CHAPTER 11: INVESTMENTS

DEBT SECURITIES

- include government bonds – both US Treasury and municipal bonds
- corporate bonds, preferred stock, convertible bonds,
- also include collateralized securities – eg – collateralized debt obligations, commercial paper

EQUITY SECURITIES

- instruments that signify ownership interests in company assets and profits
- eg – common stock, preferred stock, and other capital stock
- company may also hold derivatives such as warrants or call options

TRADING SECURITIES

- entity is holding the securities but will sell the securities quickly
- usually recorded as a current asset
- recorded at fair value – eg – mark to market
- unrealized and realized gains and losses are recorded as income

AVAILABLE-FOR-SALE-SECURITIES

- entity will hold the securities and will sell when cash is required
- recorded as current asset or non-current asset on balance sheet
- recorded at fair value – eg – mark to market
- changes in fair value are <u>not</u> recorded as income

HELD-TO-MATURITY SECURITIES

- purchased with the intent to hold the securities to maturity
- recorded as current asset or non-current asset on balance sheet
- recorded at amortized cost
- unrealized gains and losses are not included in earnings

- realized gains and losses do not exist if securities held to maturity

CHAPTER 12: IFRS

- International Financial Reporting Standards (IFRS) are guidelines and rules set by the International Accounting Standards Board (IASB)
- Big difference between US GAAP and IFRS is that US GAAP employs a rules based approach, as the standards are usually explicit as to precise rules that must be followed for recognition, measurement, and financial statement presentation
- IFRS is considered a principle based approach, as it attempts to set general principles for recognition, measurement and reporting, and allows professional judgment in applying these principles.

IASB FRAMEWORK

The Framework sets forth 4 principal qualitative characteristics of financial statements:

Relevance

- Information must be useful to the user in making the decision (capable of influencing the users decision)
- Some of the attributes of relevance include:
- Predictive value – historical info can be used to help predict the future
- Confirmatory value – use the info to confirm to prior expectations and to assess managements performance

Reliability

- Information is reliable and free from material error and bias if it has the following characteristics:
- Neutrality – free of bias
- Faithful representation – info should faithfully represent the economic events and transactions in the statements
- Substance over form – accounting should reflect the substance of a transaction and look beyond its legal form

- Prudence – use caution in exercising judgment when uncertainty
- Completeness – complete information regarding material items is critical for decision making

Understandability

- information must be understandable to users

Comparability

- Need for users to be able to compare financial statements globally of different entities to evaluate their financial position and performance
- Comparability requires accounting policies to be disclosed
- Additionally financial statements have corresponding information for preceding periods (consistency)

ASSUMPTIONS USED IN IASB FRAMEWORK

- Financial statements are prepared on the accrual basis of accounting
- Entity is a going concern

CONSTRAINTS

- The two constraints for relevant and reliable information are:
- Timeliness – if information is not timely, it can lose relevance
- Benefit > Cost – benefits derived from the information should exceed the cost of providing it

FINANCIAL STATEMENT PRESENTATION DIFFERENCES

- The table below highlights the major accounting differences between US GAAP and IFRS

IFRS Key Points:

Fixed Assets	Leases	Deferred Taxes
• impairment losses may be reversed in future • revaluation of assets is permitted but must be done for whole class of assets	• operating leases may be capitalized by lessee • IFRS does not specify % economic life for capital leases	• deferred tax assets are recognized only to extent it is probable they will be realized • all deferred tax liabilities reported • reported as non-current assets and liabilities on Statement of Financial Position

Financial Statements	Long Term Contracts	Inventory
• comparative information required • reporting of extraordinary gains/losses not allowed • statement of comprehensive income is required • statement of changes in equity required	• completed contract method not allowed	• LIFO not allowed • market is net realizable value • assets written down to market value can be written back up if value rebounds

Contingent Liabilities

- recognized when loss is probable and reasonably estimated
- present value is use for material contingent liabilities

R&D Costs

- R&D expensed as incurred
- may be capitalized if intangible asset is technologically feasible and most likely to be sold in future

Statement of Cash Flows

- interest expense or finance costs can be reported as operating or financing costs
- you cannot switch to a new classification for future costs

Intangible Assets

- value using cost model or revaluation model

Pensions

- project-unit-credit method calculates the PV of the defined benefit obligation
- prior service costs is expensed immediately for employees who have vested

Convertible Debts

- part of the proceeds are recorded as liability and part as stockholders' equity