

ACF2100 Notes - Financial Accounting

Topic 1: Regulation and Financing Company Operations

Why are companies important?

1. Companies dominate the capital and product markets
2. Companies operate within a complex web of government and professional regulation
3. Issuing financial statements / reports is part of the communication process

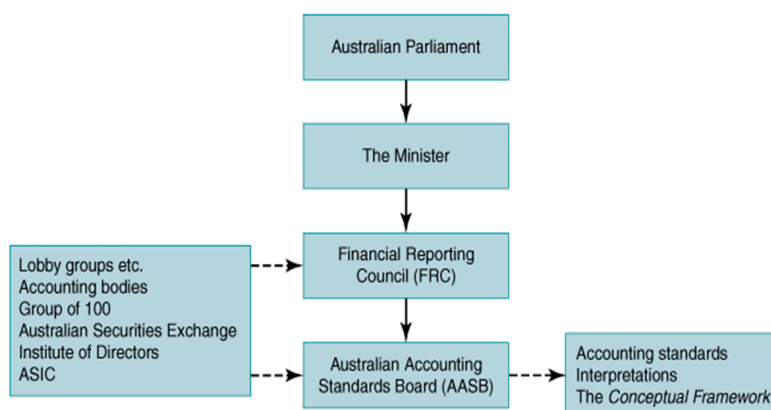
A company has its **own legal existence** (separate legal entity) therefore providing limited liability - shareholders of the company are liable only to the extent of any amounts unpaid on their shares in the event of liquidation / insolvency.

Accounting Regulation

The need for accounting regulation came about as the complexity of organisations grew resulting in disclosure requirements that developed into a more sophisticated form of financial reporting

What are the current arrangements for setting accounting standards in Australia?

- The AASB under the auspices of the Financial Reporting Council (FRC) is entrusted with the task of making accounting standards both for the purpose of the Corporations Act and for the public and not-for-profit sectors in Australia
- The AASB also developed a conceptual framework that sets down the basic objectives, principles and concepts to be used in GPFS (General Purpose Financial Statement)



SAC 1 Defines a reporting entity

SAC 2 Objective of General Purpose Financial Reporting

SAC 3 Qualitative Characteristics of Financial Information

SAC 4 Definition and Recognition of Elements of Financial Statements

Functions of the Australian Accounting Standards Board (AASB)

- Develop a conceptual framework for the purpose of the Corporations Act
- Formulate accounting standards for other purposes (NFP, Public and Non-Companies)
- Develop a conceptual framework for the purpose of evaluating proposed accounting and international standards

Which companies are required to prepare Financial Statements ?

As per **SAC 1** an entity where it is reasonable to expect the existence of users who rely on GPFS for useful information for decision making

Examples: public companies, large private companies and mid-sized smaller companies

SAC 2 Objective of General Purpose Financial Reporting : the objective of general purpose financial reporting is to provide information to users to enable them to make decisions about the allocation of resources

Financing Company Operations

Public companies are able to raise capital by issuing securities to the public via a disclosure document (often referred to as the *prospectus*)

1. Ordinary Shares (Equity)
2. Preference Shares (Equity or Liability) - often having a set rate of dividend (eg.5%)
3. Debentures (Liability)

* If preference shares are recognised as a liability, dividends are treated as interest expense (not a dividend)

The accounting treatment starts when money is received from potential investors:

- Securities can be **fully subscribed** - where it is fully allocated
- **Over subscribed** - excess monies can be refunded or held to offset future amounts payable (as per company constitution)
- **Under subscribed** - company may enter into an agreement with an underwriter to purchase excess shares avoiding the need to refund monies due to under-subscription

Eg. Underwriting companies - JPMorgan Chase, Goldman Sachs ...etc

Accounting Treatment in Equity Shares to Public

Application Account / Cash Trust

	DR	CR
Cash Trust	xx	
Application		xx
(Amount of money received on application)		

Share Capital Account

	DR	CR
Application	xx	
Share Capital		xx
(Application Fee per share * Number of Shares Issued)		

	DR	CR
Application	xx	
Cash Trust		xx
(Refunds to unsuccessful applicants)		

	DR	CR
Cash	xx	
Cash Trust		xx
(Successful applicants' money transferred into general funds - cash)		

Allotment Account - if money is due on allotment, the entry reflecting the amount owed to the company is made at the point the shares are allotted (similar to a receivable)

	DR	CR
Allotment	xx	
Share Capital		xx
(Cash receivable on allotment)		

.... when money is received from shareholders

	DR	CR
Cash	xx	
Allotment		xx
(Cash received on allotment)		