



FINANCIAL REPORTING

S1 Notebook: Regulatory framework

In this section you will learn about:

The Conceptual Framework,
IAS 1 Presentation of Financial Statements;
IAS 7 Statement of Cash Flows;
IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors;
IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

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1.1 BEFORE YOU START

1.1.1 Introduction movie

Here you may take your own notes 😊

1.1.2 About this exam

1.1.3 Prior knowledge requirements

 Now it is time for you to check your understanding. Note your answers to the quiz:

1.2 REGULATORY FRAMEWORK

1.2.1 International Financial Reporting Standards

1.2.1.1 *International Accounting Standards Board (IASB)*

1.2.1.2 *International Financial Reporting Standards (IFRS) Foundation*

IFRS Foundation is

The IFRS Foundation has 4 main objectives:

1. _____
2. _____
3. _____
4. _____

1.2.1.3 *The IFRS Interpretation Committee (IFRS IC)*

1.2.1.4 *The IFRS Advisory Council (IFRS AC)*

1.2.2 The Conceptual Framework for financial reporting

Information extracted from: <https://www.ifrs.org/-/media/project/conceptual-framework/fact-sheet-project-summary-and-feedback-statement/conceptual-framework-project-summary.pdf>

The Conceptual Framework's purpose is to:

1. Assist the Board to
2. Assist the preparers of financial reports to
3. To assist

The Revised Conceptual Framework sets out:

1. the _____ of financial reporting
2. the _____ of useful financial information
3. a description of the _____ and its _____
4. definitions of _____, _____, _____, _____ and _____
5. the _____ for _____ assets and liabilities in financial statements (the _____ criteria) and guidance on when to _____ them (the _____ criteria)
6. _____ and guidance on when to use them
7. concepts and guidance on _____ and _____

1.2.3 The objective of financial reporting.

To provide financial information that is _____ to _____ in _____

Type of users' decisions:

--	--	--

Users need to assess:

--	--

Information needed:

--	--

1.2.4 The qualitative characteristics of useful financial information

The FUNDAMENTALS characteristics are:

1.2.4.1 *Relevance*

1.2.4.2 *Faithful representation*

The ENHANCING characteristics are:

1.2.4.3 *Verifiability*

1.2.4.4 *Comparability*

1.2.4.5 *Understandability*

1.2.4.6 *Timeliness*

1.2.4.7 *“Cost constraint”*

1.2.5 Financial statements and the reporting unit

The reporting unit is that entity that is _____, or _____, to prepare financial statements.

The financial statements are a particular form of _____ that provide information about the reporting entity's _____, _____, _____, _____ and _____.

The financial statements might be:

1. _____ financial statements: provide information about assets, liabilities and equity, income and expenses of _____
2. _____ financial statements: provide information about assets, liabilities and equity, income and expenses of _____
3. _____ financial statements: provide information about assets, liabilities and equity, income and expenses of _____

1.2.6 The elements of financial statements

The balance sheet elements are:

Asset = a present _____ controlled by the entity as a result of past events.

An economic resource is a _____ that has the potential to produce _____.

Liability = a present _____ of the entity to transfer _____ as a result of past events.

An obligation is a duty or responsibility that the entity has _____

Equity = the _____ in the assets of the entity after deducting all its liabilities.

The unit of account = the right(s) or obligation(s), or group of rights and obligations, to which similar _____ criteria and _____ concepts are applied.

The income statement elements are:

Income = any _____ in assets, or _____ in liabilities, that result in increases in _____, other than those relating to contributions from holders of equity claims

Expenses = any _____ in assets, or _____ in liabilities, that result in decreases in _____, other than those relating to distributions to holders of equity claims.

1.2.7 Recognition and derecognition

Recognition = the process of _____ in the statement of financial position or the statement(s) of financial performance an item that meets the definition of an asset, a liability, equity, income or expenses

Recognition is appropriate if it results in both _____ information about assets, liabilities, equity, income and expenses and _____ .

Relevance may be affected, for example by:

1. _____
2. _____

Faithful representation may be affected by:

3. _____
4. _____
5. _____

Derecognition = the _____ of all or part of a recognised asset or liability from an entity's statement of financial position

Derecognition normally occurs:

For an asset – when the entity _____

For a liability - when the entity _____

Derecognition aims to faithfully represents both

- any _____ and _____ retained after the transaction that led to the derecognition AND
- the _____ in the entity's assets and liabilities as a result of that transaction

1.2.8 Measurement

The conceptual framework recognises two measurement bases: _____ cost and _____ value.

