ACC2120 Notes
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Topics:

1- Financial Company Operations
2- Accounting for Income Tax Current Tax Issues
3- Accounting for Income Tax Deferred Tax Issues
4- Property, Plant and Equipment & Impairment of Assets
5- Business Combinations & Introduction to Consolidation
6- Consolidation: Wholly Owned Subsidiaries
7- Consolidation: Intragroup Transactions
8- Consolidation Non-Controlling Interest
9- Equity Accounting and Joint Arrangements
10- Liquidation of Companies

TOPIC 1: Financing Company Operations

Why are Companies so Important?

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

Nature of Companies:

- A company has its own **separate legal existence**
  - Incorporated via registration by Australian Securities and Investments Commission (ASIC)
  - Subject to requirements of Corporations Law
- Like a person, a company has rights, powers and responsibilities
- Unlike a person, a company need never die
- Main distinguishing feature is **limited liability** (only a shareholders shares are affected, not their personal assets)

Reporting Entities-

- Public companies, large proprietary companies, and some small proprietary companies are known as **reporting entities**
- A reporting entity is an entity where it is reasonable to expect the existence of users who rely on **General Purpose Financial Reports (GPFR)** for information useful for decision making (SAC 1)
- The objective of general purpose financial reporting is to **provide information to users** to enable them to make decisions about the allocation of resources (AASB Framework)

Financial Reports-

- Reporting entities are required to prepare GPFRs in accordance with **Australian Accounting Standards-**
- Statement of comprehensive income
  - company's total comprehensive income for the period
- Statement of changes in equity

  - how the company's capital, reserves and retained earnings have changed during the period
- Statement of financial position
  - assets, liabilities and equity
- Statement of cash flows
  - sources and uses of entity's cash resources

Financing Company Operations:

- Public companies can raise funds by issuing securities to the public
  - Ordinary shares (equity)
  - Preference shares (equity or liability) (see whether the definition of a L is satisfied, do we have a present obligation?)
  - Debentures (liability)
- Disclosure document (prospectus) is issued
- Accounting treatment begins when money is received from applicants
- Private placements (issuing shares too another institution, different way of accounting for this)

PRACTICAL WORK:

1. Issuing Shares-

- Which accounts do we use?
  - Cash (once shares are issued we use this account)
  - Cash trust (shares not yet issued, hence we use this account)
  - Application
  - Allotment (2 or more instalments)
  - Call (3 or more instalments)

1a) ***Share Issue Fully Payable on Application:***

Cash Trust xxx
Application xxx
(amount of money received on application)

- NOTE: Application account represents a L too the company, as if the shares are not issued, the money must be returned too the applicants.

Application xxx
Share Capital- Ordinary/Pref. xxx
(Number of Shares issued x application fee per share)

Application xxx
Cash Trust xxx
(Refunds to unsuccessful applicants)

Cash xxx
Cash Trust xxx
(Successful applicants money transferred into general funds)

- NOTE: WE ALWAYS NEED CASH TRUST AND APPLICATION TOO EQUAL 0!!!

1b) ***Share Issue Payable in Allotments-***

Allotment xxx
Share Capital- Ord./Pref. xxx
(Cash receivable on allotment)

- NOTE: Allotment account is very similar too a receivables account. However it is disclosed as reduction in share capital in the company's financial statements as it represents money receivable from shareholders for unpaid shares.
- Application and Allotment debit entries (too credit share capital) occurs on the same date!!!

Cash xxx
Allotment xxx
(Cash received on allotment)

****If we have a third installment…CALL:*

Call xxx
Share Capital- Ord./Pref. xxx
(Call of $x per share on shares issued)

- NOTE: Similarly too the allotment account, call account is similar to a receivables account, and any unpaid calls (calls in arrears) are shown as a reduction of share capital in the company's financial statements.

