Accounting

Operation accounting: employees salaries & deductions, inventory prices, day to day. Largest collection of information

Financial Acct: info intended for mgmt, shareholders, banks, govt, etc.. - used for financial reporting

Management acct: used for 3 managerial functions
- planning
- implementation
- control

Tax acct: using tax rules which differ from financial reporting rules & mgmt Acct principals.

CPA: Chartered Professional Accountant: all subfamilies of acct roll up into CPA
- CA.
- CMA: Certified management Acct
- CGA: Specialized in financial Accounting

XBRL: extensible Business Reporting Language: digital business language designed to standardize financial statement data transmission

Acct is ran by principals, not rules. Set by humans, they require
- Relevance
- Objectivity
- Feasability

Acct
NPOO

GAAP: Source of Acct principals.

FASB: Financial Acct Standard Board → Set GAAPs.

Companies not forced to follow GAAP but strongly recommended to do so

IFRS: International Financial Reporting Standards
Set by the IASB - international Acct. Standards Board

Sarbanes Oxley: instored in july 2002, requires CEO & CFO of public companies to certify that statements filled w/ SEC are materially accurate, complete & ~~reflect~~ present fairly financial condition & results of issuer

Status Report: snapshot @ point in time: ⇒ Balance Sheet
Flow Report: Activity over a period ⇒ Income Statement, CF Statement

Chapter 4

Account: Device used to calculate net change in an item

Permanent Account: aka real account, records items on balance sheet & balances are carried forward into next period

Temporary accounts: established for each Revenues & expenses to avoid cluttering retained earnings. Accounts summed up to create income statement. @ end of period, balances transfered to R.E. So always Ø @ begining

Acct
NPO.1

Ledger: Book w/all the accounts, sometimes called General Ledger or GL

Subsidiary ledger: Sub-ledger to contain more details & avoid cluttering the ledger. Ex: AR/AP w/details of collection/payment or Inventory

Chart of Accounts: list of all accounts, established by mgmt.

Debit: left side of an account
Credit: Right side of an account

Book keeping double entry: for each transaction, Dr = Cr.

expenses.

Revenues

Assets		=	Liability		+	Owner's Equity	
+	−		−	+		−	+
Dr	Cr		Dr	Cr		Dr	Cr

unpaid expense

unearned revenue

Revenues are credits
Expenses are debits.

Revenues	
−	+
Dr	Cr

Expenses	
+	−
Dr	Cr

Journal: Records all transactions.

Accounting Process.

1. Analyse transactions
2. Journalyse original entries
3. Post journal entries to ledger, organized by Account
4. Identify, journalize & post adjusting entries
5. Journalize & post closing entries/close temp. Accounts.
6. Prepare financial statements.

ACCT
N
p0.3.

Adjusting entries: Non systematic charges. ex: Accrued salaries on Dec 31st

Contra Account: Account that reduces another ex: Depreciation or provisions for bad debt

Funky transactions.

4.2 2 Sales discount allowance were 34150
dr Sales discount & Allowances
cr Provisions for Sales discount & Allowances.
Sales disc & allowances is a deduction from gross sales to arrive @ net sales. The provision is a liability

4.2 3- A loan for 3500 @12% is still owed by an employee.
Dr Interest receivable 35
Cr Interest income
Interest income will be listed under "Other income" in the I/S.

4.2 4 Depreciation expense was 13 600
Dr. Depreciation Expense
Cr. Accumulated dep
Depreciation expense is an income statement item

4.2 5 Customer paid for services he will receive in future.
Dr. Cash
Cr. Deferred Revenues

4.2 6 Estimated increase of 1350 in bad debts.
Dr. Bad debts expense
Cr Allowance for doubtful Accounts
contra Account for AR

Acct
N
pg. 4

Ruling & balancing: Sub total transactions in permanent Accounts. Put a double rule to indicate that all above transactions have been counted.

ex)

Cash	
0	750
5000	250
5000	1000
4000	

Trial Balance: list of account names with balances of each account

Purpose: Shows equality of Dr & Cr (i.e. integrity check)

provides a summary for making adjusting entries & prep statements.

Adjusting entries: Unlike original entries, do not come w/supporting objective documents. They modify balances to better reflect reality. Types:

- Recorded costs related to 2+ periods. (ex: insurance)
- Unrecorded (Accrued) expenses (ex. wages, bad debt)
- Recorded revenues related to 2+ periods (ex: rent)
- Unrecorded revenues (ex: interest earned but not paid)

continuous transactions ex: fuel inventory

ex:

Buy a 2y. insurance policy

Prepaid ins	
1500	

Cash	
	1500

Adjustment

Prepaid ins	
1500	750

ins. Expense +	−
750	

Buy 10k equipment, depreciate 5y, sv = 0.

Equipment	
10000	

Cash	
	10 000

Adjustment

Allowance for dep.	
	2000

Depreciation Exp. +	−
2000	

ex) Rent collected 1st month @ 600

Rent Revenue	
600	

Unearned Rent Rev	
	600

Make 120$ of interest but not paid.

Accrued interest Receivable	
120	

Interest Revenue	
	120

Acct

N

p.05

Closing Entries. Temporary Rev. & Expenses are sub divisions of owner's equity (R.E).

Closing Sales Revenues.

Sales Revenues

12 200	12 000
	200

closing entry

Balance 12200

Income summary

	12 200 ← from closing sales.

Closing Cost of Sales.

