

Faculty of Economic, Commercial and Management Sciences
Department of Finance and Accounting
Academic level : Third Year (3rd Year)
Teacher's name : Boutabouna Ferial
Academic Year : 2024/2025



Lesson N° : 01 (1st Semester)

Liabilities

Understanding the various types of liabilities :

The Conceptual Framework defines liability as a present obligation which will be settled through an outflow of resources embodying economic benefits. **Liabilities** are classified into current (**short-term**) and non-current (**long-term**). Current liabilities are obligations due within one year or within a company's normal operating cycle, Obligations due beyond that period of time are classified as non-current or long-term liabilities.

1. **Accounts Payable.** Amounts owed for products or services purchased on account are called accounts payable or trade payables or trade creditors. They are typically short-term, as credit terms are usually between 30 and 90 days.
2. **Accrued Liabilities (Accrued Expenses).** An accrued liability usually results from an expense the business has incurred but not yet paid. Therefore, an accrued expense creates a liability, which explains why it is also called an accrued expense.
3. **Deposits.** There may be occasions when a business is required to pay a deposit for securing goods, property, or serviced such as power supplies and telephony services. The deposits are refundable once the service is no longer required or when the contract lapses.
4. **Unearned Revenues.** Unearned revenues are also called deferred revenues or revenues collected in advance. For all unearned revenue, the business has received cash from customers before earning the revenue.
5. **Payroll-related Liabilities.** Payroll, also called employee compensation, is a substantial expense for many companies. For service organizations—such as law firms, real estate companies, and airlines—employee compensation is the major expense, just as cost of goods sold is the largest expense for a merchandising company.

6. **Sales Tax Payable.** Most countries have some form of consumption tax. This tax is usually called Goods and Services Tax (GST), Value-Added Tax (VAT), or simply sales tax. Retailers collect the tax from customers and thus owe the tax authority for sales tax collected.
7. **Tax Payable.** Business entities are expected to pay tax on their income. Taxation rules vary
8. from one jurisdiction to another, and in most cases, taxable income may not equal net profit.
9. **Provisions.** A business may know that a liability exists but not know its exact amount. The business must still report the liability on the Balance Sheet based on the best estimates possible on the reporting date. Estimated liabilities vary among businesses.
10. **Notes Payable.** Notes are a common form of borrowing in some parts of the world. Depending on the maturity or term of the note, you may have short-term notes (due within one year) or occasionally medium-term notes, usually up to two or three years but they can be longer as well.
11. **Debt.** There are many forms of borrowing, from a simple term loan to a complex financing structure. Some long-term debt must be paid in installments. Some only require interest payments during the term of the loan, with payment of the loan amount at a specific time in the future.

Faculty of Economic, Commercial and Management Sciences

Department of Finance and Accounting

Academic level : Third Year (3rd Year)

Teacher's name : Boutabouna Ferial

Academic Year : 2024/2025

Lesson N° : 02 (1st Semester)



Accrual Accounting

Cash and profits are not the same thing. You may have used part of your profits to pay for new assets; you may have collected cash in advance from your customers; you may have expenses that you have not paid or prepaid some expenses ahead of utilizing them.

We use accrual accounting in financial reporting because it is a better measure of performance than cash payments and receipts. Let's find out more about accrual accounting!

Accrual accounting records the impact of business transactions and events on an entity's assets and liabilities over the period in which they occur, even if the resulting cash receipts or payments occur in a past or future period. For example, when a business performs a service, makes a sale, or incurs an expense, the accountant records the transaction even if it receives or pays no cash at the time of the transaction.