Cash xxx
Call xxx
(Receipt of Call)

******SEE EXAMPLE 2.2 (page 41, of text book)******

1c) ***Under and Oversubscription:***

Issues of securities can be…

- Fully subscribed (number of shares taken=number of shares offered)

- Undersubscribed
  - Receive less applications than the prospectus has called for.
  - The company may simply issue the number of shares that have been applied for.
  - OR Company may enter into an agreement with an underwriter to purchase excess shares
  - Avoids having to refund monies due to under-subscription
- Costs of underwriting and issuing shares are treated as a reduction in equity (share capital), SEE ACCOUNTING FOR SHARE ISSUE COSTS FURTHER BELOW…

***** IF UNDERSUBSCRIBED AND IT IS UNDER WRITTEN, LOOK AT EXAMPLE:**

e.g.- $30,000 underwritten, commission of $6,500…THEN, underwriter pays amount due less commission.

Cash 23,500
Share Capital (/Share Issue Costs) 6,500
Application 30,000

IF MULTIPLE PAYMENTS FOR SHARES:
Cash
SIC
Application
Allotment

- Oversubscribed
    - Receive more applications/application money than the prospectus has called for.
    - Excess money can be refunded or held to offset future amounts payable (as per constitution)
    - Soo, directors may either use the excess money to reduce the allotment money due, or, they may refund the excess money too the shareholder.

i) No authority too retain excess money exists (refund shareholders):
Application xxx
Cash Trust xxx
(Refund of excess application money)

ii) Authority too retain excess money exists (reduce future allotment money due):
Application xxx
Allotment xxx
Calls in Advance xxx
Cash Trust xxx
(Transfer of successful applicants' excess money in payment of allotment and future calls, and refund)

OR COULD BE:
Cash
Allotment
Calls in Advance
(Paid extra on allotment too go towards call)

*****If have 'Calls in Advance':**
Call xxx
Share Capital xxx
(Call of $x on x of shares)

Call In Advance xxx
Call xxx
(Calls in advance money transferred in reduction of first call)

Cash xxx
Call xxx
(**Cash received on Call)**

NOTE* *If interest paid on call money received in advance:*
Retained Earnings xxx
Cash xxx
(Interest paid on calls received in advance)

******SEE EXAMPLE 2.3 (page 45, of text book)******

2. Forfeiture Of Shares (not paying on call):

- Directors may be given the power under the company's constitution to forfeit (cancel) shares for which calls are not paid. This may be done if calls are not paid by the certain date. This means we have once amount which has been paid and one which has not (call)

AMOUNT ALREADY PAID (before forfeit)

- Balance of money retained by company
  - Forfeited shares reserve, OR…
- Amount paid refunded back to forfeiting shareholder
  - Forfeited shares liability
  - Shares could be reissued to new shareholders, with new shareholders paying less than the fully paid value of the share
- IT WILL DEPEND ON THE CONSTITUTION OF THE COMPANY WHAT HAPPENS WITH THE MONEY PAID BEFORE CANCELLATION OF THE SHARES!!!

NOTE: If the companies Constitution is *silent on the issue*, the shares *cannot be forfeited and must be re-issued!*

2a) *Shares Forfeited-*
Share Capital xxx (# shares x amount called up too)
Call xxx (# shares x unpaid call)
Forfeited Shares Reserve xxx (# shares x amount paid up)

- NOTE: FS RESERVE only if the company does not need to pay shareholders back as per the Constitution…if they do it is FS LIABILITY!!!
- The forfeited shares account is made up of the amount of money paid by shareholders who did not pay the final call amount.
- The final destination of this account depends on the requirements of the companies Constitution, as well as listing rules of the ASX (if the company is listed). ***Some possible options are:***
  a) The money in the forfeited shares account is kept by the company and hence regarded as equity.
  b) The forfeited shares may be re-issued either by private sale or public sale and the funds provided by the shareholders funds are returned to them (after taking out any costs of forfeiture and any interest payable. Hence this account would be seen as a liability.

2b) *Shares Reissued-*

Cash xxx (Cash received on sale)
Forfeited Shares Liability xxx (discount allowed on reissued shares)
Share Capital xxx (number of share by amount called up too)

- Any expenses on the reissue…OR if **balance refunded** too former shareholders…

Forfeited Shares Liability xxx
Cash xxx
(Expenses of reissue)

3. Share Issue Costs and Formation Costs:

3a) *Share Issue Costs (including underwriting fees):*

- Underwriting costs, transaction costs on share issues such as printing costs, stamp duties and taxes, professional advisers' fees and brokerage fees are all included under share issuing costs. These are treated very differently under accounting standard too formation costs and hence must be separated.
- ***All of these expenses are treated and recorded as a reduction in owners equity.***

e.g-
Share Capital xxx
Cash xxx
(Payment of other share issue costs)

3b) *Formation Costs-*

- Write these expenses immediately off as an expense!!!

