AOS EXAM Notes

Accounting in Organisations and Society (Royal Melbourne Institute of Technology)

Module 1 topic 1: what is accounting and what do accountants do and why?

What is accounting?
Accounting: The provision of information about aspects of the performance of and resources held or controlled by an entity to a particular group of people with an interest, or stake in the organisation

Stakeholders: people who take interest in an organisation, can be internal or external

Accountability
Accountability: concerned with the relationship between groups, individuals, organisations and the rights to information that such relationships entail.
- Put simply: duty to provide an account of the actions for which one is held responsible

Involves 2 responsibilities
1. Undertake certain actions (or refrain) in accordance with the expectations of a group of stakeholders
2. Provide a reckoning of account of those actions to the stakeholders

The role of accounting
- To inform relevant stakeholders about the extent to which the actions which an organisation is deemed to be responsible have actually been fulfilled
- Reporting fulfils the requirement to be accountable
- Perspectives about accountability influence how we measure performance

Why 'accounts' should be prepared?
- Different views about what accounts should be produced and the extent of accounting applied

An accountability model
Decisions made about the process of reporting aspects of an organisations performance
- Why would an entity decide to disclose information about its performance to the general public?
- Who are the stakeholder to whom the disclosures will be directed to?
- What types of disclosures will be made?
- How should the information be disclosed?

Why?
- Managements motivations
  - Providing accountability to various stakeholders
  - Win support of powerful stakeholders
- Objectives driving organisation to generate particular accounts
  - Ethically motivated to ensure organisation benefits society
  - Ensure not having a negative impact on society and the natural environment
  - Economically focused motive to use reporting to protect or enhance owner/shareholder value
- Motivations

    - Comply with legal requirements
    - Forestall efforts to introduce more onerous disclosure/accounting regulations
    - Influence the perceived legitimacy of the organisation
    - Manage particular (powerful) stakeholder groups
    - Increase wealth of shareholders/managers
    - Entity has an accountability to provide particular information to particular stakeholders

Who?
Targeted dependent on managers views about corporate views about corporate responsibilities and accountabilities

- Motivated by managerial reasoning (increasing wealth)
    - Stakeholder to whom hold the greatest economic power over corporation
- Motivated by ethical/moral reasoning
    - Broad range of stakeholders
    - Brader ethical approach
    - Issues such as ‘right to know’
- Motivated by maximisation of shareholder value
    - Economically powerful stakeholders

What?

- Broad stage involving many details stages regarding the report
- Various reporting conventions and frameworks that address different aspects of performance
    - Financial performance
    - Environmental performance
    - Social performance

How?

- Again, broad range that is dependent on what the organisation feels they should disclose
- Reporting frameworks and conventions available regarding aspects of performance in
    - Financial performance
    - Environmental performance
    - Social performance

Module 1 Topic 2: Organisational forms and why, what, how and to whom should they provide accounts?

What is an organisation?

Organisation: a collection of people who work toward a common goal or objective

- Each organisation will have different responsibilities and accountabilities and demands on accounting

Sole trader

Sole trader: One individual controls and manages a business and is responsible for all of its debts

Advantages	Disadvantages
- Easy to set up - Absolute control - No specific accounting requirements	- Unlimited liability - Limited life - Sole risk bearer (and profit recipient)

Partnerships

Partnerships: when two or more people come together with a common purpose and usually for the purpose of making a profit

Advantages	Disadvantages
- Easy to set up - Sharing of risks (and profit) - Reports do not have to comply with accounting standards	- Mutual agency - Unlimited liability - Limited life

Company

Company: an entity that has a separate legal existence from its owners

Advantages	Disadvantages
- Separate legal entity - Limited liability - Indefinite life	- More complicated to form - Might have to comply with accounting standards

Resources of an organisation

Resource: something that has value in the same sense that it allows an entity to accomplish an activity so as to achieve a desired outcome

Examples:

- Financial resources
- Machinery
- Natural resources (air, water, timber, material from mining)
- Human based resources (factory labour, managerial labour, intellectual capital)

Measurement of resources

- Many ways to measure resources
- Is it necessary to measure all resources

Outputs of an organisation

- Organisations create various outputs, some intended and some not
- Examples
  - Goods and services for sale
  - Educated people (universities)
  - Healthy people (hospital)
  - Healthy environment (environmental people)
  - Safe people (employee unions)
  - Wasted material and other rubbish
  - Co_2 emissions
  - Polluted water
  - Noise

Measurement of outputs

Questions to consider

- Why
- Is it practical
- Is this accounting

Measurement

- Goals of managers and purposes determine what we measure and report
- Depends on expectations of stakeholders

Externalities

Externalities: impacts that an entity has on parties external to the organisation where such parties did not agree to or take part in the activities causing the externality

- Views as positive or negative

Positive	Negative
- Benefits to the environment from a zoo releasing a bred endangered animal back into the environment	- Loss of homes of people living in the pacific islands as a result of climate change due to industry Co_2 emissions

Module 1 topic 3: What do we provide an account of and why?

