor vehicle despatched from manufacturer to show-room owner are substa
ere the inventory doesn't leave the premise of the seller and sale is to a bank - it is considered a seure
t be underestimated and incomes recorded should not be overestimated. This is often called 'assymet

st event and from which future economic benefits are expected (i.e. there are potencial economic ben
settlement of which is certain and will result in (potencial) outflow of resources embodying economic
hem liabilities => equity = net assets
ncements of assets or decreases of liabilities that result in increase in equity other than by controbutio
reases of assets or increases of liabilities that result in decrease in equity other than by distributions to

ized as element of fin statements (i.e. recorded in fin statements as such) if it:

its associated with such item will inflow or otflow from the entity

ties) provides users of fin statements with information
of the event is low, this may not be the most relevant information. The most relevant information may
the cost of providing that information
elements are recorded in fin statements):
nd economic substance
input info is available but it can be outdated
asset cost to purchase less any depreciation or amortization. It is exit value
all input info may be available (thus actuals can be substituted with estimates), but up to date
value) - it is an estimate of what the asset could be sold for (if certain conditions are met). Thus it is exi
of level 1 - quoted price: identical items at active market
of level 2 - observable inputs: similar items at active/inactive market
of level 3 - unobservable inputs: best info available e.g. valuation models
ent value for liabilities) - it is present value, which is an estimate of discounted future cash flow which
acement cost, which is an estimated cost to buy an identical item or construct/produce it at current pri

ount at which item is recorded in evidence

;her of either the asset's **future** value for the company or the amount it can be sold for, minus any tran
›r of either the asset's **present** value for the company or the amount it can be sold for, minus any trans

2 months of the reporting date or
g or
ing cycle
ıe statement)

;
ıents classified as financial assets measured at FV through othercomprehensive income

›e items, known as exceptional items, may be listed on the face of income statetemnts before profit fr
disclosed in income statement but instead within notes to accounts, normally the operatingprofit note

; equity due to
ıses (losses) generated during busoness activity of the company
s of equity components by/to business owners
ferent components of equity

ıas generated and spent cash.
ıas sufficient cash to run its day to day operations.

f fact and are not distorted by accounting policies (adjustments, estimates, accruals etc.)
unlike profit which is subjective.
ish how business has generated cash.
h has been spent.
iness to generate cash in the future.

; cash flow
extracted from ledger accounts (not just fin statements), mainly from bank accounts (cash flow picture

ved from credit customers
ases
o credit suppliers
ıses
; and salaries
is extracted from fin statements (cash flow picture is reconciled from fin stataments) => used by extern
re tax
t for non-cash items
depreciation/amortization
loss/(profit) on disposal of non-current assets
finance costs - it needs to be added here because it will be deducted in the part of Financing cash flow
(investment income) - it needs to be dedcuted here because it will be adde back in part of Investing ca
decrease in inventory

decrease in receivables
lecerase) in payables

ent assets)
non-current assets

in cash)

ı issue of financial instruments

financial instruments)

sh)

ıtrolling interest in another company, giving it control of its operations.
gs to another company, which is usually referred to as the parent company. Subsidiary's fin statatment

ny has power over another when it has the ability to direct that company's business activities, which si
chieved simply by owning a majority or voting shares or it may come from contractual arrangements
ınt wether a parent company uses its ability to direct business activity of subsidiary, what is important
ninority interest; it is an ownership position wherein a shareholder owns less than 50% of outstanding
ıother company owns a significant portion of voting shares (aka 'significant interest'), usually 20–50%. I
ıpany holds approximately 20% to 50% of a company's stock, it is considered to have significant influen

wo separate companies but the economic reality is single entity and that must be reflected in the met
nt and subsidiary used in the consolidation should have the same year end. If subsidiary has different y
ıould have the same accounting policies. This may require adjustments to subsidiary's figures.
concept: all intergoup transactions between the parent and subsidiary should be cancelled out becaus
ions from consolidation:
ıouldn't prepare consolidated fin stataments if it itself is wholly-owned subsidiary
curities are not publicly traded and it is not in the process of issuing secutiries
al position