4. Dividends:

- Dividends represent a **distribution of profits to the shareholders** of the company
- Dividends can only be paid from profits
- Power to declare dividends at any time rests with directors
- Dividends may be in the form of cash, bonus shares or assets
- Dividends come from Retained Earnings which is an account which holds the past profits/losses. Sometimes they may come from a reserve account.

4a) *Interim Dividends-*

- Declared and paid part way during the financial year
- Not a legal debt/liability
- Hence, Journal entry…

Where date= Date declared/paid:
Dr Retained earnings (Dividend paid) xxx
Cr Cash xxx

OR (if date declared and paid not the same):
Dr Interim Dividend xxx
Cr Interim Dividend Payable xxx

Dr Interim Div Payable xxx
Cr Cash xxx

Dr Retained earnings (Dividend paid) xxx
Cr Interim Dividends xxx

4b) *Final Dividends-*
- Liability recorded when declared **and** when not subject to further approval
- Journal entries…

→ *If Dividend Declared (legal debt once declared):*
Dr Retained earnings (Dividend declared) xxx
Cr Dividend payable (L) xxx
(Declaration of final dividend (create the L))

Dr Dividend payable (L) xxx
Cr Cash xxx
(Payment of final dividend (reduce the L))

→ *If Dividend Determined (only legal debt when paid):*
ON DATE PAID
Dr Retained Earnings xxx
Cr Cash xxx

If not all share money is paid for (still have some Call owing)
- e.g. 16 cent final dividend, however only 3/5 of the total value of shares has been called up.
- 0.16*3/5 total value= the dividend

4c) *Preference Dividends-*
- e.g. 6% redeemable preference shares
- = 6% dividend on the total value of those redeemable preference shares!!!

4d) *General Reserve-*
- Reserves are generally created too indicate too shareholders that such profits are not intended for distribution.

Retained Earnings xxx
General Reserve xxx
(Transfer of funds too General Reserve)

EXAMPLE 1-

On 1 March 2015, Amarok Ltd was incorporated and a prospectus was issued inviting applications for 200,000 ordinary shares at an issue price of $4. The shares were payable $2 on application, $1 on allotment (due 30 April), and $1 on a final call.

By 31 March, applications had been received for 210,000 ordinary shares (OVERSUBSCRIBED). On 4 April, the directors allotted 200,000 shares to applicants in proportion to the number of shares applied for. The surplus application was offset against allotment money payable.

All outstanding allotment money was received by the due date. The issue was underwritten at a commission of $2,500 which was paid on 1 May (part of share capital). Share issue costs of $3,000 were also paid on this date (part of share capital).

The final call was made on 2 May with money due by 31 May. All money was received on the due date, except for the holder of 10,000 shares who failed to meet the final call. On 15 June, as provided in the constitution, the directors decided to forfeit these shares (money held by the company). The constitution does not provide for any refund to former shareholders.

On 30 June, the directors declared a 20 cent per share final dividend. This dividend was subsequently paid on 22 July.

Required:

Prepare the journal entries to record the transactions of Amarok Ltd for the events outlined above.

2015				
March 31	Cash Trust	Dr	420,000	
	Application	Cr		420,000
	(Cash received on application: 210 000 sh x $2)			
April 4	Application (200 000 sh x $2)	Dr	400,000	
	Allotment (200 000 sh x $1)	Dr	200,000	
	Share Capital - Ordinary	Cr		600,000
	(Allotment of 200 000 shares)			
	Application	Dr	20,000	
	Allotment	Cr		20,000