Which organisations should produce an account?

- Different forms of organisations with different activities, responsibilities, resources and stakeholders
- Accounts can be produces internally and externally
- 3 specific areas
  - Financial
  - Social
  - Environment
- Depends on what the organisation wants to produce accounts of

Factors that influence internal reporting

- Various types of info needed to manage the organisation
- Influences
  - What aspects of performance they want to manage
  - Personal values
  - Stakeholder pressure
  - Basis or remuneration
  - Scarcity and/ore ecological importance of resources
  - Professional and educational background

Factors that influence external reporting (public reports)

- Regulating
  - Reported due to no alternative
  - Consequences if not complied with
  - E.g. taxation require financial reports
- Stakeholder demands/needs
  - Required to monitor their investments
  - 'Right to know'
  - Particularly social and environmental aspects
  - Accountability
- To manage particularly powerful stakeholders
  - Strategic business reasons
  - Stakeholders that have power to influence the operations of the organisation
- Manage perceived legitimacy of an organisation
  - Reports change around a time of particular crisis
  - Reporting that is reactive to a crisis is about organisational survival not true accountability
- Increase wealth of the managers of the organisation
  - Shares in organisation or bonuses linked to profits
  - Produce particular accounts that increase wealth

Frameworks used to produce accounts for external stakeholders

Three types of external reporting (sustainability)

- Financial

- Social
- Environmental

External reporting

Financial	- Produced through financial accounting - Provides info about financial performance/position o Audience is owners and individuals with a financial stake - Accounting standards used as a basis

Social	- Social accounting
	- Provides info about organisations interaction with/associated impacts on particular societies
	- Includes
	    o Interaction with local community
	    o Level of support from community projects
	    o Support for employees within the supply chain
	    o Health and safety record
	    o Employment
	    o Training/education
	    o Diversity and equal opportunity
	    o Child labour
	    o Indigenous rights

Environmental	- Environmental accounting
	- Addresses organisations impact on living and non-living natural systems
	    o Materials
	    o Energy
	    o Water
	    o Biodiversity
	    o Emissions
	    o Effluents and waste
	    o Environmental compliance
	    o Supplier environmental assessment

Module 2 topic 1: setting the scene

What does management do?

- Plans: what does the organisation want to achieve?
- Organises: how does the organisation achieve its goals, plans/
- Makes decisions: determining the best course of action amongst alternatives
- Monitors performance: how is the organisation performing relative to what it wanted to achieve?
- Revise plans in light of performance/feedback: cycle continues

Manager's role	Accountant's role (IFAC, 2011)	What the Accountant does
Planning What does the organisation want to do/achieve	Framing business models Challenging conventional assumptions of doing business and redefining success in the context of achieving sustainable value creation	Sets objectives Encourages long-term sustainability (vs. short-term approach) Promotes a value added approach
Organising How does the organisation achieve its goals, plans	Encouraging and rewarding the right behaviors	Allocates resources to add value and achieve goals Structures incentives to align behavior with organisational goals
Decision Making Determining the best course of action from amongst alternatives	Ensuring that decisions are supported by the necessary information, analysis, and insights	Provides cost information for decision-making Prepares forecasts Undertakes analysis (e.g. cost/benefit, scenario)
Monitoring Performance How is the organisation doing relative to what it wanted to achieve?	Ensuring that monitoring and reporting performance go beyond the traditional ways of thinking about economic success	Sets targets/KPI's Budgeting and analysis Benchmarking Measurement Reporting

Planning: key factors to consider

- Planning is central to managing a business
- Continuous proves
- Acts as a benchmark which future performance can be assessed
- Things to take into consideration:
  - Organisations missions
  - Available resources
  - Stakeholders expectations
  - Current and future technologies
  - Economic, social and environmental implications of various strategies
  - Existing and projected regulations

Planning: planning as a continual process

- Plans must be monitored and controlled alongside standards/goals to establish opportunities for improvement therefore must be continuously considered