Accrual Accounting and Cash Flows

Accrual accounting is a more faithful representation of economic reality than cash-basis accounting. To be sure, accrual accounting records cash transactions, such as the following:

- Collecting cash from customers
- Receiving cash from interest earned
- Paying salaries, rent, and other expenses
- Borrowing money

- Paying off loans
- Issuing shares

But accrual accounting also records noncash transactions, such as the following:

- Sales on account
- Purchases of inventory on account
- Accrual of expenses incurred but not yet paid
- Depreciation expense
- Usage of prepaid rent, insurance, and supplies
- Earning of revenue when cash was collected in advance

Basic terms :

Accrual Accounting : المحاسبة على أساس الاستحقاق

Cash Flows : تدفقات نقدية

Faculty of Economic, Commercial and Management Sciences

Department of Finance and Accounting

Academic level : Third Year (3rd Year)

Teacher's name : Boutabouna Ferial

Academic Year : 2024/2025



Lesson N° : 03 (1st Semester)

Accounting concepts and principles

To use accrual accounting, we need to understand a few more concepts. We turn now to the time-period concept, the revenue recognition principle, and the expense recognition principle.

The Time-Period Concept :

The only way for a business to know for certain how well it has performed is to shut down, sell the assets, pay the liabilities, and return any leftover cash to the owners. This process, called liquidation, means going out of business. Ongoing companies cannot close down operations just to measure income! Instead, they need regular progress reports. Accountants, therefore, prepare financial statements for specific periods. The time-period concept ensures that accounting information is reported at regular intervals.

IAS 1 – Presentation of Financial Statements requires an entity to present a complete set of financial statements (including comparative information, as appropriate) at least annually. This is why you have been looking at extracts of annual reports of companies at the start of every chapter. Companies also prepare financial statements for interim periods of less than a year, such as a month, a quarter (three months), or a half-yearly period (six months). Usually, this is a requirement of the stock exchange where the company is listed. In general, as a company gets larger, it may be subjected to more frequent reporting requirements. Most of the discussions in this text are based on an annual accounting period.

The Matching Concept :

The matching concept is used to explain the relationship between expenses and revenues. The Conceptual Framework states that expenses are recognized in the Income Statement on the basis of a direct association between the costs incurred and the earning of specific items of income.

This process is commonly referred to as the “*matching of costs with revenues.*” Unlike assets, expenses offer no future benefits to the company. Matching includes two steps:

1. Identify decreases in assets or increases in liabilities that result in a reduction in equity (excluding transactions with owners) during the period. These are expenses.
2. Measure these expenses, and subtract expenses from revenues to compute profit or loss.

The Revenue Recognition Principle :

When should you recognize, i.e., record, revenue? In short, when you “earn” revenue. It sounds simple, but revenue recognition can be a very contentious topic. Think about the things you buy (music DVDs, electronic gadgets, and clothes), the services you consume (a magazine, a World of Warcraft or Netflix subscription, and your tuition fees), and ask yourself when do the companies that provide you with these goods and/or services actually earn your money?

The basic guidance for the revenue recognition principle comes from IAS 18 – Revenue. In general, for the sale of goods, revenue is recognized when:

- The entity has transferred to the buyer the significant risks and rewards of ownership of the goods;
- The entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the entity; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

When should you record revenue?

After it has been earned—and not before. Revenue is earned when there is an increase in asset or reduction in liability that results in an increase in equity (excluding transactions with owners). In most cases, revenue is earned when a business delivers goods or services to its customer.

The Expense Recognition Principle :

The expense recognition principle is the basis for recording expenses. Expenses are the costs of assets used up or liabilities incurred in earning income. Expenses have no future benefit to the business. Once you have identified and measured all the expenses, we match the expenses incurred to the associated revenue earned during the same period in order to obtain profit or loss.

Faculty of Economic, Commercial and Management Sciences
Department of Finance and Accounting
Academic level : Third Year (3rd Year)
Teacher's name : Boutabouna Ferial
Academic Year : 2024/2025



Lesson N° : 04 (1st Semester)

ANNUAL REPORTS

THE ROLE OF ANNUAL REPORTS AS A COMMUNICATION TOOL :

A search on Google for “annual report” yields over a billion entries. In the world of electronic information and communication, annual reports are the top source of information for shareholders, lenders, potential investors, and many other stakeholders. Annual reports are used to project and share a vision, and with the ease of distribution via the Internet, they serve as an important element of any entity’s communication with all its stakeholders. Annual reports provide readers with information on a company, ranging from company visions, goals, and strategies, to its financial statements and other required or compulsory disclosures (depending on jurisdictions).

Obtaining Annual Reports :

Traditionally, annual reports are hard copy reports that are only sent to shareholders (and those who request them directly from the company). With advances in information technology and connectivity of the Internet, virtually everyone now can obtain an electronic copy of annual reports of any public companies online. With search engines such as Google or Bing, it is usually easy to find the websites of the companies you are interested in. Many companies have now developed “web versions” of their annual report, which allows for better navigation, use of digital media, and interactivity.

Note that some businesses separate their “corporate website” from their “consumer website.” The corporate website is where you will find company and financial information pertinent to you, the investor or potential investor, whereas the consumer website is where the company showcases its product and services offerings to the consumer. With many websites now making use of location-based data, sometimes you may be redirected to your local, country, or region consumer website by default. You will have to specifically navigate to the company’s corporate website in order to obtain financial statements. For example, for Sony Corporation, if you go to www.sony.com, you will arrive at the consumer side (either a global or local site, depending on your physical location), whereas www.sony.net will direct you to Sony’s corporate website.

Typical Structure of an Annual Report :

For some companies, the primary purpose of an annual report is to meet legal requirements. Consequently, they only focus on compliance and do not invest much in corporate reporting. Small private companies’ annual reports, for example, primarily consist of financial statements and their accompanying notes. The larger the company and the more investors (or in some cases, creditors) it has, the more likely you will see more content in the annual report. Regardless of their creative themes, annual reports must meet requirements as dictated by the regulatory authority and, in the case of listed companies, the stock exchange’s listing requirements. You can visit your local stock exchange and check out its listing requirements or listing manual. It would most probably contain many disclosure items beyond the scope of this text, but it should give you an idea of the importance of communicating financial information and events to investors and potential investors.

Typically, an annual report has the following structure:

- corporate information
- analysis and commentaries
- other statements or disclosures
- financial statements

Faculty of Economic, Commercial and Management Sciences
Department of Finance and Accounting
Academic level : Third Year (3rd Year)
Teacher's name : Boutabouna Ferial
Academic Year : 2024/2025



Lesson N° : 05 (1st Semester)

ADJUST THE ACCOUNTS

At the end of the period, a reporting entity presents its financial statements to its users. This process begins with the trial balance introduced earlier (in Chapter 2). We refer to this trial balance as unadjusted because the accounts are not yet ready for the financial statements. We shall continue with our RedLotus Travel, Inc., example in the following discussions :

Which Accounts Need to Be Updated (Adjusted)?

The shareholders and management need to know how well RedLotus Travel, Inc., is performing. The financial statements report this information, and all accounts must be up-to-date. That means we need to make sure all necessary adjustments and updates are reflected in the accounts before the financial statements are prepared.

Exhibit 3-3 gives the unadjusted trial balance of RedLotus Travel, Inc., at June 30, 20X8. It reflects the same accounts as those in Chapter 2 (Exhibit 2-12), except for two additional months of transaction activities (i.e., May and June). However, the trial balance remains unadjusted. Let's see what we need to do to prepare the accounts before financial statements can be produced.

Exhibit 3-3 | Unadjusted Trial Balance

A1	A	B	C	D	E
	RedLotus Travel, Inc. Unadjusted Trial Balance June 30, 2018	Debit	Credit		
1					
2	Cash	\$ 34,800			
3	Accounts receivable	2,200			
4	Supplies	700			
5	Prepaid rent	3,000			
6	Land	20,000			
7	Equipment	24,000			
8	Accounts payable		\$ 13,100		
9	Unearned service revenue		400		
10	Share capital		50,000		
11	Retained earnings		18,800		
12	Dividends	3,200			
13	Service revenue		7,000		
14	Salary expense	900			
15	Utilities expense	500			
16	Total	\$ 89,300	\$ 89,300		
17					

Cash, Equipment, Accounts Payable, Share Capital, and Dividends are up-to-date and need no adjustment at the end of the period. Why? Because the day-to-day transactions provide all the data for these accounts.

Accounts Receivable, Supplies, Prepaid Rent, and the other accounts are a different story.

These accounts are not yet up-to-date on June 30. Why? Because certain transactions have not yet been recorded. Let's consider Supplies. During June, RedLotus used supplies in their operations. But RedLotus didn't make a journal entry for every supply item used each time it used them. That would be inefficient, wasting time and money. Instead, RedLotus waits until the end of the period and then records the supplies used up during the entire month.

The cost of supplies used up is an expense. An adjusting entry at the end of June updates both Supplies (an asset) and Supplies Expense. We must adjust all accounts whose balances are not yet up-to-date.

Categories of Adjusting Entries :

Accounting end-of-period adjustments fall into three basic categories: Deferrals, depreciation, and accruals. Deferral adjustments include deferred expenses (or prepaid expenses) and deferred income (or unearned revenue). Accrual adjustments include accrued expenses and accrual revenue. As you move forward with this textbook, you may see additional end-of-period adjustments for other items on the Balance Sheet.

Deferrals. A deferral is an adjustment for an item for which the business paid or received cash in advance. Richemont purchases supplies for use in its operations. During the period, some supplies (assets) are used up and become expenses. At the end of the period, an adjustment is needed to decrease the supplies account for the supplies used up and to record the supplies expense. Prepaid rent, prepaid insurance, and all other prepaid expenses require deferral adjustments.

Accruals. An accrual is the opposite of a deferral. For an accrued expense, Richemont records the expense before (eventually) paying for it. For an accrued revenue, Richemont records the revenue before (eventually) collecting cash. An accrued revenue is a revenue that the business has earned and will collect **next** year. At yearend, Richemont must accrue such revenue. The adjustment debits a receivable and credits a revenue. For example, accrual of interest revenue debits Interest Receivable and credits Interest Revenue.

Depreciation. Depreciation allocates the cost of an item of Property, Plant and Equipment (PPE) to expense over the asset's useful life. **Depreciation** is the most common longterm deferral. Richemont buys buildings, equipment, and other fixed assets to use in its operations.

Faculty of Economic, Commercial and Management Sciences
Department of Finance and Accounting
Academic level : Third Year (3rd Year)
Teacher's name : Boutabouna Ferial
Academic Year : 2024/2025



Lesson N° : 06 (1st Semester)

Investments

An Overview :

Businesses make investments in many forms, from buying equipment and inventory to investing in financial assets.—**Financial Instruments:** Presentation defines financial assets as any asset that is (a) **cash**, (b) **an equity instrument in another entity**, (c) **a contractual right to receive cash or financial assets of another entity**, or (d) **a contract that will or may be settled in the entity's own equity instruments**. In this chapter, we examine various investments that an entity makes, with emphasis on financial asset investments other entities.

Companies invest in debt or equity securities of other companies for a number of reasons, such as:

- They may have excess cash that they do not need immediately that can be put to better use by investing on a short-term basis with the hope to earn additional income (from interest, dividend, or capital appreciation) to benefit operations.
- They may have longer-term strategic objectives, such as obtaining the ability to influence or control another company. For example, a company may move up or down their value chain (a supplier or a distributor) in order to obtain a steady stream of raw materials and a secure distribution channel.

To consider investments, we need to define two key terms. The entity that owns the shares of a corporation is the investor. The corporation that issues the shares is the investee.

Reporting Investments on the Balance Sheet :

An investment is an asset to the investor. The investment may be short-term or long-term, as classified by IAS 1—Presentation of Financial Statements. **Short-term investments :** are investments in financial assets that are expected to be realized within 12 months. They can be classified as either trading, held-to-maturity, or available-for-sale, depending on management's intent and ability to hold them until they mature.

Investments that aren't short-term are listed as long-term investments, a category of non-current assets. **Long-term investments :** include shares and bonds that the investor expects to hold for longer than one year.