estment into subsidiary shown in parent's BS is canceleld against subsidiary's share capital and pre-acqu
if difference is positive, then goodwill is recognized as intangible asset, which is not amortized but mea
if difference is negative, then goodwill is credited to consolidated income statement.
Note! Inherent (non-purchased) goodwill should never be included into BS
not purchasing 100% of subsidiary, then NCI is recognized
liabilities of parent and subsidiary are combined on line-by-line basis (except group receivables and pa
al presented in BS is only that of parent (because the one of subsidiary was already cancelled at prior s
ırnings are parent's retained earnings plus subsidiary's post-acquisition retained earnings

Adjustmen

non-current assets			1 Goodwill ac
PPE	100% P + S		
goodwill	see adjustments No. 1		
current assets			
stock	100% P + S		
receivables	100% P + S (BUT except intra-group balances)		2 NCI adjustr
bank and c	100% P + S		
;			
equity			
share capit	100% P		3 Consolidate
retained ea	see adjustments No. 3		
NCI	see adjustments No.2		
non-current liabilities	100% P + S		
current liabilities	100% P + S (BUT except intra-group balances)		
/ and liabilities			

ı of intra-group balances

group accounts should only show balances with parties outside the group. If intra-group balance exists

Db Group payable

Cr Group receivable

or unrealized profit (PUP)

companies within a group have made sales to one another at a profit, yet the goods traded between s

If there is intra-group sales but all goods have subsequently been sold outside the group i.e. nothing is

If there is intra-group sales and not all goods have subsequently been sold outside the group i.e. some

from P to S - debit Group sale, credit Group COS of such inventory, credit Group inventory.

from S to P - debit Group sale, credit Group COS of such inventory, credit Group inventory.

from S to S - debit Selling entity's sale, credit Selling entity's COS of such inventory, credit P

estment

ways how to structure the deal:

to purchase shares in subsidiary for cash

to purhase shares in subsidiary and give them paranet's own sahers in return (known as sh

if share exchange is the case how transaction price is paid, then the cost of investment is determined i

work out number of shares acquired in the subsidiary

calculate how many parent's shares will be issued in return (what is the ration between sha

calculate the value of parent's shares by multiplying by the parent share price at acquisitio

me = parent's income + subsidiary's income (as all income is controlled by the group)

nses = parent's expenses + subsidiary's expenses (as all expenses are ontrolled by the group)

come from subsidiary which is shown in parent's income statement, should be cancelled in consolidate

outable to NCI is calculated as: NCI% * subsidiary's profit after tax adjusted for consolidation purposes (

cognized as result of business combination in consolidated balance sheet should be tested for impairm

if full goodwill is impaired - loss is shared between the NCI and the group in the same ratio as subsidia

if proportionate goodwill is impaired - loss is assigned only to the group reservesin group's share on su

Mid-year acquisitions of subsidiary

we must include into consolidated business result only that part of subsidiary's business re

Elimination of intra-group trading

an adjustment shuld be made to reflect intra-group sales revenue: such revenue should be

Db	Group sales
Cr	Group COS

If there is intra-group sales but all goods have subsequently been sold outside the group i.e

Accounting treatment of associate (equity methond)

investment into associate is initially recognized at cost in the group BS and the carrying am

investor;s share of profit or loss of investee is recognized in the group income statements a

till revenue		Adjusteme
direct COS	transaction margin	Adjusteme
transaction margin		
supplier rebates		
product WOFs/WONs	non-transaction margin	
product returns		
non-transaction margin		
product margin		
services sold to customers		
direct COS	non-product margin	
bad debt expense		
credit cards commissions		
non-product margin		
marketing costs	operating expenses before gross margin	
distribution costs		Extra line: l
Gross margin		
property costs	operating expenses after gross margin	
payroll costs		
overheads		
		Extra line: p
Operating profit		
Finance costs		
Profit before tax		
Income tax expense		
Profit after tax		

Discontinued operations	Extra line: l
Profit for the year	

nt that occurs between the accounting year end and the date on which the fin statements are authoriz
nents
nal evidence of conditions that existed before/at year-end date => fin statements need to be adjusted
that did not exist before/at year-end date => fin statements shouldn't be adjusted to include the impa

gies) for fin reporting applied by business
ld be applied retrospectively i.e. adjustment should be done to at least one period (fin year) from the p
l by change in environment of the business (external or internal)
g policy for the first time, it is not a change in exisitng policy, but first-time adoption of new one. Thus
t done by accountant when actual amount is not available e.g. duration of useful life of non-current as
ays based on new information which was not available before (i.e. in the moment when original estima
ounted prospectively i.e. starting from the current period

always based on information which was available before (i.e. when original estimate was done or actu
pectively i.e. in the period when the error happened.

ıining how transactions should be measured (historcial value or current value) a
t have serios drawbacks:

vith by detailed specific rules or requirements. Such system is very prescriptive a

ional markets.

work of juresdiction may include all of the following:

ɜxplains the issue and possible accounting solutions and invites to comment
ɥuired ED is amended and re-exposed.

s revised.

Conceptual
IFRS
Fin stateme

ments
be comparable between periods)

mples

n case of such lease - fin lease - lessee is user of leased asset during the assets e
are added to parent's assets). Legally the parent may own 51% only but in day-t
ntially with the showroom owner then the showroom owner must treat it as of i
d loan. Legally title mayhave passed to the bank but linking the two transaction
ric prudence'.

efits)
benfits

n from equity participants. Note: some types of ncome are required tobe directl
equity participants

y be about the potential magnitude of the item, the possible timing and the fact

it value focusing on the values which will be gained from the item. Methogology

is expected to be generated by the asset
ices. It is entry value.

ısaction costs. It is used for comparison with carrying amount in **cases of impair**
ıaction costs. It is used for comparison with carrying amount in **cases of revalua**

om operations
e.

is actual) => used by internal users who have access to management accounts

al users who do not have access to management accounts

; otherwise it will be double counted: (1) as part of Profit before tax; (2) as part
ısh flow' otherwise it will be double counted: (1) as part of Profit before tax; (2)

ts are consolidated with fin statements of the parent.

ignificantly affect investee's returns

is that it has the ability to do so.
shares and has no control over decisions.
In this case, parent company does not consolidate the associate's financial state
ıce

thod of consolidation.
rear end date within 3 months of that of the parent then the fin statements can

e they took place within the same entity and only transactions with the outside

uisition retained earnings. Any difference between the two offseting amounts (i.
asured at its historical cost and tested for impairment annualy.

yables)
tep against parent's investment into subsidiary)

ts to BS

djustments - **net total** value acquired | Substance of adjusting entries:
investment at cost | price paid for consolidation
NCI at FV at acquisition date | price paid for consolidation
(Net assets at FV at acquisition date) | value acquired from consolidatior

nents - **total** value
NCI at FV at acquisition date | amount before consolidation
NCI % in post acquisition reserves of subsidia | impact of consolidation

ed reserves - **net total** value acquired
100% of reserves of parent at year-end | amount before consolidation
group % of post acquisition reserves in subsic | impact of consolidation
(PUP adjustment (P sells to S)) | remove double counting

s between parent and subsidiary then an adjustment should be made in group a

uch companies remain within the group at the reporting date, this creates 'unre
in the inventory at the year-end, there is no PUP
inventories acquired in IC transaction are left is in the inventory of the Group a
By reversal of profit margin of the Group we are basically debiting its Reserves/
By reversal of profit margin of the Subsudiary we are basically debiting its Net a
urchasing entity's inventory (at difference between market price and transfer pı

are exchange)
in the following way:

ares subsidiary's share acquired and parent's shares given away)
n

ed income statement (because single entity doesn't pay income to itself)
(see PuP adjustment)
ent annually.
ry's profit for the year
ıbsidiary's profit for the year

sult that arose after acquisition i.e. whilest under the control of the parent. If th

deducted from total consolidated revenue. The same should be done for COS: t

e. nothing is in the inventory at the year-end, show only cancellation of intra-gro

ount is increased/decerased to recognize the investor's share of profit or loss of
as a single line entry.

nt: less intra-group sales (reversal; if it is vertical IC transaction)
nt: less intra-group purchases (reversal; if it is vertical IC transaction)

ess unralized profit in inventory

plus admin expenses

Db	BS - as getting new res
Cr	CF statement - as outfl
Db	CF statement - as inflo
Cr	BS - as taking out an ex
Cr/Db	P/L - as result on dispo

ess unralized profit in non-current assets

:ed for issue

to include the impact of such event
ct of such event. EXCEPTION: going concern is the only exception

›ast.

no retrospective adjustments are needed for this new policy.
set, likelihood of collection of aged debt from customer, expected amount of de
ıte was done)

al was calculated)

ınd reported - i.e. how transactions are presented and communicated to users of fin st

and inflexible but has the attraction of fin statements being more comparable and con

l framework

ents
quality characteristics of information
underlying assumptions for preparation of fin statements
elements of fin statetments

reporting of elements of fin statements(recognition and measurement)
types of fin statatments

consolidation of fin statements
events after reporting period

:conomic life: lessee capitalizes it at cash price, depreciates etc.
o-day economic reality the parent can control the entire subsidiary.
it is its inventory even though legally they belong to manufacturer until paid for
; together, it is inventory of seller.

ly recognized in equity (not through P/L first) e.g. revaluation gains on assets go straigh

:ors affecting the probability.

' how it should be determined:

ment testing
tions (write downs or write ups)

of Financing cash flow
as part of Investing cash flow

Amount of investment:	Classification of investment
<20% of ordinary shares of acquired entity	**investment**
20-50% of ordinary shares of acquired entity	**associate**
>50% of ordinary shares of acquired entity	**subsidiary**

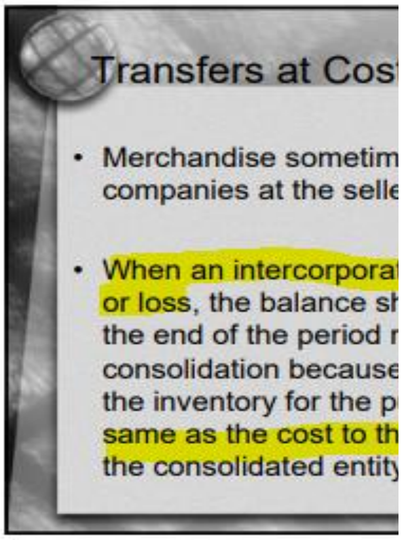
ement

be used with adjustment for any significant transactions in the 3 month period. if the

world must be recorded in the consolidated accounts.

.e. balancing figure) is recognized as goodwill

ו



ccounts in order to cancel the respective balance.

alized profit'.

t the year-end, there is PUP and adjustments to IC accounts are needed. The type of a
retained earnings)
ssets at NCI% => we are debiting NCI
rice if transfer price was higher i.e. profit) between controlling and NCI.

e acquisition occurred in the middle of the year, we should only include the second ha

:hey need to be deducted from total COS.

›up tarding (i.e. cancelation of intra-goup sales and COS) but nort PUP.

ᶠ investee after date of acquisition.

.ource for the business
low of cash

w of cash
‹isting resource from the business
›sal

elivery costs from 3d party (cost accrual) atements

ısistent.

Many standards, such as International Accountir
Liabilities and Contingent Assets, apply a systen
outflow of economic benefits would be recognise
would only be shown as a contingent asset and
Therefore, two sides in the same court case cou
the likelihood of the pay-out being identical for e
asymmetric prudence as necessary under some
of the term was required. Whilst this is true, the
should not identify asymmetric prudence as a ne
reporting.

The 2018 Conceptual Framework states that the
asymmetry, such as the need for more persuasi
than liabilities. It has included a statement that, i
may sometimes arise as a consequence of requ

nt to reserves which are part of equity.

A key change to this is the removal of a 'probab
financial reporting standards apply different crit
virtually certain and some reasonably possible.
prohibit the recognition of assets or liabilities wi
economic resources.

The first of the measurement bases discussed is
is unchanged, but the Conceptual Framework no
financial items held at historical cost should be a
form of depreciation or amortisation). Alternativel
that the historical cost is no longer recoverable (i

cost should reflect subsequent changes such as
often referred to as amortised cost.

Method of accounting to be applied

cost method. Cost is measured at fair value. Two sides of the deal remain as two **independent companies**. N

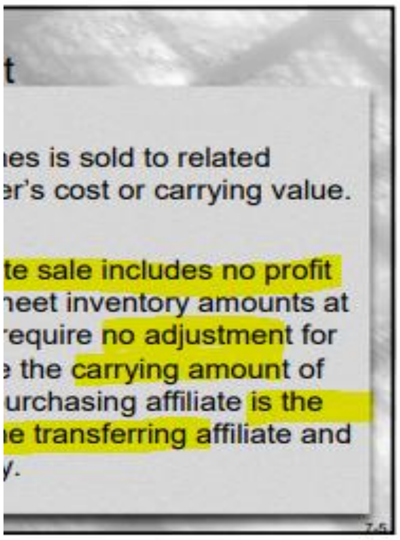
equity method of accounting. Use of equity method is based on assumption that investor has a significant in

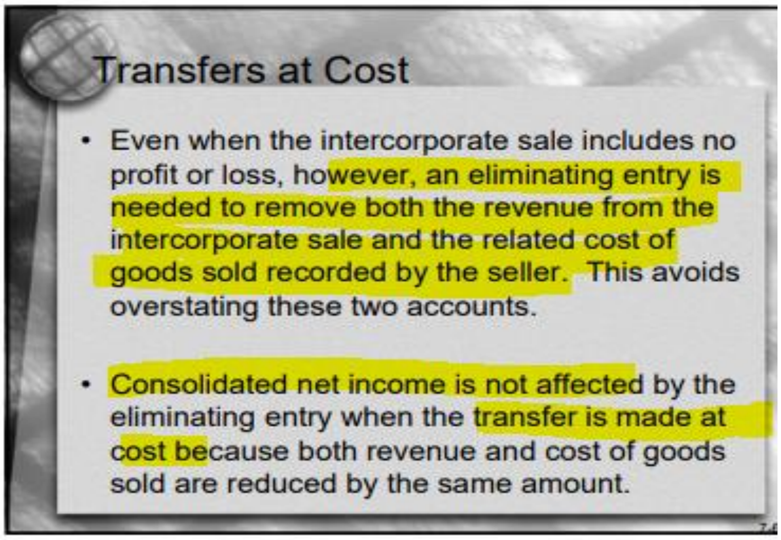
consolidation method of accounting for such investment. Use of consolidation method is based on assumpt

0%	**20%**	
	investment	
		associate

period is greater than 3 months, then the draft fin statements for the subsidiary must be prepared for the pu

https://www.ocf.berkeley.edu/~cchang/pdf%20docs/ch007.pdf





djustment depends on direction of original IC sale of inventory: from P to S (downstream IC transaction), fron

What is pup in accounting?

The second step here is to identify the pro
although we refer to this as a provision, it i
asset, inventory.

ılf of the subsidiary's result for the year

ıg Standard (IAS®) 37, *Provisions, Contingent*
n of asymmetric prudence. In IAS 37, a probable
ed as a provision, whereas a probable inflow
merely disclosed in the financial statements.
ıld have differing accounting treatments despite
ither party. Many respondents highlighted this
e accounting standards and felt that a discussion
Board believes that the Conceptual Framework
ecessary characteristic of useful financial

e concept of prudence does not imply a need for
ve evidence to support the recognition of assets
in financial reporting standards, such asymmetry
ıiring the most useful information.

bility criterion'. This has been removed as different
erion; for example, some apply probable, some
. This also means that it will not specifically
ith a low probability of an inflow or outflow of

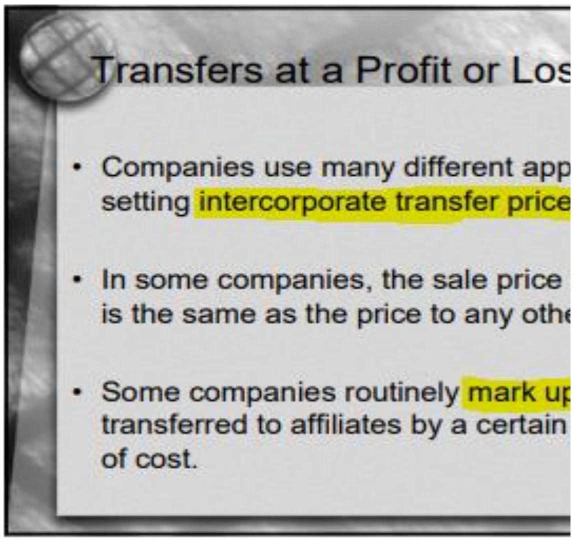
historical cost. The accounting treatment of this
w explains that the carrying amount of non-
djusted over time to reflect the usage (in the
y, the carrying amount can be adjusted to reflect
mpairment). Financial items held at historical

interest and payments, following the principle

/inority interest (NCI) in the FS of investee belongs to investing company.
ıfluence over the investee (purchased company). Two companes - investing company and associate - car
ion that investor exerts a full control over the investee (purchased company). Two companes - parent cc

50%	100%
	subsidiary

rpose of consolidation



n S to P (upstream IC transaction), from S to S (horizontal IC transaction)

vision for unrealised profit (**PUP**). Note
is not a liability but an adjustment to the

ı become together **a joint venture**. Minority interest (NCI) in the FS of investee belongs to investing co
ımpany and subsidiary - become together a group. Minority interest in the FS of investee belongs to 3d

ss

roaches in
s.

to an affiliate
er customer.

inventory
percentage

7-7

Transfers at a Profit or Loss

- Regardless of the method used in setting intercorporate transfer prices, the elimination process must remove the effects of such sales from the consolidated statements.

- When intercorporate sales include profits or losses, there are two aspects of the workpaper eliminations needed in the period of transfer to prepare consolidated financial statements (see next two slides).

7-8

mpany.
l party as parent company is majority owner.

First Aspect: Income Statement Focus

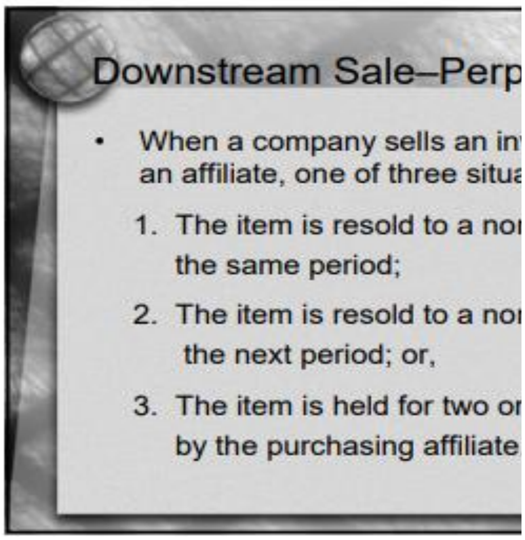
- Elimination of the income statement effects of the intercorporate sale in the period in which the sale occurs, including the sales revenue from the intercorporate sale and the related cost of goods sold recorded by the transferring affiliate.

7-9

Second A

- Elimination
sheet of an
sale that ha
the invento

DOWNSTREAM STOCK SALE (from P to S)



spect: Balance Sheet Focus

from the inventory on the balance
y profit or loss on the intercompany
as not been confirmed by resale of
ry to outsiders.

1. Profit Realized in Sa

- Required Elimination Entry:

Sales $1

Cost of Goods Sold

- Note the elimination entry do
consolidated net income bec
cost of goods sold both are r
same amount. [Continued o

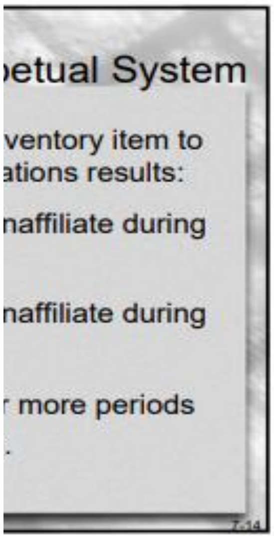
2. Profit Realized in Ne

- When inventory is sold to an aff
and the inventory is not resold d
period, appropriate adjustments
prepare consolidated financial s
the period of the intercompany s
subsequent period until the inve
a nonaffiliate. [Continued on ne

3. Inventory Held Two or

- Companies may carry the cost
purchased from an affiliate for
accounting period. For examp
an item may be in a LIFO inve
would be included as part of th
balance until the layer is liquid

- Prior to liquidation, an eliminat
needed in the consolidation w
time consolidated statements
restate the inventory to its cos
consolidated entity.


etual System
ventory item to
ations results:
naffiliate during
naffiliate during
more periods
7-14

me Period

0,000
$10,000
es not effect
ause sales and
educed by the
n next slide.]

7-15

1. Profit Realized in Same Period

- No elimination of intercompany profit is needed because all of the intercompany profit has been realized through resale of the inventory to the external party during the current period.

7-16

xt Period

iliate a profit
luring the same
are needed to
tatements in
sale and in each
ntory is sold to
xt slide.]

7-17

2. Profit Realized in Next Period

- By way of illustration, assume that Peerless Products purchases inventory in 20X1 for $7,000 and sells the inventory during the year to Special Foods for $10,000. Thereafter, Special Foods sells the inventory to Nonaffiliated Corporation for $15,000 on January 2, 20X2.
- Required Elimination Entry (20X1):

Sales	$10,000	
Cost of Goods Sold		$7,000
Inventory		$3,000

7-18

More Periods

t of inventory
more than one
le, the cost of
ntory layer and
e inventory
ated.

ing entry is
orkpaper each
are prepared to
t to the

3. Inventory Held Two or More Periods

For example, if Special Foods continues to hold the inventory purchased from Peerless Products, the following eliminating entry is needed in the consolidation workpaper each time a consolidated balance sheet is prepared for years following the year of intercompany sale, for as long as the inventory is held:

Retained Earnings, January 1	$3,000	
Inventory		$3,000

Eliminate beginning inventory profit.

7-19

7-20

UPSTREAM STOCK SALE (from S to P)

HORIZONT

Upstream Sale – Perpetual System

- When an upstream sale of inventory occurs and the inventory is resold by the parent to a nonaffiliate during the same period, all the eliminating entries in the consolidation work paper are identical to those in the downstream case.

Upstream Sale – Perpetual System

- When the inventory is not resold to a nonaffiliate before the end of the period, work paper eliminating entries are different from the downstream case only by the apportionment of the unrealized intercompany profit to both the controlling and noncontrolling interests.
- The elimination of the unrealized intercompany profit must reduce the interests of both ownership groups each period until the profit is confirmed by resale to the inventory to a nonaffiliated party.

AL STOCK SALE (from S to S)

ale from One Subsidiary to Another

ransfers of inventory often occur between ompanies that are under common control or wnership.

Vhen one subsidiary sells merchandise to nother subsidiary, the eliminating entries are dentical to those presented earlier for sales rom a subsidiary to its parent.

he full amount of any unrealized intercompany rofit is eliminated, with the profit elimination llocated proportionately against the ownership nterests of the selling subsidiary.

Lower of Cost or Market

- Inventory purchased from an affiliate might be written down by the purchasing affiliate under the lower-of-cost-or-market rule if the market value is less than the intercompany transfer price. [Continued on next slide.]

Lower of Cost or Market

The subsidiary writes the inventory down from $35,000 to its lower market value of $25,000 at the end of the year and records the following entry:

Loss on Decline in Value of Inventory	$10,000	
Inventory		$10,000

Write inventory down to market value.