- Previous plants revides
- Feedback taken into consideration, stakeholders especially

Planning

Sustainability incorporated within organisational strategy

- Sustainability of organisations and development is an issue for politicians, consumers and business leasers
- Competitive advantage
- Long term value
    - Need for short term results distracts the long-term vision

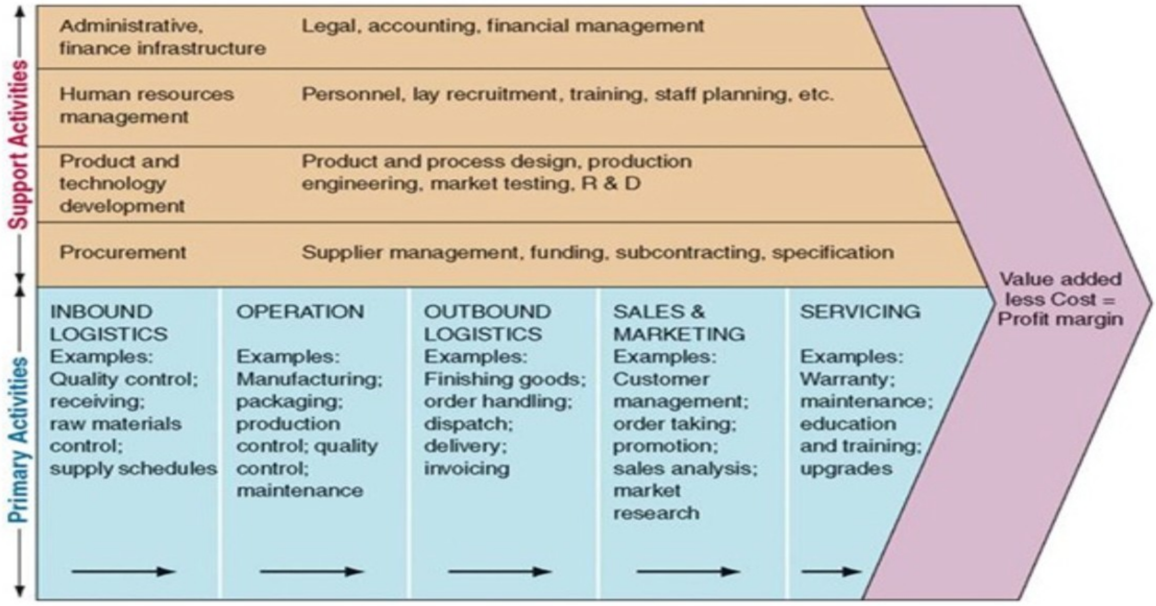
Components

Overview/description of business	- What do they want to achieve? - Who/why key stakeholders/customers - Key personnel and their roles expertise
Financial plan	- Funding requirements - Potential sources of funding - Projected financial performance - Budgets
Marketing plan	- Current and expected competition - Expected demand - Factors to influence demand
Social and environmental management plan	- Operate in socially and environmentally responsible manner - Key impacts - Life cycle analysis
Operating plan	- Actions to succeed - Key suppliers/supply chains - Required employees - Implications pf regulations - Stakeholders expectations and related engagement policies

Planning: value creating within an organisation

- Expected to create value for various stakeholders and environment
- Value creation occur in an ecologically and socially sustainable and responsible manner
- Greater efficiency = greater value
- Value requires clear vision, strategy and planning