	(Offset surplus application money (***if refund, credit too cash trust!!!))			
	Cash	Dr	420,000	
	Cash Trust	Cr		420,000
	(Transfer of trust funds)			
April 30	Cash	Dr	180,000	
	Allotment	Cr		180,000
	(Receipt of allotment money)			
May 1	Share Capital	Dr	2,500	
	Cash	Cr		2,500
	(Payment of underwriter's commission)			
	Share Capital	Dr	3,000	
	Cash	Cr		3,000
	(Payment of share issue costs)			
May 2	Call (sort of like a receivables acc., but is OE)	Dr	200,000	
	Share Capital – Ordinary	Cr		200,000
	(Call of $1 per share on 200 000 shares)			
May 31	Cash	Dr	190,000	
	Call	Cr		190,000
	(Cash received on 190 000 shares @ $1)			
June 15	Share Capital – Ordinary (10 000 x $4)	Dr	40,000	
	Call	Cr		10,000
	Forfeited Shares Reserve	Cr		30,0000
	(Forfeiture of 10 000 shares)			

June 30	Dividend Declared (Retained Earnings)	Dr	38,000	
	Dividend Payable	Cr		38,000
	(Declaration of final dividend: 20c x 190000 sh)			
July 22	Dividend Payable	Dr	38,000	
	Cash	Cr		38,000
	(Payment of final dividend)			

5. Subsequent Issues of Shares

5a) ***Rights Issue-***

- Existing shareholders have the right to buy additional shares in proportion to their current shareholding… eg 1 for 5
- If all existing shareholders take up the new shares, there is no change in the shareholders percentage ownership interest of the company.
- Can be renounceable (where shareholders decline their rights too buy additional shares, or, also sell their rights too acquire the additional shares) OR non-renounceable (where shareholders are not allowed too sell their rights and must either accept or reject the offer).
- This is very different too a public offering as it is the company who sends the letter of offer too its shareholders and the shareholders are the ones who accept or reject the application offer. The point of acceptance is the point of allotment of the shares.
- ***As no money is received by the company before the allotment, there is no need for the company too raise a Cash Trust fund.***

Cash xxx
Share Capital-Ordinary xxx
(1 in 6 rights issue… # shares/6= number of new shares x price)

******NOTE:*** Underwriters will buy any share offers that are not fully taken up, if non-renounceable the underwriter will not be able to take up the 'non-taken' shares.

5b) ***Private Placement-***

- This is a private issue of shares too institutional investors such as life insurance companies and superannuation funds.

Cash xxx
Share Capital xxx
(Private placement of # shares @ $x)

5c) ***Bonus Issue***-

- Issue of shares to existing shareholders in proportion to current shareholding at no cost to shareholders

Revaluation Surplus xxx
Share Capital xxx
(Issue of Shares under Bonus issue out of revaluation surplus)

6. Share Options-

- Gives the holder the right to buy or sell a certain number of shares by a specified date at a stipulated price
- We are concerned with **company-issued share options**
- Issued at no cost to the recipient, or at a specified price
- **'Share Options'** account is used when issued at a price

6a) ***Share Options for NO COST too recipient (e.g. under an employee scheme)***

Cash xxx
Share Capital xxx
(Allotment of x shares at $x per share)

6b) ***Share Options for A COST too recipient***

- Here we credit the Share Options account. This is treated as part of the company's equity.

e.g. 36,000 options for 36,000. Option costs 50 cents and entitles you too one share at $1.50. Option is for between 23 Nov and 20 Dec.
Cash xxx
Share Options xxx
(Issue of 36,000 options at 50c each)

Then, by 20 Dec 30,000 Options were exercised, the remaining 6,000 Options lapsed.
Cash xxx
Share Capital xxx
(Issue of 30,000 shares on payment of $1.50 per share)

Share Options xxx (36,000 x 50c)
Share Capital xxx (30,000 x 50c)
Lapsed Share Options xxx (6,000 x 50c)
(Write-off of share options, reflecting 30,000 options exercised and 6,000 lapsed)

7. Redeemable Preference Shares:

- These are shares issued on the terms that they may be redeemed by the company at a later date, either by payment out of profits which would otherwise be available for dividends or out of proceeds of a fresh issue of shares.

- Preference shares can be classified as equity, liability, or both
  - Depends on whether liability definition is satisfied
  - Consider whether redeemable, cumulative, participating
- Redeemable preference shares can be redeemed out of profits, or from proceeds of a new issue of shares
  - Can be redeemed at a premium
  - 'Shareholders' redemption' account is used

7a) *Classified as Equity:*

Three ways of redeeming the shares:

i) Redemption from a Fresh issue of Shares:

e.g- Previous issue of 20,000 preference shares at $1. Company redeems the shares out of a fresh issue of 10,000 ordinary shares at $2 per share under a private placement.

Share Capital- Preference 20,000
Shareholders' Redemption 20,000
(Transfer of Preference capital too redemption account)

Cash 20,000
Share Capital- Ordinary 20,000
(Receipt of cash on issue of 10,000 ordinary shares issued at $2 per share)

*****ON DATE PAYMENT MADE TOO SHAREHOLDER**
Shareholders' Redemption 20,000
Cash 20,000
(Redemption of Preference Shares)

ii) Redemption Out of Profits:

Share Capital- Preference 20,000
Shareholders' Redemption 20,000
(Transfer of Preference capital too redemption account)

Retained Earnings 20,000
Share Capital- Ordinary 20,000
(Transfer of R/E too capital too preserve the total capital of the company)

*****ON DATE PAYMENT MADE TOO SHAREHOLDER**
Shareholders' Redemption 20,000
Cash 20,000
(Redemption of Preference Shares)

iii) Redemption out of Profits at a Premium:
e.g. Premium was $,5000

Share Capital- Preference 20,000
Shareholders' Redemption 20,000
(Transfer of Preference capital too redemption account)

Retained Earnings 5,000
Shareholders Redemption 5,000
(Premium on Redemption)

Retained Earnings 20,000
Share Capital- Ordinary 20,000
(Transfer of R/E too capital too preserve the total capital of the company)

*****ON DATE PAYMENT MADE TOO SHAREHOLDER**
Shareholders' Redemption 25,000
Cash 25,000
(Redemption of Preference Shares)

NOTE: If question says that 'the main purpose of the share issue was too fund the redemption of pref. shares, AND it was made at a premium, do the premium entry as shown above but you do not need too maintain capital, as capital was already increased when the new shares were issued.

7b) *Classified as Liability:*
If the preference share has the following characteristics it should be recorded as a liability:

- redeemable in cash on a certain specified date or on the option of the holder.
- Cumulative as to the payment of dividends
- Non-participating in further dividend distributions

i) Redemption from a Fresh issue of Shares:
e.g- Had issued 30,000 preference shares at $1 each. The shares are too be redeemed in cash out of a fresh issue of 15,000 redeemable preference shares issued at $2 each.

Preference Shares Liability 30,000
Shareholders Redemption 30,000
(Transfer of Preference Shares too redemption account)

Cash 30,000
Preference Shares Liability 30,000
(Issue of 15,000 preference shares at $2 each)

*****ON DATE PAYMENT MADE TOO SHAREHOLDER**
Shareholders Redemption 30,000
Cash 30,000

(Redemption of Preference Shares)

ii) Redemption out of Profits at a Premium:
Preference Shares Liability 30,000
Shareholders Redemption 30,000
(Transfer of Preference Shares too redemption account)

Redemption Premium Expense 3,000
Shareholders Redemption 3,000
(Premium on Redemption)

Retained Earnings 30,000
Share Capital 30,000
(Transfer of R/E too capital too preserve the capital of the company under the law)

*****ON DATE PAYMENT MADE TOO SHAREHOLDER**
Shareholders Redemption 33,000
Cash 33,000
(Redemption of Preference Shares at a premium)

8. Share Buy-backs-
EXAMPLE:
Equity:

Share capital (2.3 million shares)	$2.3 mil (hence $1 per share)
General Reserve	$ 35,000
R/E	$ 375,000

- The company acquired 10% of its shares currently on offer for $2.20 per share. Costs of the buy-back scheme were $3,000. The original amount of the shares is first taken from Share Capital, then adjustments made from the General Reserve and then and remaining amount taken from R/E.

General Reserve	35,000	
Share Capital	230,000	
R/E	244,000	
Cash		509,000

(230,000 shares x $2.20 per share + $3,000)

Debentures:
- **Debentures** are type of debt security (liability)