Historical cost:

- provides information derived from _____
- historical cost of assets is reduced if they become _____ and historical cost of liabilities is increased if they become _____
- one way to apply a historical cost measurement basis to financial assets and financial liabilities is to measure them at _____

Historical cost is _____, _____, _____, _____, _____

but it has its disadvantages: _____; _____; _____; _____; _____

Current value:

- provides information _____
- its measurement bases include: _____, _____ and _____

Fair value:

= _____

Reflects _____

Value in use or fulfilment value

Reflects _____

Assesses the value of the asset _____

Current cost

Reflects _____

Differs from historical cost since _____

The factors to be considered when selecting a measurement basis are _____ and _____.

Relevance of information provided by a measurement basis is affected by:

1. _____
2. _____
3. _____
4. _____
5. _____
6. _____

Whether a measurement basis can provide or not a **faithful representation** is affected by:

1. _____
2. _____

1.2.9 Presentation and disclosure

 Now it is time for you to check your understanding. Note your answers to the quiz:

1.3 PRESENTATION OF FINANCIAL STATEMENTS (IAS 1)

1.3.1 The financial statements

Financial statements present to their readers information about:

1. _____
2. _____
3. _____

The financial position of the entity _____ is shown through the Statement of financial position (SoFP)

[click]

The financial performance of the entity _____ is shown through:

- Statement of profit or loss and other comprehensive income (SoPoLOCI) as one statement or as two separate statements
- Statement of changes in equity (SoCE) which shows how the wealth of the owners of the company _____ and also shows _____

How cash was generated or spend is shown through _____

All these statements must be accompanied by

● _____ to the accounts: _____

● Comparatives – _____

Very important information to be included in each set of FS are:

1. _____
2. _____
3. _____
4. _____
5. _____

1.3.2 The purpose of IAS 1

The purpose of IAS 1 (revised) is to enhance the quality of financial statements by:

1. _____
2. _____
3. _____
4. _____

1.3.3 General features of financial statements

1. _____ – _____
2. _____ – _____
3. _____ – _____
4. _____ – _____
5. _____ – _____
6. _____ – _____
7. _____ – _____

1.3.4 SoFP

NETFLIX, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)

	As of December 31,	
	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 5,018,437	\$ 3,794,483
Current content assets, net	—	5,151,186
Other current assets	1,160,067	748,466
Total current assets	6,178,504	9,694,135
Non-current content assets, net	24,504,567	14,951,141
Property and equipment, net	565,221	418,281
Other non-current assets	2,727,420	910,843
Total assets	<u>\$ 33,975,712</u>	<u>\$ 25,974,400</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Current content liabilities	\$ 4,413,561	\$ 4,681,562
Accounts payable	674,347	562,985
Accrued expenses and other liabilities	843,043	481,874
Deferred revenue	924,745	760,899
Total current liabilities	6,855,696	6,487,320
Non-current content liabilities	3,334,323	3,759,026
Long-term debt	14,759,260	10,360,058
Other non-current liabilities	1,444,276	129,231
Total liabilities	26,393,555	20,735,635
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized at December 31, 2019 and 2018; no shares issued and outstanding at December 31, 2019 and 2018	—	—
Common stock, \$0.001 par value; 4,990,000,000 shares authorized at December 31, 2019 and December 31, 2018, respectively; 438,806,649 and 436,598,597 issued and outstanding at December 31, 2019 and December 31, 2018, respectively	2,793,929	2,315,988
Accumulated other comprehensive loss	(23,521)	(19,582)
Retained earnings	4,811,749	2,942,359
Total stockholders' equity	7,582,157	5,238,765
Total liabilities and stockholders' equity	<u>\$ 33,975,712</u>	<u>\$ 25,974,400</u>

See accompanying notes to consolidated financial statements.

1.3.5 SoPoLOCI

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NETFLIX, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

	Year ended December 31,		
	2019	2018	2017
Revenues	\$ 20,156,447	\$ 15,794,341	\$ 11,692,713
Cost of revenues	12,440,213	9,967,538	8,033,000
Marketing	2,652,462	2,369,469	1,436,281
Technology and development	1,545,149	1,221,814	953,710
General and administrative	914,369	630,294	431,043
Operating income	2,604,254	1,605,226	838,679
Other income (expense):			
Interest expense	(626,023)	(420,493)	(238,204)
Interest and other income (expense)	84,000	41,725	(115,154)
Income before income taxes	2,062,231	1,226,458	485,321
Provision for (benefit from) income taxes	195,315	15,216	(73,608)
Net income	\$ 1,866,916	\$ 1,211,242	\$ 558,929
Earnings per share:			
Basic	\$ 4.26	\$ 2.78	\$ 1.29
Diluted	\$ 4.13	\$ 2.68	\$ 1.25
Weighted-average common shares outstanding:			
Basic	437,799	435,374	431,885
Diluted	451,765	451,244	446,814

See accompanying notes to consolidated financial statements.