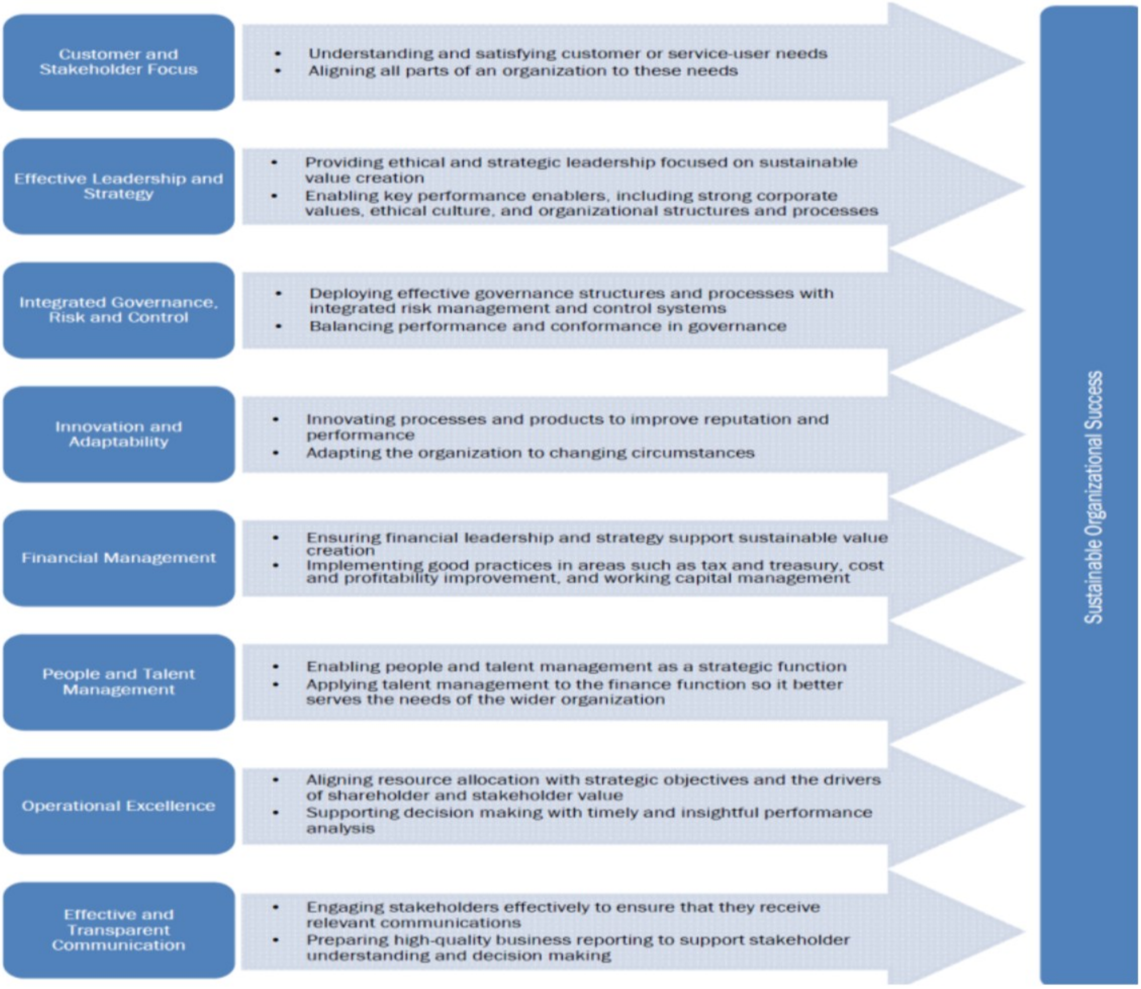
Porters value chain



Organising: value drivers and resource allocation

Value creation influenced by

- Culture and leadership style
- Management willingness to collaborate
- Preparedness to be innovative
- Level of efficiency being embraced
- Awareness of market opportunities and changes therein


Customer and Stakeholder Focus
• Understanding and satisfying customer or service-user needs
• Aligning all parts of an organization to these needs
Effective Leadership and Strategy
• Providing ethical and strategic leadership focused on sustainable value creation
• Enabling key performance enablers, including strong corporate values, ethical culture, and organizational structures and processes
Integrated Governance, Risk and Control
• Deploying effective governance structures and processes with integrated risk management and control systems
• Balancing performance and conformance in governance
Innovation and Adaptability
• Innovating processes and products to improve reputation and performance
• Adapting the organization to changing circumstances
Financial Management
• Ensuring financial leadership and strategy support sustainable value creation
• Implementing good practices in areas such as tax and treasury, cost and profitability improvement, and working capital management
People and Talent Management
• Enabling people and talent management as a strategic function
• Applying talent management to the finance function so it better serves the needs of the wider organization
Operational Excellence
• Aligning resource allocation with strategic objectives and the drivers of shareholder and stakeholder value
• Supporting decision making with timely and insightful performance analysis
Effective and Transparent Communication
• Engaging stakeholders effectively to ensure that they receive relevant communications
• Preparing high-quality business reporting to support stakeholder understanding and decision making
Sustainable Organizational Success

The accountant's role in managerial activities

Revises and adjusts

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In the topic that follows we will consider:

Revises and adjusts

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Module 2 topic 2: performance measurement

Different approaches to performance measurement

- Products/services
- Mission/goals
- Culture
- Stakeholder expectations
- Environmental or social sensitivity of the environment in which the organisation operates
- Degree of competition
- Supply chains in place
- Existing and projected regulation

Stakeholders perception of value

Shareholders	- Maximisation of dividends, share value	- Need to measure financial performance - control various financial costs - maximising revenues
Employees (local)	- Timely payment of wages - Provision of safe and healthy work environment - Promotion and training opportunities	- Provide accounts about how safe and healthy work environment is - Account of training for employees - Communities perception of organisation
Employees (offshore supply factories)	- Provision of safe and healthy work environmental - Liveable wages	- Account of employee practices - Outcomes with supply company factories
Customer	- Low price high quality - Social impact throughout supply chain - Positive environmental impact throughout supply chain - Reliable after sale service	- Costs of produces - Monitoring suppliers throughout supply chain - Social and environmental impacts - Satisfaction surveys -
Local communities	- Contribution to community activities - Safe place of work for local residents - Low social and environ impacts	- Key economic, social and environmental costs and benefits
Suppliers	- Reliable payment - Ongoing support for products/services	- Levels of satisfactions and areas of improvements

Life cycle analysis

- Evaluates a product or service across its entire life
- Addresses social/environmental impacts
- Identifies improvements
- Example is an Eco Balance

Life cycle costing

Life-cycle cost analysis: tool to determine the most cost effective option among different competing alternatives to purchase, own, operate, maintain and finally dispose of an object or process, when each is equally appropriate to be implemented on technical grounds

The balanced scorecard (BSC)

Performance measurement framework that adds strategic non-financial performance measures to give managers and executives a more balances perspective of organisational performance

- Looks at 4 perspectives
    - Financial: sales, cost reduction, profit, return on assets
    - Customer: customer satisfaction/retention,
    - Business processes: productivity, fault rate, time to complete orders
    - Innovation and learning: training

Considerations of costs and revenues

- Need reliable info about cost of goods/services so accurate pricing can be made and profit

Relevant costs	- Change as a result of a particular decision - Occur in future
Variable costs	- Costs that change as a result of changing production or service - Future
Fixed costs	- Costs that do not change in a particular period as volume of production or services change - Not just financial

Contribution margin

Total contribution margin: difference between total variable costs and total sales revenue generated from a particular product or service (total sales revenue – total variable costs)
Contribution margin per unit: difference between revenue per unit and variable cost per unit

Breakeven point

- Occurs when total financial costs equal the total financial revenues
- Profit is 0
- Calculation: total fixed costs/ contribution margin per unit

How much to generate a target financial profit

Required units of products/services to generate a profit
= (total fixed costs + desired profit)/contribution margin per unit

Module 2 topic 3: performance measurement budgeting

What is a budget?

Budget: detailed, quantitative plan of management activities for a certain time period (usually 12 months)

- Associated to long term strategic plans and goals
- Budget essentially reflects the short-term goals of the primary decision makers as linked to the long term plan

Why budget and to whom?

- Provided to people within the organisation who have responsibility for resources
- One of the most important means of communication
- Essential for planning, organising and controlling activities
- Goals are reflected in budgets
- Important source of feedback
    - Compared against actual performance

What and how budget information should be provided?

- Can be both financial and non-financial
- Influenced by gaols

Annual budget (master)

Annual budget: comprehensive set of budgets that cover all aspects of a firm's activities

Consists of

- Operating budgets: sales budget, various cost budget
- Financial budgets: budgeted statement of financial performance and position, cash budgets

The operating budgets

The sales budget	Sales budget: detailed summary of the estimated sales units and revenues from the organisations products for the budgeted year
	- Based on the sales forcast
	- Factors to consider
	    ○ Internal: Past sale levels, new products, intended pricing policy
	    ○ External: economic/industry trends, political/legal events

The cost budgets	Manufacturing firms - Production budget includes costs for direct materials, labour and overheads - Costs relating to the manufacturing processes = direct - Resources used in production process such as electricity/heating = overheads - Budgets for marketing, general and administrative expensive Retailers and wholesalers - Purchasing budget determine quantity and cost of foods

	purchased for resale
The financial budgets	Cash budget - Expected cash receipts and planned cash payments - Timing of all cash movements important to identify cash shortages and surpluses Budgeted statement of financial performance - (profit and loss) Shows expected revenues and planned expenses for the budgeted period - (balance sheet) expected assets and liabilities at the end of budgeted period

