

Brief contents

Preface	xx
Publisher's acknowledgements	xxvi
Part 1	
INTRODUCTION TO ACCOUNTING ON A CASH FLOW AND ACCRUAL ACCOUNTING BASIS	1
1 Accounting and reporting on a cash flow basis	3
2 Accounting and reporting on an accrual accounting basis	21
Part 2	
PREPARATION OF INTERNAL AND PUBLISHED FINANCIAL STATEMENTS	31
3 Preparation of financial statements of comprehensive income, changes in equity and financial position	33
4 Annual report: additional financial disclosures	72
5 Statements of cash flows	104
Part 3	
REGULATORY FRAMEWORK – AN ATTEMPT TO ACHIEVE UNIFORMITY	133
6 Financial reporting – evolution of global standards	135
7 Concepts – evolution of an international conceptual framework	159
8 Ethical behaviour and implications for accountants	184
Part 4	
INCOME AND ASSET VALUE MEASUREMENT SYSTEMS	211
9 Income and asset value measurement: an economist's approach	213
10 Accounting for price-level changes	232
11 Revenue recognition	265

Part 5	
STATEMENT OF FINANCIAL POSITION – EQUITY, LIABILITY AND ASSET MEASUREMENT AND DISCLOSURE	291
12 Share capital, distributable profits and reduction of capital	293
13 Liabilities	317
14 Financial instruments	340
15 Employee benefits	371
16 Taxation in company accounts	400
17 Property, plant and equipment (PPE)	425
18 Leasing	460
19 Intangible assets	485
20 Inventories	515
21 Construction contracts	542
Part 6	
CONSOLIDATED ACCOUNTS	567
22 Accounting for groups at the date of acquisition	569
23 Preparation of consolidated statements of financial position after the date of acquisition	590
24 Preparation of consolidated statements of income, changes in equity and cash flows	603
25 Accounting for associates and joint arrangements	625
26 Introduction to accounting for exchange differences	651
Part 7	
INTERPRETATION	673
27 Earnings per share	675
28 Review of financial ratio analysis	701
29 Analysis of published financial statements	736
30 An introduction to digital financial reporting	779
Part 8	
ACCOUNTABILITY	805
31 Corporate governance	807
32 Integrated reporting: sustainability, environmental and social	843
Index	879

Contents

Preface	xx
Publisher's acknowledgements	xxvi
Part I	
INTRODUCTION TO ACCOUNTING ON A CASH FLOW AND ACCRUAL ACCOUNTING BASIS	1
1 Accounting and reporting on a cash flow basis	3
1.1 Introduction	3
1.2 Shareholders	3
1.3 What skills does an accountant require in respect of external reports?	4
1.4 Managers	4
1.5 What skills does an accountant require in respect of internal reports?	5
1.6 Procedural steps when reporting to internal users	5
1.7 Agency costs	8
1.8 Illustration of periodic financial statements prepared under the cash flow concept to disclose realised operating cash flows	8
1.9 Illustration of preparation of statement of financial position	13
1.10 Treatment of non-current assets in the cash flow model	14
1.11 What are the characteristics of these data that make them reliable?	15
1.12 Reports to external users	16
Summary	17
Review questions	18
Exercises	19
Notes	20
2 Accounting and reporting on an accrual accounting basis	21
2.1 Introduction	21
2.2 Historical cost convention	22
2.3 Accrual basis of accounting	22
2.4 Mechanics of accrual accounting – adjusting cash receipts and payments	23
2.5 Reformatting the statement of financial position	24
2.6 Accounting for the sacrifice of non-current assets	24
2.7 Published statement of cash flows	27