NETFLIX, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)

	Year ended December 31,		
	2019	2018	2017
Net income	\$ 1,866,916	\$ 1,211,242	\$ 558,929
Other comprehensive income (loss):			
Foreign currency translation adjustments	(3,939)	975	27,409
Change in unrealized gains (losses) on available-for-sale securities, net of tax of \$0, \$0, and \$378, respectively	—	—	599
Total other comprehensive income (loss)	(3,939)	975	28,008
Comprehensive income	\$ 1,862,977	\$ 1,212,217	\$ 586,937

See accompanying notes to consolidated financial statements.

1.3.6 SoCE

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NETFLIX, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except share data)

	Common Stock and Additional Paid-in Capital		Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
	Shares	Amount			
Balances as of December 31, 2016	430,054,212	\$ 1,599,762	\$ (48,565)	\$ 1,128,603	\$ 2,679,800
Net income	—	—	—	558,929	558,929
Other comprehensive income	—	—	28,008	—	28,008
Issuance of common stock upon exercise of options	3,338,474	89,425	—	—	89,425
Stock-based compensation expense	—	182,209	—	—	182,209
Cumulative Effect Adjustment of ASU 2016-09	—	—	—	43,585	43,585
Balances as of December 31, 2017	433,392,686	\$ 1,871,396	\$ (20,557)	\$ 1,731,117	\$ 3,581,956
Net income	—	—	—	1,211,242	1,211,242
Other comprehensive income	—	—	975	—	975
Issuance of common stock upon exercise of options	3,205,911	123,935	—	—	123,935
Stock-based compensation expense	—	320,657	—	—	320,657
Balances as of December 31, 2018	436,598,597	\$ 2,315,988	\$ (19,582)	\$ 2,942,359	\$ 5,238,765
Net income	—	—	—	1,866,916	1,866,916
Other comprehensive loss	—	—	(3,939)	—	(3,939)
Issuance of common stock upon exercise of options	2,208,052	72,565	—	—	72,565
Stock-based compensation expense	—	405,376	—	—	405,376
Adoption of ASU 2016-02, Leases (Topic 842)	—	—	—	2,474	2,474
Balances as of December 31, 2019	438,806,649	\$ 2,793,929	\$ (23,521)	\$ 4,811,749	\$ 7,582,157

See accompanying notes to consolidated financial statements.

1.3.7 IAS 7 Statement of Cash Flow

The benefits of Cash Flow are:

1. Helps in assessing _____
2. Helps in assessing _____
3. Offers a different view on the _____
4. Helps in assessing _____

The Statement of Cash Flows shows _____

Cash equivalents is _____

1.3.8 SCF

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NETFLIX, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended December 31,		
	2019	2018	2017
Cash flows from operating activities:			
Net income	\$ 1,866,916	\$ 1,211,242	\$ 558,929
Adjustments to reconcile net income to net cash used in operating activities:			
Additions to streaming content assets	(13,916,683)	(13,043,437)	(9,805,763)
Change in streaming content liabilities	(694,011)	999,880	900,006
Amortization of streaming content assets	9,216,247	7,532,088	6,197,817
Depreciation and amortization of property, equipment and intangibles	103,579	83,157	71,911
Stock-based compensation expense	405,376	320,657	182,209
Other non-cash items	228,230	81,640	117,864
Foreign currency remeasurement loss (gain) on long-term debt	(45,576)	(73,953)	140,790
Deferred taxes	(94,443)	(85,520)	(208,688)
Changes in operating assets and liabilities:			
Other current assets	(252,113)	(200,192)	(234,090)
Accounts payable	96,063	199,198	74,559
Accrued expenses and other liabilities	157,778	150,422	114,337
Deferred revenue	163,846	142,277	177,974
Other non-current assets and liabilities	(122,531)	2,062	(73,803)
Net cash used in operating activities	(2,887,322)	(2,680,479)	(1,785,948)
Cash flows from investing activities:			
Purchases of property and equipment	(253,035)	(173,946)	(173,302)
Change in other assets	(134,029)	(165,174)	(60,409)
Purchases of short-term investments	—	—	(74,819)
Proceeds from sale of short-term investments	—	—	320,154
Proceeds from maturities of short-term investments	—	—	22,705
Net cash provided by (used in) investing activities	(387,064)	(339,120)	34,329
Cash flows from financing activities:			
Proceeds from issuance of debt	4,469,306	3,961,852	3,020,510
Debt issuance costs	(36,134)	(35,871)	(32,153)
Proceeds from issuance of common stock	72,490	124,502	88,378
Other financing activities	—	(1,956)	255
Net cash provided by financing activities	4,505,662	4,048,527	3,076,990
Effect of exchange rate changes on cash, cash equivalents and restricted cash	469	(39,682)	29,848
Net increase in cash, cash equivalents and restricted cash	1,231,745	989,246	1,355,219
Cash, cash equivalents and restricted cash, beginning of year	3,812,041	2,822,795	1,467,576
Cash, cash equivalents and restricted cash, end of year	\$ 5,043,786	\$ 3,812,041	\$ 2,822,795
Supplemental disclosure:			
Income taxes paid	\$ 400,658	\$ 131,069	\$ 113,591
Interest paid	599,132	375,831	213,313