Behavioural consequences of budgeting

- Affects all in an organisation
- 3 approaches to budgeting that affect people's behaviour
  - Participative budgeting: allows managers at all levels of firm to develop their own initial estimates for budgeted sales/costs
  - Top-down budgeting: senior managers impose budgeted targets on less senior managers
  - Bottom-up: employees at the lower managerial and operations levels play an active role in setting their own budgets
- Budgets are generally expected when
  - Targets developed with employee participation
  - Targets considered achievable
  - Frequent feedback on performance
  - Employees held responsible for activities that are within their control
  - Set at level that provides challenges but not impossible

Module 3: social and environmental accounting

Why/who/what/how?

why?	- Responsibility for social and environmental performance - Failure undermines legitimacy - External stakeholders expect to receive information - Impacts decisions
Who?	- Different stakeholders - Managers, investors, employees, customers, government, news etc
What?	- Prioritisation is needed to identify which specific aspects should be reported - Influenced by responsibilities and accountabilities accepted by managers
How?	- Form of reporting largely voluntary therefore variation in reporting - Many reporting frameworks available

Accountability

- Organisations perspective about its accountability directly impacts on what information is provided
- Organisations have a responsibility for its social and environmental performance therefore it has an associated accountability

Social accounting	- Training of employees - Diversity and equal opportunity policies - Health and safety - Support of community projects - Treatment of employees within supply chain - Actions taken to indigenous culture/values - Customer privacy policy - Compliance with OH&S requirements - Compliance with various social codes of conduct
Environmental accounting	- Materials used - Effluents and waste generated - Energy consumed - Emissions generated - Water consumed - Waste water generated and impacts of this waste water - Impacts upon biodiversity - Compliance with environmental regulations

Corporate social responsibility

Corporate social responsibility (CSR): responsibilities an organisation accepts over and above the law and the way in which it focuses its attention on the well-being of various stakeholders and the environment

- Extends reasonability beyond maximising the interest (wealth) of shareholders, and beyond the usual activities associated with the provision of goods and services
- Information about addressing social and environmental responsibilities

Sustainability reporting

- Relates to sustainable development

Sustainable development: the development that meets the needs of the present world without compromising the ability of future generations to meet their own needs

- Helps organisations measure, understand and communicate their economic, environmental, social and governance performance, then set goals and manage effectively

Module 4 topic 1: introduction to financial accounting

What is financial accounting?

- Relates to the preparation and presentation of financial information for a variety of users so as to enable them to make decisions about where they shall allocate their resources
- Used by both internal and external people to the organisation
- Financial statements
    - Income statement
    - Statement of cash flows
    - Balance shows
    - Statement of changes in equity

Why/who/what/how?

Why?	- Extensive amount of regulation requires it - Stakeholders with a financial interest demand it - Used as a communication tool to assist decision making
Who?	- Primary audience = investors, creditors, managers - Other stakeholder have interest
What	- Types of disclosures highly regulates - Accounting standards, stock exchange requirement, corporations law requirements
How?	- Usually regulated for general purpose financial statements

Objective of financial accounting

Special purpose financial statements (SPFSs)	- Financial statements designed to meet needs of a specific group/satisfy specific purpose
General purpose financial statements (GPFRs)	- Financial statements that comply with accounting standards which are intended to meet the information needs common to users of financial information who are unable to command the preparation of statements for their own specific needs

Qualitative characteristics

Relevance	Capable of influencing the decisions of users (materiality)
Faithful representation	Information should be complete, neutral and free from error. Needs to be both relevant and faithfully represented
Comparability	Entity uses the same accounting principles each year
Variability	Information provided can be sourced back to a transaction or event
Timeliness	If collection of information spans too long a period, it is no longer relevant
Understandability	Issues of understandability need judgements to be made of the capabilities of financial statement users

Accounting principles

Entity concept	Accounting only recognises the transactions and events which affect the financial performance or position of the organisation, separate from the owners and other entities
Accounting period	Life of an organisation may be considered to be indefinite, the accountant determines the financial performance of the entity fir smaller periods
Monetary unit assumption	Practice of financial accounting typically only recognises transactions or events if a related monetary value can be assigned.
Going concern	Assumes the organisation will continue operating into the foreseeable future
Accrual basis of accounting	Income is recognised when is it earned, and expenses recognised as the expense is incurred
Conservatism	Financial accountant shall not overstate the value of assets and understate the value of liabilities

Sources of regulation for financial accounting

Minimum levels of disclosures are legislated
- Cant disclose what they prefer to disclose
- Disclose about social and environmental performance which are relatively unregulated

Major source of company regulation = corporation act
- Accounting standards

Assets: AASB conceptual framework's

Asset: a resource controlled by the entity as a result of a past even and from which future economic benefits are expected to flow to the entity

Ways to clarify assets

Current asset	- Expects to realise the asset, or intends to sell or consume it in its normal operating cycle - Holds the asset primarily for the purpose of trading - Expects to realise the asset within 12 months after the reporting - Asset is cash or cash equivalent, or used to settle a liability for at lest 12 months after the reporting
Tangible and intangible assets	Tangible - Assets that have a physical substance - E.g. plant and machinery, motor vehicles Intangible - Asset provide expected future benefits but have no physical substance - E.g. copyrights, patents
Property plant and equipment	Tangible item that - Are held for use in the production/supply of, goods and services, for rental to others, administrative purpose

	- Expected to be used during more than one period
Contra accounts	- Account with its balance to be the opposite of the normal balance found in an asset account

Liabilities

Liability: a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits

Ways to clarify liabilities

Current liability	- Expects to settle the liability in its normal operating cycle - Holds the liability in its normal operating cycle - Due to be settled within 12 months after the end of the reporting period - Does not have an unconditional right to defer settlement of the liability for at least 12 months after the reporting period
Provisions	- Estimated liability for which there is greater uncertainty regarding the among or timing of the amount that for a normal liability
Contingent liabilities	- A potential liability that might arise in the event of a particular event occurring

Owners' equity

Equity: the residual interest in the assets of the entity after deducting all its liabilities

Types of equity accounts

- Contributions
- Retained earnings
- Reserves
- Distributions/drawings

Income

Income: increases in economic benefits during the accounting period in the form of inflows of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants

Expense

Expense: decreases in economic benefits during the accounting period in the form of outflows of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants

The accounting equation

Asset = L + Oe

A E D = L I C

Module 4 topic 2: general purpose financial statements – further consideration of the balance sheet

Balance sheet

- Also known as the statement of financial position
- A, L, E at a point in time
- Relevance decreases with the passing of time
- Prepared at least once a year

Current assets

- Expected to be sold, consumed or used to create income within one year of the date of the balance sheet, or within the current operating cycle of the business
- Operating cycle of entity: time between the acquisition of assets for processing and their realisation in cash or cash equivalents
- Classifying as current allows us to identify which of those we are able to sell or liquidate easier
- Examples
  - Cash
  - Accounts receivable
  - Inventory
  - Prepaid expenses
  - Investments expected to be sold
- Assets not classified as current are called non-current

Measurement of assets

- Measurement: the amount assigned
- Not all assets measured on the same basis
  - Additivity problem: not all assets measured on the same basis
  - Mixed measurement approach
- Measurement bases
  - Cash
    - Measured at face value: value shown on the face of a security certificate, including currency
  - Debtors (accounts receivable)
    - Face value, less an allowance for doubtful debts
  - Inventory
    - Materials/supplies to be consumed in production process or rendering of services
    - Measured: lower of cost and net realisable value
    - Costs to include: cost of purchase, conversion and costs incurred into bringing it into the location and condition

Prepayments

Prepayments: adjustments that are made to ensure that expenses and income are recognised in the correct accounting period

Property, plant and equipment (P, P & E)

These are tangible items that:

- Held for use in the production or supply of goods or services, for rental to others or for administrative purposes
- Are expected to be used during more than one period

Measurement of P, P & E

Cost value	Revaluation model
Item carried at its cost, lest any accumulated depreciation and any accumulated impairment losses	Item measured at its fair value at the date of revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses Fair value: price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date Carrying value: amounts that the company has on its books for an asset or liability Recoverable amount: higher of an assets fair value less costs of disposal (net selling price) and its value in use Value in use: net presents value of a cash flow or other benefits that an asset generates for a specific owner under a specific use

Depreciation of P, P & E

- Expectation that their useful life, and related economic benefits is not indefinite (other than land)
- Depreciation: allocation of the cost of an asset over the periods in which benefits are expected to be generated by the asset
- when calculating depreciation judgements must be made about
  - depreciable base
  - useful life
  - appropriate method of cost apportionment

Straight-line method	Reducing balance method	Units of production
Allow the depreciation cost to be charged evenly throughout the useful life of the asset $$\textit{Depreciation expense per annum} = \frac{\textit{Cost} - \textit{Expected Residual Value}}{\textit{Expected Useful Life of the Asset}}$$	A fixed percentage is applied to the written-down value of the asset.	The calculation of depreciation expense is based on the productive capacity and actual use of the asset. $$\textit{Depreciation expense per annum} = \frac{\textit{Cost} - \textit{Expected Residual Value}}{\textit{Total estimated units}} \times \textit{units used in the period}$$

Intangible assets

Non-monetary assets without physical substance

- separately disclosed from other assets
- examples
    - brand names
    - mastheads, publishing titles
    - computer software
    - licenses and franchises
    - copyrights, property rights
    - recipes, formulae, models, design

summary of different asset measurement

Asset	Measurement rule
Cash	Face value
Debtors	Face value less an allowance for doubtful debts
Inventory	Lower of cost and net realisable value
Prepayments	Amortised cost (valued at cost which is reduced as it is used)
Property, plant and equipment	At cost or fair value
Marketable securities	Fair value
Intangible assets	Generally only externally acquired intangible assets can be recognised. Recognition is generally at cost given restrictions on revaluations
Leased assets	At the present value of the future lease payments

Current liabilities

Considered a current liability when

- expects to settle the liability in its normal operating cycle
- it holds the liability primary for the purpose of trading
- liability is due to be settled within 12 months after the reporting period
- does not have an unconditional right to defer settlement of the liability for at least 12 months after the reporting period

examples

- bank overdraft
- accounts payable
- accrued expenses
- dividends payable
- short term loans

measurement of liabilities

Bank overdraft	Line of credit designed to cover short term cash flow shortfalls and occurs when money is withdrawn from a bank account and the available balance goes below zero - CL measures at face value
Accounts payable	- Presented as CL measured at face value
Provisions	Some uncertainty about eh timing or amount of the future expenditure
Bonds	Organisation borrows funds and then is obliged to pay the bondholder interest on a periodic basis and also repay the principal at a later date - Measured at present value

Contingent liabilities

Contingent liability: obligation that is dependent upon a future even or where the obligation cannot be measured reliably at a given point in time

Equity

Examples of equity components

Share capital	Amount attributable to the amount paid by shareholders, to the company for their shares
Retained earnings	Accumulation of past profits (and losses) less aggregated dividends and less transfers of retained earnings to reserves
Reserves	Companies have numerous types of equity reserved e.g. transferring money out of retained earnings and into reserved to cover future expansion plans

Module 4 topic 3: general purpose of financial statements, income statement, statement of changes In equity and the statement of cash flows

The income statement
Provides details about the income and expenses of an organisation

Income: increases in economic benefit during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants

Expenses: decreases in economic benefits during the accounting period in the form of outflows of depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants

The reporting period
- Profit calculated for a period of time
- Life of a business expected to last indefinitely financial accounting breaks the life up into smaller time periods
- Financial year: July 1st to June 30

The use of accrual accounting
- Financial statements prepared on accrual basis
    - Income recognised when earned, expenses recognised when incurred

Prepayment
Occurs when a payment for a good or service Is made in advance of receiving it
- Asset

Income received in advance
Occurs when an organisation is paid for a good or service in advance of it being provided to a customer
- Liability

Income receivable
Arises when an organisation performs a service bust has not been paid for it

Depreciation
Represents another expense which is recognised in a period that generally different from when the underlying asset was acquired

Judgements required
- Accounting requires many judgments to be made
- Unlikely that different accounts will derive the same profits, assets and liabilities

Statement of changes in equity
role: provide a reconciliation of opening and closing equity, and to also provide detailed of the various equity accounts that are impacted on by the periods total comprehensive income

Statement of cash flows
purpose: provide detailed of the cash inflows and outflows of an organisation
- Provides a reconciliation of opening and closing cash

Operating	Principle revenue producing activities of the entity and other activities that aren't investing or financing, relate to the provision of goods and services	- Receipts from customers - Payments to suppliers and employees - Interested received - Cash generated from operations - Interest paid - Income taxes paid
Investing	The acquisition and/or disposal of long term assets (plant property equipment) and other investments not included in cash equivalents	- Purchase of property/plant and equipment - Proceeds from sale of equipment - Dividends received
Financing	Relating to changing the size and/or composition of the financial structure of the entity, including equity and borrowings not falling within the definition of cash	- Proceeds from uses of shares - Proceeds/ repayments from borrowings - Dividends paid - Share buybacks

Cash controls
Systematic measures put in place by an organisation to
- Conduct business in an orderly and efficient manner
- Safeguard its assets and resources
- Deter and detect errors, fraud and theft

Examples of internal controls
- Payments require authorisation and documentation
- All payments and receipts have evidence by pre-numbered documents
- Payments not directly made with tills
- Cash in tills regularly verified against internal register records