SECTION B

List SIX components that comprise a complete set of financial statements (6 marks).

**a)** ***statement of financial position as at the end of the period; (Formerly, the BALANCE SHEET)***

***b) a statement of comprehensive income for the period;***

***c) a statement of changes in equity for the period:***

***d) a statement of cash flows for the period;***

***e) notes, comprising a summary of significant accounting policies and other explanatory information; and***

***f) a statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.***

Explain what is meant by faithful representation and how it enhances reliability. (6 marks)

The financial statements shall present fairly the financial position, financial performance and cash flows of the entity.

***Fair presentation requires the faithful representation of the effects of transactions, other events and conditions, in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework for the Preparation and Presentation of Financial Statements (the Framework). The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.***

***In virtually all circumstances, an entity achieves a fair presentation by compliance with applicable IFRSs.***

***A fair presentation also requires an entity:***

***• to select and apply accounting policies in accordance with IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, which sets out a hierarchy of authoritative guidance that management considers in the absence of an IFRS that specifically applies to an item;***

***• to present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and***

***• to provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity’s financial position and financial performance.***

Discuss what is meant by consistency of presentation, and conditions under which the classification and representation of items in financial statements may be changed. (8 marks).

***An entity shall retain the presentation and classification of items in the financial statements from one period to the next, unless:***

***a) it is apparent, following a significant change in the nature of the entity’s operations or a review of its financial statements, that another presentation or classification would be more appropriate having regard to the criteria for the selection and application of accounting policies in IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors; or***

***b) an IFRS requires a change in presentation.***

Discuss briefly the position of international financial reporting standards in regards to offsetting of assets/ liabilities and income/ expenses. (3.5 marks)

***An entity shall not offset assets and liabilities unless required or permitted by an IFRS.***

***Note: Measuring assets net of valuation allowances (e.g. obsolescence allowances on inventories and doubtful allowances on receivables) is not offsetting.***

***An entity shall not offset income and expenses unless required or permitted by an IFRS.***

***Where an entity undertakes, in the course of its ordinary activities, transactions that do not generate revenue but that are incidental to its main revenue-generating activities, it presents the results of such transactions by netting any income with the related expenses arising on the same transaction, when such presentation reflects the substance of the transaction or other event.***

***An entity presents on a net basis gains and losses arising from a group of similar transactions (e.g. foreign exchange gains and losses, or gains and losses arising on financial instruments held for trading) unless the gains and losses are material, in which case they are reported separately.***

1. i Write short notes on the following:

***Cumulative vs non-cumulative prefered stock.***

***Prefferd stock is cumulative if any undeclared dividends accumulate each year until paid. It is non-cumulative if the right to recieve dividend is forfeited in any year that dividends are not declared.***

***Participating vs non- participating preffered stock***

***Dividends paid on preffered stock is usually a fixed percentage of the par value. Such stock is non- participating prefferd stock. However some prefferd stock may be paid additional dividends in excess of the stated percentage . Such stock is called the participating preffered stock.***

***Convertible vs non convertible preffered stock***

***Convertible stock can be converted into ordinary shares. Non convertible prefferd stock contains no provision to convert to ordinary shares.***

ii. State and briefly discuss 2 types of debentures (4 marks).

***Types of debentures***

***Debenture can be classified as under :***

***1. From security point of view***

***(i) Secured or Mortgage debentures : These are the debentures that are secured by a charge on the assets of the company. These are also called mortgage debentures. The holders of secured debentures have the right to recover their principal amount with the unpaid amount of interest on such debentures out of the assets mortgaged by the company. In India, debentures must be secured. Secured***

***debentures can be of two types :***

***(a) First mortgage debentures : The holders of such debentures have a first claim on the assets charged.***

***(b) Second mortgage debentures : The holders of such debentures have a second claim on the assets charged.***

***(ii) Unsecured debentures : Debentures which do not carry any security with regard to the principal amount or unpaid interest are called unsecured debentures. These are called simple debentures.***

***2. On the basis of redemption***

***(i) Redeemable debentures : These are the debentures which are issued for a fixed period. The principal amount of such debentures is paid off to the debenture holders on the expiry of such period. These can be redeemed by annual drawings or by purchasing from the open market.***

***(ii) Non-redeemable debentures : These are the debentures which are not redeemed in the life time of the company. Such debentures are paid back only when the company goes into liquidation.***

***3. On the basis of Records***

***(i) Registered debentures : These are the debentures that are registered with the company. The amount of such debentures is payable only to those debenture holders whose name appears in the register of the company.***

***(ii) Bearer debentures : These are the debentures which are not recorded in a register of the company. Such debentures are transferrable merely by delivery. Holder of these debentures is***

***entitled to get the interest.***

***4. On the basis of convertibility***

***(i) Convertible debentures : These are the debentures that can be converted into shares of the company on the expiry of predecided period. The term and conditions of conversion are generally announced at the time of issue of debentures.***

***(ii) Non-convertible debentures : The debenture holders of such debentures cannot convert their debentures into shares of the company.***

***5. On the basis of priority***

***(i) First debentures : These debentures are redeemed before other debentures.***

***(ii) Second debentures : These debentures are redeemed after the redemption of first debentures.***

iii. Discuss the accounting treatment in regards to:

* changes in accounting policies (4 marks)

An entity is permitted to change an accounting policy only if the change:

* ***Is required by a standard or interpretation; or***
* ***Results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance, or cash flows.***

***Note that changes in accounting policies do not include applying an accounting policy to a kind of transaction or event that did not occur previously or were immaterial.***

* Changes in accounting estimates (3.5 marks).

***Many items in financial statements cannot be measured with precision and must be estimated.***

***These involve judgements based on the latest available information. Examples where this would be applied include bad debts, inventory obsolescence, useful lives, warranty obligations etc. Estimates need to be revised if circumstances change as a result of new information or experience. A change in measurement base is, however, a change in policy. If it is difficult to distinguish between a policy and an estimate change, the change should be treated as a change in estimate. A change in estimate is charged prospectively in the income statement in the current and future years. Any related asset/liability should equally be adjusted in the period of change.***