See accompanying notes to consolidated financial statements.

You can find the notes and the accounting policies at:

https://s22.q4cdn.com/959853165/files/doc_financials/2019/ar/2019-10-K.pdf

1.3.9 Exam style question

FIRST TRY Ltd presented for the year ended 202X the following trial balance:

Account	Db/(Cr) (\$)
Vehicles at cost (2 with a useful life of 5 years)	50,000
Accumulated depreciation of vehicles @ 1 January 202X	(5,000)
Trade Receivables	45,500
Cash	27,800
Inventory @ 1 January 202X	15,800
Allowance for trade receivables @ 1 January 202X	(2,300)
Purchases	144,100
Trade payables	(38,700)
Share capital (2 mil shares @ \$0.01/share)	(20,000)
Share premium	(2,300)
5-years loan	(30,000)
Retained earnings @ 1 January 202X	(25,450)
Revenues from sales	(194,874)
Administrative expenses	32,900
Tax expense	1,240
Interest expense	1,375

The following information is relevant:

Notes:

1. The vehicles are to be depreciated using straight-line depreciation and the depreciation expense is part of the administrative expenses
2. The company consider that the allowance for trade receivable should be 5% of its balance, the variation on trade receivable's allowance is considered also an administrative expense
3. Included in administrative expenses is also the Rent expense
In this year the rent expense booked is for \$15,000 - for 15 months since the beginning of the leasing contract, on 1st March 202X
4. The interest expense booked is the interest expense paid. The loan was concluded at the beginning of the year with a 5% interest rate and the interest related to December is due by 5th January next year.
5. As at the year end, the value of closing inventory was assessed to be \$16,300.

Requirement:

Complete the year-end adjustments needed and write the Statement of Financial Position and the statement of profit or loss.

1.3.10 Example with SoCE

Consider again FIRST TRY Ltd with the following data:

Account	Balance as at 1 January 202X Db/(Cr) (\$)	Balance as at 31 December 202X Db/(Cr) (\$)
Share capital (2 mil shares @ \$0.01 each)	(20,000)	(20,000)
Share premium	(2,300)	(2,300)
Retained Earnings (See Note 1)	(30,850)	(36,200)

The following information is relevant:

1. During the year the company paid \$5,400 dividend
2. The profit of the year is \$10,750
3. As at the year end, the management appointed an expert to evaluate its vehicles and the value of vehicles was considered \$45,000.

Requirement:

Write the statement of Changes in Equity

 Now it is time for you to check your understanding. Note your answers to the quiz:

1.4 PRESENTATION OF DISCONTINUED OPERATIONS (IFRS 5)

1.4.1 IFRS 5 Requirements

According to IFRS 5 we call “discontinued operations” that component of an entity that _____

A component of a business is _____

The profit or loss from the discontinued operations includes:

1. _____
2. _____

The gain or loss on disposal is:

1. _____ OR
2. _____

IFRS 5 requires specific disclosure for the components meeting the definition of “discontinued operations” during the accounting period so as to allow readers of financial statements to distinguish between operations which will continue in the future and those which will not and to allow them to make better predictions for the future performance of the company.