Summary	28
Review questions	28
Exercises	29
Notes	30
Part 2	
PREPARATION OF INTERNAL AND PUBLISHED FINANCIAL STATEMENTS	31
3 Preparation of financial statements of comprehensive income, changes in equity and financial position	33
3.1 Introduction	33
3.2 Preparing an internal statement of income from a trial balance	33
3.3 Reorganising the income and expenses into one of the formats required for publication	36
3.4 Format 1: classification of operating expenses and other income by function	37
3.5 Format 2: classification of operating expenses according to their nature	40
3.6 Other comprehensive income	40
3.7 How non-recurring or exceptional items can affect operating income	42
3.8 How decision-useful is the statement of comprehensive income?	44
3.9 Statement of changes in equity	44
3.10 The statement of financial position	45
3.11 The explanatory notes that are part of the financial statements	46
3.12 Has prescribing the formats meant that identical transactions are reported identically?	49
3.13 Fair presentation	51
3.14 What does an investor need in addition to the primary financial statements to make decisions?	53
Summary	58
Review questions	58
Exercises	60
Notes	70
4 Annual report: additional financial disclosures	72
4.1 Introduction	72
4.2 IAS 10 <i>Events after the Reporting Period</i>	72
4.3 IAS 8 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>	75
4.4 What do segment reports provide?	77
4.5 IFRS 8 <i>Operating Segments</i>	77
4.6 Benefits and continuing concerns following the issue of IFRS 8	81
4.7 Discontinued operations – IFRS 5 <i>Non-current Assets Held for Sale and Discontinued Operations</i>	83
4.8 Held for sale – IFRS 5 <i>Non-current Assets Held for Sale and Discontinued Operations</i>	84
4.9 IAS 24 <i>Related Party Disclosures</i>	86
Summary	91
Review questions	91
Exercises	92
Notes	103

5 Statements of cash flows	104
5.1 Introduction	104
5.2 Development of statements of cash flows	104
5.3 Applying IAS 7 (revised) Statements of Cash Flows	105
5.4 Step approach to preparation of a statement of cash flows – indirect method	108
5.5 Additional notes required by IAS 7	111
5.6 Analysing statements of cash flows	112
5.7 Approach to answering questions with time constraints	118
5.8 Preparing a statement of cash flows when no statement of income is available	120
5.9 Disclosure Initiative (Amendments to IAS 7)	122
5.10 Critique of cash flow accounting	123
Summary	123
Review questions	123
Exercises	124
Notes	132

Part 3

REGULATORY FRAMEWORK – AN ATTEMPT TO ACHIEVE UNIFORMITY 133

6 Financial reporting – evolution of global standards	135
6.1 Introduction	135
6.2 Why do we need financial reporting standards?	135
6.3 Why do we need standards to be mandatory?	136
6.4 Arguments in support of standards	138
6.5 Arguments against standards	138
6.6 Standard setting and enforcement by the Financial Reporting Council (FRC) in the UK	139
6.7 The International Accounting Standards Board	142
6.8 Standard setting and enforcement in the European Union (EU)	143
6.9 Standard setting and enforcement in the US	146
6.10 Advantages and disadvantages of global standards for publicly accountable entities	148
6.11 How do reporting requirements differ for non-publicly accountable entities?	149
6.12 IFRS for SMEs	150
6.13 Why have there been differences in financial reporting?	151
6.14 Move towards a conceptual framework	154
Summary	154
Review questions	155
Exercises	156
Notes	157

7 Concepts – evolution of an international conceptual framework 159

7.1 Introduction	159
7.2 Different countries meant different financial statements	159

7.3	Historical overview of the evolution of financial accounting theory	160
7.4	Developing a Framework for the Preparation and Presentation of Financial Statements	162
7.5	Conceptual Framework for Financial Reporting 2018	163
7.6	Current developments – concept of materiality	179
	Summary and evaluation of position to date	180
	Review questions	180
	Exercises	181
8	Ethical behaviour and implications for accountants	184
8.1	Introduction	184
8.2	The meaning of ethical behaviour	184
8.3	The accounting standard-setting process and ethics	185
8.4	The International Code of Ethics for Professional Accountants	186
8.5	Implications of ethical values for the principles versus rules-based approaches to accounting standards	189
8.6	Ethics in the accountant's work environment – a research report	193
8.7	Implications of unethical behaviour for stakeholders using the financial reports	194
8.8	The increasing role of whistle-blowing	199
8.9	Legal requirement to report – national and international regulation	201
8.10	Why should students learn ethics?	202
	Summary	203
	Review questions	204
	Exercises	206
	Notes	208
Part 4		
	INCOME AND ASSET VALUE MEASUREMENT SYSTEMS	211
9	Income and asset value measurement: an economist's approach	213
9.1	Introduction	213
9.2	Role and objective of income measurement	213
9.3	Accountant's view of income, capital and value	216
9.4	Critical comment on the accountant's measure	219
9.5	Economist's view of income, capital and value	220
9.6	Critical comment on the economist's measure	226
9.7	Income, capital and changing price levels	226
	Summary	228
	Review questions	228
	Exercises	229
	Notes	231
	Bibliography	231

10 Accounting for price-level changes	232
10.1 Introduction	232
10.2 Review of the problems of historical cost accounting (HCA)	232
10.3 Inflation accounting	233
10.4 The concepts in principle	233
10.5 The four models illustrated for a company with cash purchases and sales	234
10.6 Critique of each model	238
10.7 Operating capital maintenance – a comprehensive example	241
10.8 Critique of CCA statements	252
10.9 Measurement bases	253
10.10 The IASB position where there is hyperinflation	253
10.11 Future developments	254
Summary	256
Review questions	257
Exercises	257
Notes	264
Bibliography	264
11 Revenue recognition	265
11.1 Introduction	265
11.2 IAS 18 <i>Revenue</i>	266
11.3 The issues involved in developing a new standard	267
11.4 The challenges under both IAS 18 and IFRS 15	268
11.5 IFRS 15 Revenue from Contracts with Customers	269
11.6 Five-step process to identify the amount and timing of revenue	270
11.7 Disclosures	281
Summary	282
Review questions	282
Exercises	284
Notes	289
Part 5	
STATEMENT OF FINANCIAL POSITION – EQUITY, LIABILITY AND ASSET MEASUREMENT AND DISCLOSURE	291
12 Share capital, distributable profits and reduction of capital	293
12.1 Introduction	293
12.2 Common themes	293
12.3 Total owners' equity: an overview	294
12.4 Total shareholders' funds: more detailed explanation	295
12.5 Accounting entries on issue of shares	297
12.6 Creditor protection: capital maintenance concept	298
12.7 Creditor protection: why capital maintenance rules are necessary	298
12.8 Creditor protection: how to quantify the amounts available to meet creditors' claims	299
12.9 Issued share capital: minimum share capital	300

12.10	Distributable profits: general considerations	300
12.11	Distributable profits: how to arrive at the amount using relevant accounts	302
12.12	When may capital be reduced?	302
12.13	Writing off part of capital which has already been lost and is not represented by assets	302
12.14	Repayment of part of paid-in capital to shareholders or cancellation of unpaid share capital	308
12.15	Purchase of own shares	308
	Summary	310
	Review questions	311
	Exercises	311
	Notes	316
13	Liabilities	317
13.1	Introduction	317
13.2	Provisions – a decision tree approach to their impact on the statement of financial position	318
13.3	Treatment of provisions	319
13.4	The general principles that IAS 37 applies to the recognition of a provision	319
13.5	Management approach to measuring the amount of a provision	320
13.6	Application of criteria illustrated	322
13.7	Provisions for specific purposes	322
13.8	Contingent liabilities	325
13.9	Contingent assets	325
13.10	ED IAS 37 <i>Non-financial Liabilities</i>	326
13.11	ED/2010/1 <i>Measurement of Liabilities in IAS 37</i>	332
	Summary	334
	Review questions	334
	Exercises	335
	References	339
14	Financial instruments	340
14.1	Introduction	340
14.2	Financial instruments – the IASB's problem child	340
14.3	IAS 32 <i>Financial Instruments: Disclosure and Presentation</i>	342
14.4	IFRS 9 <i>Financial Instruments</i>	347
14.5	IFRS 7 <i>Financial Instruments: Disclosure</i>	357
	Summary	362
	Review questions	363
	Exercises	364
	Notes	370
15	Employee benefits	371
15.1	Introduction	371
15.2	Greater employee interest in pensions	371
15.3	Financial reporting implications	372
15.4	Types of scheme	373

15.5	Defined contribution pension schemes	375
15.6	Defined benefit pension schemes	376
15.7	IAS 19 (revised 2011) <i>Employee Benefits</i>	376
15.8	The asset or liability for pension and other post-retirement costs	377
15.9	Changes in the pension asset or liability position	378
15.10	Comprehensive illustration	380
15.11	Multi-employer plans	383
15.12	Disclosures	383
15.13	Other long-service benefits	383
15.14	Short-term benefits	384
15.15	Termination benefits	385
15.16	IFRS 2 Share-based Payment	385
15.17	Scope of IFRS 2	386
15.18	Recognition and measurement	387
15.19	Equity-settled share-based payments	387
15.20	Cash-settled share-based payments	390
15.21	Transactions which may be settled in cash or shares	390
15.22	IAS 26 Accounting and Reporting by Retirement Benefit Plans	391
	Summary	394
	Review questions	394
	Exercises	395
	Notes	399
16	Taxation in company accounts	400
16.1	Introduction	400
16.2	Corporation tax	400
16.3	Corporation tax systems – the theoretical background	401
16.4	Dividends pre and post 2016	402
16.5	Corporation tax systems – avoidance and evasion	403
16.6	IAS 12 – accounting for current taxation	408
16.7	Deferred tax	409
16.8	A critique of deferred taxation	417
16.9	Value added tax (VAT)	418
	Summary	419
	Review questions	420
	Exercises	421
	Notes	424
17	Property, plant and equipment (PPE)	425
17.1	Introduction	425
17.2	PPE – concepts and the relevant IASs and IFRSs	425
17.3	What is PPE?	426
17.4	How is the cost of PPE determined?	427
17.5	What is depreciation?	429
17.6	What are the constituents in the depreciation formula?	430
17.7	Calculation of depreciation	432
17.8	Measurement subsequent to initial recognition	436
17.9	IAS 36 <i>Impairment of Assets</i>	438
17.10	IFRS 5 <i>Non-current Assets Held for Sale and Discontinued Operations</i>	443

17.11	Disclosure requirements	444
17.12	Government grants towards the cost of PPE	445
17.13	Investment properties	447
17.14	Effect of accounting policy for PPE on the interpretation of the financial statements	448
	Summary	451
	Review questions	451
	Exercises	452
	Notes	459
18	Leasing	460
18.1	Introduction	460
18.2	Need for an accounting standard on leasing	461
18.3	Terms and conditions of a lease	466
18.4	Leases in the financial statements of lessees under IFRS 16	468
18.5	Leases in the financial statements of lessors	473
18.6	Sale and leaseback transactions	475
	Summary	479
	Review questions	479
	Exercises	481
19	Intangible assets	485
19.1	Introduction	485
19.2	Intangible assets defined	486
19.3	Accounting treatment for research and development	489
19.4	Why is research expenditure not capitalised?	490
19.5	Capitalising development costs	491
19.6	Disclosure of R&D	491
19.7	<i>IFRS for SMEs'</i> treatment of intangible assets	492
19.8	Internally generated and purchased goodwill	492
19.9	The accounting treatment of goodwill	493
19.10	Critical comment on the various methods that have been used to account for goodwill	495
19.11	Negative goodwill/Badwill	497
19.12	Brands	498
19.13	Accounting for acquired brands	500
19.14	Intellectual capital disclosures (ICDs) in the annual report	500
19.15	Review of implementation of IFRS 3	502
19.16	Review of implementation of identified intangibles under IAS 38	502
	Summary	504
	Review questions	504
	Exercises	505
	Notes	512

20 Inventories	515
20.1 Introduction	515
20.2 Inventory defined	515
20.3 The impact of inventory valuation on profits	516
20.4 IAS 2 <i>Inventories</i>	517
20.5 Inventory valuation	518
20.6 Work in progress	524
20.7 Inventory control	526
20.8 Creative accounting	527
20.9 Audit of the year-end physical inventory count	529
20.10 Published accounts	531
20.11 Agricultural activity	532
Summary	534
Review questions	535
Exercises	535
Notes	541
21 Construction contracts	542
21.1 Introduction	542
21.2 The need to replace IAS 11 <i>Construction Contracts</i>	543
21.3 Identification of contract revenue under IAS 11	544
21.4 Identification of contract costs under IAS 11	545
21.5 IFRS 15 treatment of construction contracts	547
21.6 An approach when a contract can be separated into components	549
21.7 Accounting for a contract – an example	550
21.8 Illustration – loss-making contract using the step approach	552
21.9 Public–private partnerships (PPPs)	554
Summary	557
Review questions	558
Exercises	558
Notes	565
Part 6	
CONSOLIDATED ACCOUNTS	567
22 Accounting for groups at the date of acquisition	569
22.1 Introduction	569
22.2 Preparing consolidated accounts for a wholly owned subsidiary	569
22.3 IFRS 10 <i>Consolidated Financial Statements</i>	569
22.4 Fair values	571
22.5 Illustration where there is a wholly owned subsidiary	572
22.6 Preparing consolidated accounts when there is a partly owned subsidiary	573
22.7 The treatment of differences between a subsidiary's fair value and book value	576
22.8 The parent issues shares to acquire shares in a subsidiary	577
22.9 IFRS 3 <i>Business Combinations</i> treatment of goodwill at the date of acquisition	578

22.10	When may a parent company not be required to prepare consolidated accounts?	579
22.11	When may a parent company exclude or not exclude a subsidiary from a consolidation?	579
22.12	IFRS 13 <i>Fair Value Measurement</i>	580
22.13	What advantages are there for stakeholders from requiring groups to prepare consolidated accounts?	581
	Summary	582
	Review questions	582
	Exercises	583
	Notes	589
23	Preparation of consolidated statements of financial position after the date of acquisition	590
23.1	Introduction	590
23.2	Uniform accounting policies and reporting dates	590
23.3	Pre- and post-acquisition profits/losses	590
23.4	The Bend Group – assuming there have been no inter-group transactions	591
23.5	Inter-company transactions	593
23.6	The Prose Group – assuming there have been inter-group transactions	594
	Summary	596
	Review questions	597
	Exercises	597
	Notes	602
24	Preparation of consolidated statements of income, changes in equity and cash flows	603
24.1	Introduction	603
24.2	Eliminate inter-company transactions	603
24.3	Preparation of a consolidated statement of income – the Ante Group	604
24.4	The statement of changes in equity (SOCE)	606
24.5	Other consolidation adjustments	606
24.6	A subsidiary acquired part-way through the year	608
24.7	Published format statement of income	610
24.8	Consolidated statements of cash flows	611
	Summary	613
	Review questions	613
	Exercises	614
	Notes	624
25	Accounting for associates and joint arrangements	625
25.1	Introduction	625
25.2	Definitions of associates and of significant influence	625
25.3	The treatment of associated companies in consolidated accounts	626
25.4	The Brill Group – group accounts with a profit-making associate	626
25.5	The Brill Group – group accounts with a loss-making associate	629
25.6	The acquisition of an associate part-way through the year	631

25.7	Joint arrangements	632
25.8	Disclosure in the financial statements	636
25.9	Parent company use of the equity method in its separate financial statements	637
	Summary	639
	Review questions	639
	Exercises	640
	Notes	650
26	Introduction to accounting for exchange differences	651
26.1	Introduction	651
26.2	How to record foreign currency transactions in a company's own books	652
26.3	Boil plc – a more detailed illustration	654
26.4	IAS 21 <i>Concept of Functional and Presentation Currencies</i>	655
26.5	Translating the functional currency into the presentation currency	657
26.6	Preparation of consolidated accounts	657
26.7	How to reduce the risk of translation differences	661
26.8	Critique of the use of presentational currency	662
26.9	IAS 29 <i>Financial Reporting in Hyperinflationary Economies</i>	662
	Summary	664
	Review questions	664
	Exercises	665
	Notes	672
Part 7		
INTERPRETATION		673
27	Earnings per share	675
27.1	Introduction	675
27.2	Why is the earnings per share figure important?	675
27.3	How is the EPS figure calculated?	676
27.4	The use to shareholders of the EPS	677
27.5	Illustration of the basic EPS calculation	678
27.6	Adjusting the number of shares used in the basic EPS calculation	678
27.7	Rights issues	681
27.8	Adjusting the earnings and number of shares used in the diluted EPS calculation	686
27.9	Procedure where there are several potential dilutions	688
27.10	Exercise of conversion rights during the financial year	690
27.11	Disclosure requirements of IAS 33	690
27.12	Enhanced disclosures	692
	Summary	693
	Review questions	693
	Exercises	694
	Notes	700

28 Review of financial ratio analysis	701
28.1 Introduction	701
28.2 Overview of techniques for the analysis of financial data	702
28.3 Ratio analysis – a case study	703
28.4 Introductory review	704
28.5 Financial statement analysis, part 1 – financial performance	707
28.6 Financial statement analysis, part 2 – liquidity	714
28.7 Financial statement analysis, part 3 – financing	717
28.8 Peer comparison	719
28.9 Report based on the analysis	720
28.10 Caution when using ratios for prediction	721
Summary	723
Review questions	723
Exercises	724
Note	735
29 Analysis of published financial statements	736
29.1 Introduction	736
29.2 Improvement of information for shareholders	737
29.3 Published financial statements – their limitations for interpretation purposes	739
29.4 Published financial statements – additional entity-wide cash-based performance measures	740
29.5 Ratio thresholds to satisfy Shariah compliance	743
29.6 Use of ratios in restrictive loan covenants	744
29.7 Investor-specific ratios	747
29.8 Predicting corporate failure	752
29.9 Professional risk assessors	756
29.10 Valuing shares of an unquoted company – quantitative process	757
29.11 Valuing shares of an unquoted company – qualitative process	760
29.12 Possible effect of 'Brexit' on financial statements	762
Summary	763
Review questions	764
Exercises	765
Notes	777
30 An introduction to digital financial reporting	779
30.1 Introduction	779
30.2 The objectives of financial reporting	779
30.3 Reports and the flow of information pre-XBRL	781
30.4 What are HTML, XML and XBRL?	782
30.5 Reports and the flow of information post-XBRL	783
30.6 Why are companies adopting XBRL?	784
30.7 What are the processes followed to adopt XBRL for outputting information?	788
30.8 What is needed when receiving XBRL output information?	791
30.9 Progress of XBRL development for internal accounting	796
30.10 Real-time reporting	796
30.11 Stakeholder interaction with XBRL data	798

Summary	799
Review questions	800
Exercises	800
Notes	802
Part 8	
ACCOUNTABILITY	805
31 Corporate governance	807
31.1 Introduction	807
31.2 A systems perspective	807
31.3 Different jurisdictions have different governance priorities	809
31.4 Pressures on good governance behaviour vary over time	810
31.5 Types of past unethical behaviour	811
31.6 The effect on capital markets of good corporate governance	812
31.7 Risk management	813
31.8 The role of internal control, internal audit and audit committees in corporate governance	814
31.9 External audits in corporate governance	816
31.10 Executive remuneration in the UK	822
31.11 Corporate governance, legislation and codes	826
31.12 Corporate governance – the UK experience	827
Summary	835
Review questions	835
Exercises	838
Notes	840
32 Integrated reporting: sustainability, environmental and social	843
32.1 Introduction	843
32.2 Environmental and social disasters, the adverse consequences that can follow and the lessons to be learnt	844
32.3 Management accountability for environmental and social responsibility	846
32.4 Integrated reporting concepts	850
32.5 The historical context of the evolution of integrated reporting including the drivers of this movement	854
32.6 The efforts on which integrated reporting builds	858
32.7 The contribution of accountants	862
32.8 Integrated reporting – its impact on the future development of financial reporting and accounting	867
Review questions	869
Exercises	871
Notes	876
Index	879