Cost of sales

6000	6000 ← closing entry

→

Income Summary

6000	12200

Closing Income summary to R.E.: After closing all temp. Accounts (except tax expenses) to income summary, close it to Retained earnings.

Income Summary

sub total → [...] 10 290	12 200
calculate tax → 382	
closing entry → 1528	1528

Income tax liability

	382

R. E

	1 528.

Acct
N
P-06

Chapter 2 - Balance Sheet

① Money measurement: in financial Acct, records is made of only info that can be expressed in monetary terms. Money is expressed in terms of its value @t when entered in the books (No track of inflation)

② Entity Concept: Organization on activity for which Acct. reports are prepared. ⇒ How do accounting events affect the entity.

③ Going Concern: Assume entity will continue to operate for an indefinetly long period in the future (i.e. do not tag liquidation value for items in supply chain)

④ Cost concept:
- Non monetary assets are recorded @ cost, not @ fair value
- Monetary assets: initially recorded @ costs then accounted for in fair value.

⑤ Dual Aspect: Assets = Liability + Owner(s) Equity
Every transaction has dual impact ⇒ Balance Sheet

⑥ Account Categories: Items are grouped into categories so that individual items ressemble each other & items in one cat are different than from another (No fixed category definition)

Balance Sheet
Canada GAAP: most liquid Asset on top
US/IFRS: most liquid Asset on bottom

ACCT
N P07

Current assets: Assets that are expected to be realized in cash or sold or consumed during operating cycle of entity or a year

- Cash
- Marketable Securities: investments that are readily marketable & expected to be converted to cash within a year
- Accounts Receivable: Owed by customers, typically adjusted for doubtful accounts. (AFDA: Allowance for Doubtful Accounts)
- Notes/Other receivable: Owed by others than customers ⇒ written Note to pay w/interest
- Inventories: Goods that will be sold in regular course of business
- Prepaid expenses: Assets, usually intangible, whos usefulness will expire in the near future. (ex: prepaid Rent or insurance)

Fixed Assets (a.k.a Property, plant & equipment): tangible assets that are long lived [land is not depreciated))

Other assets

- Investments
- Intangible assets: goodwill, patents, copyrights, trademarks

Liabilities: obligations to transfer assets or provide services to outside parties arising from events that have already happened past transactions. Claims against assets in general otherwise specified (mortgage, LTD)

ACCT
N202

Current liabilities: expected to be satisfied or extinguished during normal operating cycle or a year.

- Accounts payable: claims of suppliers
- Notes payable: Amounts owned to FIs.
- Taxes payable: amount owed to govt. agencies for taxes.
- Accrued expenses: Amounts earned by outside parties but not yet invoiced or paid (ex: interest/wage payable)
- Deferred revenues: Advanced pmt received for a service due (ex: subscriptions)
- Current portion of LTD: LTD portion due <12 months.

Owner's Equity: Amount owners have in the entity (SHE).

- Prepaid in Capital (aka contributed capital): Amount invested directly in company
  - Capital Stock: shows par values & # of outstanding shares
  - Additional paid-in capital: $ when investors paid more than par value
- Retained earnings: Difference between total earnings since inception & total dividends pain over entire life. If <0, called deficit.

  In proprietorship, one line w/ owner's name.

  In partnership, separated by partners, might have Drawings if payouts by partners.

Current ratio = current assets / current liabilities

Unincorporated Business

- Proprietorship: one owner
- Partnership: use capital account per partner (drawings = withdraws)

ACCT

~pg9

Chap 3 - Income Statement

Basic Consepts.

(6) Accounting period: Accounting measures activities over intervals of time called accounting period. (typically 1 year)

SEC requires quarterly interim reports.

Revenue: increase in RE associated with operations
Expense: decrease; outflow/consumption of ressources to generate revenue
Net income/loss: Revenue - Expense

Share holder's equity = paid in capital + Retained earnings.

(7) Conservatism (when revenue is recognized)
- Recognize revenues only when they are reasonably certain
- Recognize expense as soon as they are reasonably possible

ex: recognize revenue from sales of goods only when shipped, or services only when performed.

Unearned (percolated) revenues: liability of goods/services already paid but not yet shipped/performed.

Accrued revenues: have been earned but not yet paid
ex: interest on a loan

(8) Realization: Amount of revenue that should be recorded.
ex: Allowance for doubtful accounts
Sales returns & allowance
Sales discounts.

Acct
Np 10.

⑨ <u>Matching consept</u>: when a given event affects both revenues & expenses, the effect of each is recorded during the SAME accounting period.

Expense terminologie
- Cost: monetary measurement of amount of ressources used for some purpose
- Expenditure: Decrease in asset (usually cash) or increase in a liability
- Expense: Cost applicable to the current period.
- Disbursement: payment of cash

Expenditure take place when an entity aquires goods or services, either made in cash or increased liability

Types of expenditures
1- Expenditure made this year for expense incurred this year
2- Expenditure made in previous year for expense incurred this year
   Assets that become expenses. Ex:
   - Inventories
   - Prepaid expenses (deferred charges)
3- Expenditures that are not yet expenses
   ex: production wages & salaries, purchase inventories
4- Expenses not yet paid.
   ex: accrued wages, interest

Dividend: not expenses; reduce cash & RE.

Gains/Losses: increases/decreases in RE not associated w/ operations

Acct
Npll.

(10) - Consistency consept: once accounting method is selected, use it for all subsequent events of same character.

(11) Materiality consept: "de minimis non curat lex" the court will not consider trivial matters.
Insignificant events may be disregarded but there must be full disclosure of all important information

Income Statement

a.k.a. PnL, statement of earnings/operations.

Heading: Entity name, name of statement & period covered

- Revenues/Sales: invoice price of goods shiped/services rendered
  excluded: taxes, freight/postage, trade discounts.
- Sales returns & allowances: value of goods returned & allowances for deffective goods
- Other revenues: rev. not associated w/ sales ex: interest

Expenses:
- Cost of goods sold.
* Gross margin/Gross profit = Revenues - CoGS.
- Selling, general & administrative expenses charges.

] operating income

Disclosed Separately
- Research & Development
- Interest Expense

] income before taxes.

Provision for income tax

Net income.

Acct
Np 12.

Gross sales
- Sales returns & Allowances
- Sales (cash) discounts
Net sales

Net Sales
- Cost of goods Sold
Gross Margin

Operating income
-other Expenses
+other revenues
Earnings Before taxes
- taxes
Net income

Chap5 Revenues & Monetary Assets.

Revenue Recognition → When? How much?
- The entity has substantially performed what is required to earn the revenue
- The amount of income can be reliably measured
- Related assets received can be easily converted to cash

IFRS - Revenue Recognition
- Risks & rewards of ownership are transfered to buyer
- Seller no longer has material involvement
- Amnt of revenue can be reliably measured
- Probable that seller will recieve revenue
- Cost of transaction can be reliably measured.

Acct
Np13.

SEC - Revenue Recognition

- Persuasive evidence of an order
- Delivery occured &/or service is performed
- Fixed or determinable sales price
- Colletibility of sale is reasonably assured.

Delivery method for recognizing revenus (most common)

- Product is @ customer's place of business
- No uncertanty about customer's acceptance of product
- Seller has substantially completed terms of P.O.
- For licensing; licensing terms have begun

Consignment: consignor ships goods to consignee who attempts to sell them

dr. Inv. in consignment	1000		Ship to consignee	
cr. Merchandise inventory		1000		
dr. Cost of goods sold	1000		record c.o.g.s.	Sale.
cr. Inv. in Consignment		1000		
dr. A.R.	1400		record Revenue	
cr. Sales Revenue		1400		

Franchise Revenue: Franchisee pays lump sum to franchizer who agrees to provide advice, services, etc... Franchizor needs to complete these services (setup, training, etc...) before materializing revenues; usually happens after start of franchisee's operations.

Acct
NpH

Percentage of completion: long contracts, typically
- Fixed price contract: pre-determined amounts are paid during milestones
- Cost Reimbursement contract: customer payment @ milestone $\propto$ costs + reasonable profit.

Completed Contract method: used if % completion can't be estimated; costs incurred are held as an asset (i.e. contract work in progress) until revenue is regognized.

Production Method.
- Permitted but not required by GAAP.
- Typically used in mining & agriculture
- Recognize revenue @ harvest or when metals are extracted, rather than when sold.

Instalment method.
- Revenue regognized when installment payment is received
- Proportion of COGS is realized (proportion) @ same period.

Real Estate Sale Recognition conditions.
1- Period of contract cancellation has expired
2- Buyer has made cululative payment of at least 10%
3- Seller has completed or is clearly capable of completing required improvements (roads, utility connections, etc...).

Amount of Revenue Recognized.

NRV-Net Realizable value: Amount reasonably estimated to be collected.

Adjustment for bad debts.
- Direct write off method: write off when specific trouble account is identified. ⇒ Does not meet matching principle.
- Allowance method: total amount of uncollectible AR is estimated as a % sales based on historical default rates.

Allowance Method

Dr. A.R.	10 000		Make sale on credit
Cr Sales Revenue		10 000	
Dr. Bad debt expense	300		Record Bad debt exp;
Cr. AFDA.		300	keep AFDA provision
Dr AFDA	75.		write off debt from AR
Cr A.R.		75.	Dr. provision
Dr Cash.	75		write off ends up
Cr AFDA		75	paying

Sales discount: ex 2/10 net 30.
Can be recorded in 3 ways
1. Record as reduction of gross sales
2. Record as expense in that period.
3. Record initial sale as net, discount not taken as additional revenue.

Credit Card Sales.
- Bank plan: Visa/MC
  - Reimburse immediately (No A.R.)
  - C.C. fee is a sales discount/expense
- Credit plan (Amex, Discover).
  - Creates AR.
  - No bad debt, assume C.C. will reimburse (regardless of customer behavior)

Acct
Np16

Sales returns & Allowances.

- Estimate % revenues for returns; similar to bad debt

Sales return allowance ⇔ Bad debt expense

Provision for Return & Allowance ⇔ AFDA.

ex

Dr Cash	10000		make the sale
Cr. Sales revenue		10 000	
Dr. Sales Return Allowance expense	500		Provision %; record expense @ Sale period
Cr. Provision for Return/Allow.		500	
Dr. Provision for return/Allow 100.			Reimburse for return; disburse cash.
Cr. Cash.		100	

Adjust revenue Vs Expense

- Realization consept suggest to adjust revenue
- Same N.I, but Δ in revenues & Gross margins
- when method chosen, need to be consistent

Warranty Costs.

- Similar to bad debts & Sales Returns & Allowances

Interest Revenues.

Interest Paid @ maturity:

dr. Loans receivable	10 000		loan is granted.
cr Cash		10 000	
Dr. Interest receivable	300		Interest is earned.
Cr. Interest Revenue		300	
Dr Cash	300		interest is paid.
Cr. Interest Receivable		300	

Discounted loan.

Dr. loan Receivable 10 000
Cr Cash 9100
Cr. Unearned interest revenue 900

loan is made. Unearned revenue recorded

Dr. Unearned int. Revenue 300
Cr. Interest Revenue 300

Record revenue unearned as asset.

Dr Cash 10 000.
Cr loan Receivable 10 000

loan is repayed

Dr. Unearned int. Rev. 600.
Cr. Interest Revenue . 600

interest revenue materialized.

Monetary Assets.
- Money or claims to recieve fix sums of money
- Recorded on B.S. @ value
  - Cash: Recorded @ face value
    - Funds available for disbursmen
    - May include highly liquid assets
  - Receivables. Recorded @ NRV.
    - Called trade receivables for non F. I.s.
    - Also record employee loans (recorded separatly).
  - Marketable Securities: Recorded @ market value
    - must be temporary investments. (Commercial paper, Tbills, bonds).

Non monetary assets.
- Items used for production

Marketable securities
1. Held to maturity securities: Reported @ Cost. (gain/loss @ maturity)
2. Trading Security: Reported @ market value. (gain/loss per period)
3. Available for Sale securities: Reported @ market value

Acct
NP18.

Analysis of monetary assets.

Current Ratio: $\frac{\text{Current Assets}}{\text{Current Liabilities}}$ measures liquidity

Acid test Ratio: $\frac{\text{monetary C.A}}{\text{Current liab.}}$ excludes inventories & prepaid exp.

Day's Cash: $\frac{\text{Cash}}{\text{Cash exp} \div 365}$ cash exp excludes depreciation

Day's Receivables: $\frac{\text{AR}}{\text{Sales} \div 365}$ a.k.a. collection period; should not exceed 133% of pmt terms.

Ch6 - Cost of Sales & inventory.

Inventory: Asset held for sale in ordinary course of business or goods that will be used in production of goods & or services to be sold

Supplies: tangible items that will be used in the course of normal operation (consumed, not sold therefore ≠ inv.).

Types of Companies
- Merchandizing: Sells goods in same form as aquired; has merchandizing inventory
- Manufacturing company: Converts raw materials into finished goods. Has: Materials, work in progress & finished goods inv.
- Service company: Provides intangible services. Has: jobs in progress or unbilled costs as inv. (+ supplies)

ACLT
NP19.

Marchandising Companies

Net purchase cost: cost of marchandize + expenditure to make it available (freight, handling, etc..) ⇒ Recorded @ received, not when ordered

Begining Inventory
+ Purchases ← (Gross purchases - Returns & allowance + freight-in)
Goods available for sale
- End inventory
Cost of Goods Sold.

Measurement issue - 2 unknowns
- How much was COGS: use perpetual inventory method.
- What is end inventory: use periodic inventory method

Periodic inventory:
1) take periodic inventory count
2) Compute beg. inv + purchases = Gds avail for sale
3) Compute COGS = End inv. - GAFS.

less record keeping

Perpetual inventory:
1) When purchase, keep perpetual record of item
2) @ Sale, Cr. Marchandise inv & Dr. Cogs.
3) Inv. balance + COGS always available

Useful for re-Stocking
identifies Shrinkeage
F/S avail on the fly

Retail method
1) Record purchases @ Cost & Retail Sale price
2) Calculate average Gross margin of GAFS.
3) Sales - avg. Gross margins = COGS.

Acct
N P20

Manufacturing Companies

Material Inv	
Beg (+)	Mat. used (−)
Net purchases (+)	
End Inv	

WIP inv	
Beg (+)	Cost of gds mfged
Mat Used	
Conversion Cost (+)	
End inv	

Direct labor
Overheads

Finished Goods inv	
Beg (+)	COGS (−)
Cost of gds manufactured	
End inv	

Service Companies

Personal Services (ex: Hotels, beauty, salon, dentist)
- No inv; just supplies

Building & trade repair (ex: Garage, electric, HVAC...)
- Supplies & also parts inv.

Professional Services (ex: law, accountant, Architecture)
- Have Jobs in progress (similar to WIP in mfg).

Inventory Costing methods

[① Specific Identification ② Average Cost ③ FIFO ④ LIFO].

① Specific Identification
- Track costs per each item
- typically used for big ticket items (Cars, jewlery).
- Can lead to cost manipulation

② Average cost
- Compute average cost of all items
- Avg cost = [Beg inv + purchases] ÷ # units avail. for sale
- Cogs = # of units sold × Average cost per unit (between LIFO & FIFO).

Periodic inv: Calculate avg every period.
Perpetual inv: Calculate avg every purchase

Acct
N p21

③ FIFO Method
- Expense cost of oldest purchase first
- likely to approximate real flow of goods.
- End. inv. approximates current cost of goods.

④ LIFO Method (not permitted by IFRS).
- Assumes most recent goods sold first
- End inv. based on oldest purchases
- Growing & Shrinking inv creates layers that have huge impact in COGS.
- LIFO Reserve: Diff btw LIFO & [FIFO or average]

FIFO	Vs. LIFO.
More realistic flow of goods	w/cost-plus pricing, provides more appropriate price
More accurate BS. Valuation	Inflation = COGS↑, taxable income↓, tax↓
	Lower earnings for Shareholders

Lower Cost or Market (LCM).
To reflect conservatism in Deterioration, obsoleteness, changing tastes
- Ceiling: NRV = Sale price - Cost of selling (inv < $ received)
- Floor: NRV - Normal profit margin (inv not artificially low).
- Replacement Cost: using today figures

→ Middle = Fair market Value if(FMV<inv, FMV, inv)

ex. Item sells for 300 w/ 10$ sales overheads, 245 cost of replacement & normal profit = 50.

NRV = 300 - 10 = 290.
NRV - Profit = 290 - 50 = 240.
Repl: 245 ← FVM.

Acct Np22 if was @ 400 in inv; write off 400 - 245 = 155$ per item

Inventory Ratios

Inv. Turnover = $\frac{\text{COGS}}{\text{Inv.}}$ How many times is inv. flipped during period.

Day's Inventory = $\frac{\text{Inv.}}{\text{COGS} \div 365}$ How much inv used in a day. How many days of Inventory is on Hand.

Gross Margins = $\frac{\text{Sales} - \text{COGS}}{\text{Sales}}$ Gross margins @% Sales.

Ch7 - Long lived nonMonetary Assets & Amortization

Capitalized Assets: Benefits expected in future periods
[expensed: benefits expected in current period]

Amortization: Process of matching capitalized costs w/ revenues obtained from their use

<u>Tangible asset</u>: aka fixed asset; w/ physical substance

Land	Not amortized
Plant & Equipment	Depreciated
Natural Ressources	Depleted

Intangible assets: No physical substance

Goodwill	Not amortized
Intangible assets - limited life	Amortized
Intangible asset - indefinite life	Not amortized
Leasehold improvements	Amortized
Deferred charges	Amortized.
R&D.	Expensed

Distinction between Asset & Expense

- Betterments: Makes asset better than it was when purchased or extends service life ⇒ Capex
- Low cost items: from materiality concept: opex
- Replacement of entire asset: write off old one & Cap. New one
- Replacement of component/part/opex

What to include in costs for capitalization

- All expenditures req. to make asset ready for its intended use
- for self constructed assets: Also include interest
- NonCash: FMV of payment or of purchased asset. IFRS allows reevaluation
  increase/decrease = gain or loss in reevaluation period
- Basket purchase: Split basket costs in categories

Acct
Np23.

Depreciation: Systematic allocation of the original cost of an asset to the period in which the asset provides benefits to the entity

Service life: typically < physical life; due to deterioration/obsolecense
Book value: purchase price - Dep.
Calculating dep: GAAP - Systematic & Rational; IFRS: reflect pattern of usage

Straight line: $\frac{\text{Cost} - \text{R.V.}}{\text{life}}$ = Exp for all yrs use rate applied on purchased Price } ex 5yrs 20% 4yrs 25%

Double declining balance: Apply rate on book value; not on purchased cost. Stated as a % of the straight line rate.
ex: 10yrs S.L ⇒ 10% if 200% decl bal rate; use 200% of 10% = 20%
ex: 10yrs S.L. Rate: 10% if 150% decl bal; use 150% of 10% = 15%

Accounting for depreciation
Changes in rate: amortize remaining B.V. w/ new rate.
Fully depreciated asset: stay in B.S. until disposed of.

Disposal
Credit cash, remove asset, remove dep, record gain/loss in current period

Impaired asset: if p.v. of remaining benifits < B.V.
if expected to keep: write down to fair value
if expected to sell: write down to fair value - disposal cost

Trade Ins/Exchanges
Similar assets: New asset's B.V. = previous asset's B.V. plus additional amount paid (No gain/loss recorded
Different Assets: Record new asset @ fair value,
Acct which is F.V. of exchange + Cash. Record Gain/Loss
N p24 Either way, disregard List price of new asset

Ex:

Asset	20 000	(Car).
Accum. Dep	15 000	
B.V.	5 000	(fair market value = 7 000).

Trade 7 000 Car + 18 000 Cash for New w/ list price 30 000 (cost 25 or 23)

Car

(Cost recorded) → Cr Assets 23 000 (5+18)
Cr Dep. 15 000
Dr Cash 18 000
Dr Asset 20 000

Equipment

Cr. Asset 25 000 (7+18)
Cr. Dep 15 000
Dr Cash 18 000
Dr Asset 20 000
Dr. Gain 2 000

Group (Pool) depreciation - Disposal

Cr Cash — Gain (or Dr loss)
Dr Asset — original cost
Dr. Dep. — Sales price

No gain or loss recorded

Natural Ressources

- Full cost method: capitalize successful & unsuccessfull exploration
- Successful efforts method: if didn't find, exp, if find = Capex

Depletion: Amortization of cost of Nat. ressources typically use units of production method.

Intangible Assets

limited life: amortize over life
indefinite life: Periodic impairment test (ex. Goodwill impairment test yearly)

Leasehold improvement: Amortized over lease but if likely to renew - to next lease also

Average age of depreciable assets: $\frac{\text{Accum. dep}}{\text{annual dep exp.}}$

Ch 8 - Sources of Capital: Debt.

Liability: obligation to a 3rd party arising from an event that has already occured.

Executory contract:
- Not a liability
- Neither parties have yet performed.

Contingency: Uncertainty as to possible gain/loss that will ultimately be resolved by some future event
- Gain Contingency: (Conservatism) usually not reported
- Loss
  - Record if probable Asset impairment or liability incurred
  - Disclose if reasonably possible &/or Can't be reasonably estimated

Bonds.
- Indenture: Bond agreement
- Covenant: maintain certain ratios..
- Debenture: Bond not secured by any specific asset
- Sinking fund bond: Covenant that requires setting $ aside to be used to redeem @ maturity
- Serial Bond: redeemed in installments.
- Callable bond: Option for issuer to redeem b4 maturity
- Convertible bond: bond holder can exchange for

Bonds Accounting
Issuing costs: deferred charges for life of bond
Discount: Contra-liability amortized
Premium: Adjunct liability amortized.

Acct
Np 26.

1- Bond Issue.

Market: 851	Dr. Cash.	83 000	
Issue Cost: 21	Dr. Deferred Chrges	2100	
Discount: 149.	Dr. Bond Discount	14 900	
F.V.: 1000.	Cr. Bond payable		100 000

Case

or if ⊖ premium

Market: 1091	Dr. Cash	107 000	
Issue Cost: 21	Dr. Deferred Charges	2100	
Premium 91	Cr. Premium		9100
F.V. 1000	Cr. Bond Payable		100 000.

2- Interest

Bond discount/Premium amortized

25,53
26,25

ⓐ Calculate YTM (this case is 12%).
ⓑ For every period, interest = B.V. x YTM.
ⓒ Split in F.V.·i for interest & rest for discount Amortization
ⓓ Issuing Costs Amortized w/ straight line

Ex. B.V. = 85 100 x 12% = 10 212. | 212 = Discount Amortization
10 000 = Coupon

Adjusting entry Dec 31st if issued Oct 1st

Cr. Interest Expense [85 100x0,12]÷4 = 2553.
Dr. Discount 53.
Dr. Accrued Interest payable 2500

When paying

Dr Bond Interest Exp = [85 100x0,12]x3/4 = 7 659.
Cr Discount [7659-7500 = 159].
Dr. Accrued Interest payable 2 500
Cr Cash 10 000.

For year: total Interest Exp: 10 212.
Cr. Cash 10 000
Cr. Discount 212

Acct
N p28.

Retirement of Bonds.

- Before maturity (callable or market purchase):
  Gain/loss = Reaquisition price - Net Carrying Amnt
- @ maturity: Ø balance in Deferred Changes & Bond discount/premium
  Debit bond payable/Credit Cash

Capital lease: If any of

1- Asset becomes property of leasee @ maturity
2- lease has a purchase option
3- lease length ≥ 75% life of asset
4- P.V. of min lease pmt ≥ 90% of FMV of Asset (Use incremental Borrowing cost as i)

Otherwise ⇒ Off balance sheet lease

Capital leases are treated just like regular asset

Ratios.

- D/E
- Debt/Capitalization ratio = Debt/[Debt + SHE].
- Times interest Earned EBIT / Interest Expense.

Bond Ex.
F.V. = $250 000
Premium: $10 000
PMT: 10 000 semiA
n=10.
Use straight line Amortization

April 1st 2008
Issue
Dr Cash 260 000
Cr. Premium 10 000
Cr. Bond payable 250 000

Oct 1st 2008
Coupon
Cr. Interest Exp 10 000
Dr. Cash 10 000
Cr. Premium 500
Dr. Interest Exp 500

Dec 31st
End of period
Cr. Interest Exp 5000
Dr. Accrued 5000
Cr. Premium 250
Dr. Interest Exp 250.

April 1st 2009
Coupon
Cr. Int. Exp 5000
Dr Cash 5 000
Cr. Premium 250
Dr. Int. Exp 250.

Acct
Np29.

* Issue @ 98
means 98% FV

Chapter 9: Equity

Forms of business
- Sole proprietor] 80% of businesses; 10% of revenue
- Partnership]
- Corporation] 20% of business; 90% of revenues

Limited partnership: General partner has full liability, other partners have limited liab.

Corporation dissadvantages
- Incorporation cost
- Activities limited to granted in charter
- Need permission of each state where operates
- Double taxation

Preferred Stock: Dividend is not tax deductible
- Cumulative: Current & past dividends must be paid b4 common div. paid
- Convertible: into common
- Redeemable: may be redeemable by holder for pre-defined $

Treasury Stock: Reaquire own stock (for aquisition, bonus, warrents, takeover prevention)
- Not an asset
- No voting
- Accounting for treasury stock:
  1. Debit treasury stock (contra asset account) @ aquisition
  2. Hold @ purchase value.
  3. ~~Sell~~ @ gain: record in T. Stock paid in capital
     Sell @ lost: Debit T stock paid in Capital or R.E.
     Gain/lost: Not shown on I/S. & not recognized for tax purposes

if retired: P/L directly in R/E; not on IS.

Acct
Np 30

Cash Dividends
- Declaration date: creates Dividend payable liability
- Date of record: Determines who is eligible
- Pmt date: Pay cash, remove liability

Spin off: Pay dividends w/ shares of other companies already owned
Stock Dividend: pay w/ stock instead of Cash

Warrants: like a call option except
1. Issued by the company itself
2. New shares are issued & when warrant is exercised, shares come from the company (whereas options ⇒ shares are already outstanding & on the market)

Options
- Record @ F.M.V. using option pricing model & charge to salary expense throughout vesting period
- Vesting: option can be exercised even after employee leaves

Employee Stock ownership plan (ESOP): contributions are tax deductible

Earnings per Share (EPS): Reported

$EPS = \frac{NI - \text{prefered Div}}{\#\text{Common}}$ (weighted avg in not fix) ex: 600 prefered @ 10$ means 6000$ in pref. div.

Diluted EPS: # includes convertible securities, options & warrants as exercised

Non Profits

Equity
- Endowment = principal intact, earnings from principal
- Contributed plant: building, art, material contributions

Operating contributions are revenues, not contributed in Capital
R.E. is called operating equity

Acct
Np 31

EPS

- Preferred: 1000 prefered @ 6$ means 6 000$ of prefered div. must be paid. Use NI − #pref x div pref.
- Not fix # of common: Use weight average over time

Diluted EPS - if converted method.

- Convertible Prefered: don't subtract prefered dividend to NI & Add # of New common

Diluted EPS - treasury stock method.

Assume options & warrants are exercised & Cash received is used to purchase own Stock @ average price.

$20 per share ; 100 000 options @ $10.

if exercised, company issues 100 000 Common & receives 1 000 000$

$1 000 000 used to buy 50 000 Common Shares on the market @ $20 each

Effect ⇒ +50 000 outstanding common Shares

Ch10 Other items that affect NI & OE.

Extraordinary item

- Unusual: Highly abnormal & unrelated to ordinary activities
- Infrequent: Not expected to occur in near future.

FASB: Report on IS after income from continuing operations

IASB: No reporting req.

Examples of not extraordinary items

- Write down/off of AR, inv or intangible asset
- Gain/loss from Forex
- Gain/loss from disposal of segment of business/fixed asset
- loss due to a strike

Discontinued Operations: getting ride of a whole b.u.
◦If loss is expected: report when decision is made
◦If gain expected: report when gain materialized.

Account for
- Net income or (usually) loss attribuable to B.U. until sold.
- All associated disposal costs including amounts received & write down of assets

ex
Discontinued operations (Note A)
Loss from operations of Division X (less applicable tax)
Loss on disposal of Div. X (less applicable tax)

Changes in Accounting principles: Consistency concept requires to stay w/same. If sound reason to change, need to retrospect change

Personnel Costs

1) Wages earned

Dr Wage Cost	600	
Cr Wages payable		600
Dr. Employment tax	99.90	
Cr. EI Employer		45.90
Cr. CPP Employer		54.00

2) Employee is paid.

Dr. Wages Payable	600	
Cr. Cash		491.10
Cr. EI employee		45.90
Cr. Tax withheld		63.00

3) Government is paid

Cr. EI payable	91.80	
Cr. CPP payable	54.00	
Cr. Tax withheld payable	63.00	
Cr Cash		208.80

Acct
Np 33.

Components of pension Costs
① Service cost: (+) p.v. of futur benefits employee earned
② Interest cost: (+) amnt by which p.v. of plan's begining of year obligations are expected to increase (payout to retirees)
③ Return on plan assets (-)
④ Prior service costs (+) whenever plans are "sweetened"; $ by which plan assets need to increase to cover new liabilities

Disclosure of pension
- Period's net cost + details on 4 elements
- Assumptions for calculations
- Unfunded plan position for each defined benefit plan

Permanent diff btw. Book & tax
- Some expenses in GAAP are not tax deductible (ex. fines)
- Some revenues are tax deductible (ex: rev. from municipal bonds)

Temporary diff. btw book & tax
• Diff. that will reverse in a later period (ex: revenues/exp. that can be reported)
  - Deferred tax liability: caused by temporary Δ that creates taxable income < book income (i.e less expense or more revenues on books) ex: Accelerated depreciation
  - Deferred tax asset: taxable income > book income (i.e. more expense/less revenues on books) ex: warranty expense recognized when revenue is earned, subscriptions recognized when received for tax but when earned for book, tax loss carry forward
- Deferrals recorded @ current tax rate & adjusted for rate change if required.

Acct
NP 34.

Forex

- At balance sheet date, recorded foreign balances are adjusted to current (spot) rate
- Gain/loss included in NI in period incurred

Functional currency: Currency of primary economic environment in which company operates.

If not USD: Use net investment (current rate) method: foreign BU considered as an investment

- Assets & liabilities converted @ current rate
- Revenues/expenses converted @ average rate of period.

If USD: Remeasurement (temporal method): foreign BU treated as extension of operations.

- Same as current rate except:
  - for long lived assets & inventory + associated expenses translated when incurred. (ex: dep, COGS)
  - Gain/loss from remeasurement included in income

Derivatives

- Recognized as asset/liab. & measured @ F.M.V.
- Gain/loss included in income except if categorized as hedge in which case shown under non owner changes in owner equity

Pro forma earnings.

- Not covered by GAAP other that they must not be misleading
- Shown @ discussion of mgmt
- Excludes some items already included in NI (ex: merger related charges, non recurring items, goodwill impairment writeoff.).

Cash flow

Sources	Uses
Operations	Cash Dividends
Borrowing	Repayment of debt
Stock issues	Repurchase stock
Sale of property/plant/Eq	Purchase plant/Eq
Sale of other non current assets	Purchase other noncurrent assets

Definition of cash
- Cash or equivalents
  - Short term investments (mature <90 days)
  - Highly liquid
  - Convertible to known amount of cash
  - Subject to ↓ risk of change in value

Shortterm Assets [Operation] Short term Liab } Δ Working capital

Longterm Assets
[INVESTMENT]

Long term Liab
S.H.E
[FINANCING]
Δ R.E. ⇒ Change in Cash

Investing Activities
Sources/use
- Long lived Assets (buy/sell)
- Investments (Non cash eq).
- Make/Collect loans.

Operating CF = ΔF.A. $\underbrace{-\text{Depreciation}}_{\text{to only see } \Delta \text{ Cash}}$.

Acct
Np37.

Financing Activities - (LTL + SHE).
Sources/uses
- Borrow Cash/Repay debt
- Issue Equity/Securities
- Dividends paid.

Investment/Financial activities that do not involve cash
ex: Convert bond to stock or purchase building w/notes payable
⇒ narrative statement of disclosure (Not reported in C.F.S)

Operations.
- P/L from NI + Depreciation
- Δ Working capital (AR/AP/Inventory/Accrued/prepaids).
- Dividend + Interest received.

Direct method.
- Collections from customers.
  sales - (End AR - beg AR)
- Payments to suppliers -
  COGS + (End Inv - Beg Inv) - (End AP - Beg AP).
- Interest paid.
  Interest Expense - (End interest payable - beg. int. pay)

Indirect method.
- Net Income adjusted for non-cash items included
  - Depreciation
  - Δ A.R.
  - Δ A.P., inventory, prepaid expenses.
  - Δ Payables (wages, taxes, interest)
  - Δ Deferred taxes
  - Gain/loss on asset Disposal (Already counted in Investment CF so remove from op. CF)

Acct
p38.

Cash flow Ratios.

- Cash realization (Quality of earnings)

$$\frac{\text{C.F. ops}}{\text{N.I.}}$$

- T.I.E. / Fix changes coverage

$$\frac{\text{C.F. ops}}{\text{Interest payable} \boxed{\text{or}} \text{ Fix changes}}$$

- Free Cash flow

CF ops − (Fix Asset replacement + Debt repayment + Dividend)

Ch 13 - Financial Statement Analysis

① P/E: price earning

$$\frac{\text{Market price per Share}}{\text{N.I. per share}}$$

② Return on Assets (ROA)

$$\frac{\text{N.I.} + \text{Interest}(1-\text{tax})}{\text{LTL} + \text{SHE}}$$

Adj for pre-tax interest to evaluate mgrs who don't control financing

⑤ Gross Margins

$$\frac{\text{Gross Margins}}{\text{Net Sales}}$$

⑥ Profit Margins

$$\frac{\text{Net income}}{\text{Net Sales Revenue}}$$

⑦ Earnings per Share (EPS)

$$\frac{\text{Net income}}{\#\text{ shares outstanding}}$$

14. Day's receivable (Collection period) $\frac{AR}{\text{Sales on Credit}/365}$

15 Day's Inventory $\frac{\text{Inventory}}{\text{Cost of Sales}/365}$

16. Inventory turnover $\frac{\text{Cost of Sales}}{\text{Inventory}}$

17. Working Capital turnover $\frac{\text{Sales Revenue}}{\text{Working Capital}}$
W.C. = [Current Assets - Cur. Liab].

Cash conversion Cycle Days Receivable + Day Inventory - Days payable
→ length to complete operating cycle (during which short term borrowing might be required)

18. Current Ratio $\frac{\text{Current Assets}}{\text{current Liab}}$.

19. Acid test (Quick) Ratio $\frac{\text{Monetary current Assets}}{C.L}$.
Remove inv + prepaid

Liquidity: Ability to meet current obligations (Current/Acid Ratios)
Solvency: Ability to meet interest costs & other long term obligation (ex D/E, TIE, CF/debt)

Acct
Np40

Ch2 - Acquisitions & Consolidated Statements

① Fair Value Method
- If investor ows less than 20% of common stock of investee.
- Stock treated as "available for sale" securities.
- Stock reported on B/S @ FMV.
- Price fluctuations excluded from earnings & entered directly on SHE under "Other comprehensive income".
- Dividends received treated as revenues.

② Cost Method.
- If own <20% AND FMV not readily determinable
- Record @ cost

③ Equity method
- if ownership >20% (Assume investor can influence actions of investee).
- Initially recorded as investment @ cost

Investment	250 000	
Cash		250 000

- Earnings: increase investment based on % of earnings of investee as revenues.

ex: investee earns 100k; investor owns 25%

Investment	25 000	
Investment revenues		25 000

- Dividends: Reduce investment by dividend received, but no effect on I/S.

ex:

Cash	10 000	
Investment		10 000

} Net Ø; converts investments to cash.

④ Consolidated Bases.
- when ownership > 50%
- Accounting 3 same as equity method w/ more rules.

Acct
Np41

Business combinations

① Pooling method.
- Add both balance sheet; remove any interco AR/AP, etc...
- Issue: Actual aquisition price is not reflected in presentation
- No longer Acceptable practice.

② Purchase Method.
- Method:
  - I - tangible Assets are separated from intangible (patents/licences, etc...) & reevaluated @ FMV.
  - II - Intangible Assets
    - limited life: Amortized over life.
    - Unlimited life: Not amortized; subject to impairment test
  - III - Liabilities are adjusted to FMV.
  - IV - If purchase price ≥ adjusted B/S acquired, record goodwill otherwise Acquired tangible Assets are written down on a pro-rata basis

Consolidated Statments
- Individual statments adjusted for inter-co & combined
- when > 50% of subsidy is owned by parent

① Working Capital.
if parent owns subsidy: Dr. AP. Subsidy
Cr AR Parent

AR	
Dr	Cr
+	−

AP	
Dr	Cr
−	+

② Investments.
Use investment in subsidy to cancel out subsity C.S + R.E.
ex: if parent inv. in subsity = 55k & Subsity C.S = 40k, then RE @ aquisition was 15k.

Dr. Subsity Capital Stock 40 000
Dr. Subsidy R.E. 15 000
Cr. Parent investment in Sub. 55 000.

Acct
Np 42