This disclosure requirements are:

1. On the face of the Statement of Profit or Loss and Other Comprehensive Incomes:

1. _____ AND
2. _____

2. On the face of the Statement of Profit or Loss and Other Comprehensive Incomes OR in Notes:

1. _____

1.4.2 Example

Consider the company NEXT TRY Ltd which is a retail company with two shops, one in the capital city and another one into a small town.

The accountant of the company prepared the Statement of Profit or Loss and Other Comprehensive Incomes of NEXT TRY for the year ended 30 September 20X4:

	\$
Revenues	545,300
less cost of sales	(282,300)
Gross profit	263,000
Selling and distribution costs	(112,500)
Administrative expenses	(84,200)
Financial expenses	(21,900)
Profit before tax	44,400
Income tax expense	(11,500)
Profit for the year	32,900
Other comprehensive income for the year, net of tax	34,900
Total comprehensive income for the year	67,800

In August 20X4, the company decided to close the shop from the small town since it proved to not be a good business decision.

The performance of this shop is detailed below:

	\$
Revenues	137,200
less cost of sales	(78,900)
Gross profit	58,300
Selling and distribution costs	(81,000)
Administrative expenses	(25,800)
Profit before tax	(48,500)
Income tax expense	4,590
Profit for the year	(43,910)
Other comprehensive income for the year, net of tax	8,500
Total comprehensive income for the year	35,410

During the year, when the decision to sell the shop was taken, an evaluation was made, and the loss recognised by the accountant in the “administrative expenses” was \$40,000.

The shop was sold with a gain of \$53,000 which was recorded again in the “Administrative expenses” related to this shop.

The tax rate applicable is 20%.

Requirement:

Write the NEXT TRY Ltd.'s statement of Profit or Loss and Other Comprehensive Incomes in accordance with the IFRS 5 "Non-current assets held for sale and discounted operations"

 Now it is time for you to check your understanding. Note your answers to the quiz:

1.5 ACCOUNTING POLICIES, CHANGES IN ACCOUNTING ESTIMATES AND ERRORS (IAS 8)

1.5.1 IAS 8

The declared purpose of IAS 8 is to enhance _____ and _____ of Financial Statements as well as their _____.

IAS 8's first purpose is to set up criteria for _____

Then, it's purpose is to establish the _____ of

- a. Changes in accounting policies
- b. Changes in accounting estimates and
- c. Corrections of prior years' errors

The accounting policies are _____

The criteria established by IAS 8 to help management to select and apply the correct accounting policy is:

1. Apply _____
2. Then apply _____

Accounting policies must be _____ applied for similar transactions/events.

The changes in accounting policies are allowed only if:

- It _____

OR

- To provide more _____ and _____ information. In this case
 1. The new policy should be applied _____.
 2. If impracticable, then the conditions causing the impracticability should be _____

The disclosures required by IAS 8 to maintain the comparability of financial statements are:

1. _____
2. _____
3. _____
4. _____
5. _____

The Accounting estimates are _____

The Changes in accounting estimates

1. Must result _____
2. Must be _____
3. Must be recognised _____

The disclosures required when we have a change in an accounting estimate are:

1. _____
2. _____

Accounting errors may occur _____

The correction of errors should be made _____.

AND The entity must disclose:

1. _____
2. _____
3. _____
4. _____

1.5.2 Example 1: IAS 8 – Change in accounting policy

In 20X3 our company acquired an equipment with the following data:

- Acquisition cost: \$1,000,000
- Useful life: 10 years
- Depreciation method: straight line with a full year in the year of acquisition

In 20X5, the management realised that the most adequate depreciation method is the reducing balance method with a pace of 30% per year.

Requirements

Write the financial information to be presented in the financial statements for the year ended 31 December 20X5, related to this equipment:

1.5.3 Example 2: IAS 8 – Change in accounting estimate

In 20X3 our company acquired an equipment with the following data:

- Acquisition cost: \$1,000,000
- Useful life: 10 years
- Depreciation method: straight line with a full year in the year of acquisition

In 20X5, the management realised that the useful life of the equipment is with 5 years longer.

Requirements

Write the financial information to be presented in the financial statements for the year ended 31 December 20X5, related to this equipment:

1.5.4 Example 3: IAS 8 – Accounting errors

In 20X3 our company acquired an equipment with the following data:

- Acquisition cost: \$1,000,000
- Useful life: 10 years
- Depreciation method: straight line with a full year in the year of acquisition

In 20X5, the management realised that the depreciation charge recorded in the year 20X4 was \$10,000.

Requirements

Write the financial information to be presented in the financial statements for the year ended 31 December 20X5, related to this equipment: