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FREE CERTIFICATION PREP

FORMULA SHEET

CPA FAR

Financial Accounting & Reporting · Core section

110 formulas **3** subject areas

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HOW TO USE THIS SHEET

FAR is the broadest of the CPA sections and, for most candidates, the hardest. It is not conceptually difficult — it is simply enormous, and it rewards recall of mechanics under time pressure.

This sheet is organised the way the AICPA blueprint groups the content: financial reporting, then balance sheet accounts, then transactions. Use it to compress a topic AFTER you have studied it.

Journal entries are the currency of FAR. If you can write the entry, you can answer the question — including the multiple-choice questions that never mention an entry. When a topic here shows an entry, learn the entry, not the prose.

The ► notes flag what the examiners actually test: a direction, a threshold, a GAAP-versus-IFRS split, or the one condition everyone forgets.

FINANCIAL REPORTING · 39 formulas

EPS, cash flows, ratios, the reporting entity, and the governmental and not-for-profit frameworks.

Basic EPS

$$\text{Basic EPS} = (\text{Net income} - \text{Preferred dividends}) / \text{Weighted average common shares outstanding}$$

Where: Preferred dividends subtracted whether declared (cumulative) or not.

► *Stock dividends and splits are applied RETROACTIVELY to all periods presented — they do not change the entity, only the slicing. New shares issued for cash are weighted from the issue date.*

Diluted EPS — treasury stock method (options/warrants)

$$\Delta \text{Shares} = N - (N \times K / P)$$

Apply only if $K < P$ (in the money)

Where: N = options outstanding, K = strike, P = average market price.

► *Assume the proceeds buy back shares at the AVERAGE price. Out-of-the-money options are anti-dilutive and simply ignored — no calculation needed.*

Diluted EPS — if-converted (convertible bonds)

$$\text{Diluted EPS} = [\text{NI} - \text{Preferred} + \text{Interest}(1 - t)] / (\text{WACSO} + \text{Converted shares})$$

Where: Add back after-tax interest, because conversion would have eliminated it.

► *After-tax interest, not gross. Test each issue separately and include only the dilutive ones.*

Diluted EPS — if-converted (convertible preferred)

$$\text{Diluted EPS} = (\text{NI} - \text{Preferred} + \text{Convertible preferred dividends}) / (\text{WACSO} + \text{Converted shares})$$

Where: Add back the preferred dividends the conversion would have removed.

► *Note there is no tax adjustment here — preferred dividends were never deductible.*

Anti-dilution rule

Include a potential share in diluted EPS ONLY if it DECREASES EPS.

Where: Test each security separately, most dilutive first.

► *In a NET LOSS year, every potential share is anti-dilutive, so diluted EPS = basic EPS. That single sentence answers a whole family of questions instantly.*

Cumulative preferred dividends in arrears

$$\text{Arrears} = \text{Shares} \times \text{Par} \times \text{Rate} \times \text{Years unpaid}$$

$$\text{EPS} = (\text{NI} - \text{Preferred current} + \text{arrears}) / \text{WACSO}$$

Where: Disclosed in the notes, NOT recorded as a liability until declared.

► *Not a liability — no obligation exists until the board declares. But it still reduces income available to common in the EPS numerator.*

Indirect method — cash from operations

Start: Net income
 + Depreciation and amortisation
 + Loss / (– Gain) on asset disposal
 – Increase / (+ Decrease) in current assets
 + Increase / (– Decrease) in current liabilities
 = Cash from operations

Where: Reconciles accrual income to operating cash.

► Gains are SUBTRACTED because the whole proceeds appear in investing — leaving the gain in operations would double-count it. This sign is the single most-tested item in the cash flow statement.

Comprehensive income (PUFE)

Comprehensive income = Net income + OCI

Where: OCI items: Pension adjustments, Unrealised G/L on AFS debt, FX translation, Effective portion of cash flow hedges.

► PUFE. All reported net of tax. Note that unrealised gains on EQUITY securities go to net income, not OCI — that changed under ASU 2016-01 and it is a live trap.

Cash to accrual conversion

Accrual revenue = Cash received + Δ AR – Δ Unearned revenue
 Accrual expense = Cash paid + Δ AP – Δ Prepaid

Where: Add increases in liabilities; subtract increases in assets.

► Work the direction from first principles: if receivables grew, you earned more than you collected — so add the increase.

Book value per common share

BVPS = (Common equity – Preferred equity – Dividends in arrears) / Common shares outstanding

Where: Shares outstanding = issued – treasury.

► Preferred claims come out first. Treasury shares are issued but NOT outstanding — using issued shares is the standard error.

Debt-to-equity and times interest earned

D/E = Total liabilities / Total stockholders' equity
 TIE = EBIT / Interest expense

Where: Leverage and coverage.

► Leverage says how much debt there is; coverage says whether it can be serviced. Rating decisions need both.

DuPont decomposition (3-step)

ROE = (NI/Sales) × (Sales/Avg assets) × (Avg assets/Avg equity)

Where: Profit margin × asset turnover × equity multiplier.

► An ROE rising purely because of the leverage term is a warning, not an achievement. That interpretation is the exam point, not the arithmetic.

Profitability ratios

GM = (Sales – COGS) / Sales
 PM = NI / Sales
 ROA = NI / Avg assets
 ROE = NI / Avg equity

Where: Use AVERAGES for balance-sheet denominators.

► Income statement item (a flow) over balance sheet item (a stock) ⇒ average the stock. This rule governs every ratio in FAR.

Liquidity ratios

Current = Current assets / Current liabilities
 Quick = (Cash + ST marketable securities + Net AR) / Current liabilities

Where: Quick excludes inventory and prepaids.

- ▶ Quick strips out what cannot be converted quickly. A high current ratio driven by bloated inventory is a liquidity problem disguised as a liquidity strength.

AR turnover and days sales in AR

$$\text{AR turnover} = \text{Net credit sales} / \text{Avg net AR}$$

$$\text{DSO} = 365 / \text{AR turnover}$$

Where: Credit sales, not total sales.

- ▶ Rising DSO with flat sales means the company bought growth by loosening credit terms.

Inventory turnover and days in inventory

$$\text{Inventory turnover} = \text{COGS} / \text{Avg inventory}$$

$$\text{Days in inventory} = 365 / \text{Inventory turnover}$$

Where: COGS, because inventory is carried at cost.

- ▶ Revenue in the numerator is the classic distractor. Falling turnover means goods are piling up — obsolescence risk.

AP turnover and days payable outstanding

$$\text{AP turnover} = \text{COGS} / \text{Avg AP}$$

$$\text{DPO} = 365 / \text{AP turnover}$$

Where: How slowly the company pays suppliers.

- ▶ A higher DPO preserves cash but strains supplier relationships. It is a lever, not a virtue.

Cash conversion cycle

$$\text{CCC} = \text{DSO} + \text{DIO} - \text{DPO}$$

Where: Days cash is tied up in operations.

- ▶ Note the MINUS on DPO — paying suppliers slowly shortens the cycle. A negative CCC (Amazon, Dell) means suppliers finance the operation.

Operating cash flow ratio

$$\text{OCF ratio} = \text{CFO} / \text{Current liabilities}$$

Where: Liquidity measured in actual cash, not accruals.

- ▶ Harder to manipulate than the current ratio, because you cannot accrue your way to cash.

Multi-step income statement

$$\begin{aligned} \text{Net sales} - \text{COGS} &= \text{Gross profit} \\ - \text{Operating expenses} &= \text{Operating income} \\ \pm \text{Non-operating items} &= \text{Pre-tax income} \\ - \text{Tax} &= \text{Net income} \end{aligned}$$

Where: Discontinued operations sit BELOW net income, net of tax.

- ▶ Learn the order. Half the FAR presentation questions are simply asking where a line item goes.

Discontinued operations criteria

Held for sale — ALL required: (1) management commits to a plan (2) available for immediate sale as-is (3) active buyer search (4) sale probable within 1 year (5) marketed at a reasonable price (6) plan unlikely to change.

Where: Reported net of tax, below income from continuing operations.

- ▶ It must also be a STRATEGIC SHIFT with a major effect. Selling one store from a chain of 500 is not a discontinued operation.

Subsequent events — Type 1 vs Type 2

Type 1 (recognised): condition EXISTED at the B/S date → ADJUST the financial statements
Type 2 (nonrecognised): condition AROSE after the B/S date → DISCLOSE only

Where: Evaluation period: public = through issuance; private = through available-to-be-issued.

- ▶ Ask one question: did the condition exist on the balance sheet date? A customer who was already insolvent ⇒ adjust. A customer whose factory burned down in January ⇒ disclose.

Segment reporting — 10% tests

Reportable if ANY: revenue $\geq 10\%$ of combined revenue, OR $|\text{profit or loss}| \geq 10\%$ of the greater of total profits or total losses, OR assets $\geq 10\%$ of combined assets.

Where: 75% rule: reportable segments must cover at least 75% of consolidated external revenue.

► The tests are ALTERNATIVE (any one triggers), but the 75% rule is CUMULATIVE — if you fall short, add more segments until you clear it.

SEC Form 10-K deadlines

Large accelerated filer (float $\geq \$700\text{M}$): 60 days

Accelerated filer ($\$75\text{M}$ – $\$700\text{M}$ float, $\geq \$100\text{M}$ revenue): 75 days

Non-accelerated ($< \$75\text{M}$ float): 90 days

Where: Days after fiscal year-end.

► The pattern is 60/75/90 as the filer gets smaller. Memorise the three numbers and the float thresholds that define them.

SEC Form 10-Q deadlines

Large accelerated and accelerated filers: 40 days

Non-accelerated filers: 45 days

Where: After quarter-end; filed for Q1–Q3 only.

► There is no Q4 10-Q — those results arrive inside the annual 10-K.

Foreign currency — direct vs indirect quotation

Direct = 1 / Indirect

Where: Direct = domestic price per one foreign unit ($\$1.10/\text{€}1$). Indirect = foreign units per one domestic unit ($\text{€}0.91/\$1$).

► They are reciprocals. Write the units beside the number before you compute anything — an inverted quote is the most common FX error in FAR.

Foreign currency transaction gain/loss

$G/L = (\text{Spot at settlement} - \text{Spot at transaction}) \times \text{Foreign currency amount}$

Where: Recognised at each balance sheet date AND at settlement; hits net income (ASC 830).

► The matrix: if the foreign currency STRENGTHENS, an asset produces a gain and a liability produces a loss. Weakens $\Rightarrow$ the reverse. Reason it from whether you are owed or you owe.

Translation vs remeasurement

Translation (functional = local currency): assets/liabs at CURRENT rate, equity at HISTORICAL, income at AVERAGE; G/L $\rightarrow$ OCI

Remeasurement (functional = parent's currency): monetary at CURRENT, non-monetary at HISTORICAL, COGS/depreciation at HISTORICAL, sales at AVERAGE; G/L $\rightarrow$ NET INCOME

Where: The functional currency determines which method applies.

► The destination of the gain is the whole test: translation goes to OCI (it is a paper effect), remeasurement goes to net income (it is real economic exposure).

Stock dividend — small ($< 20\text{--}25\%$)

DR Retained earnings FMV $\times$ shares

CR Common stock Par $\times$ shares

CR APIC (FMV – Par) $\times$ shares

Where: $\Delta RE = \text{FMV} \times \text{shares}$.

► A SMALL stock dividend is capitalised at FAIR VALUE. The theory: it is small enough not to move the market price, so shareholders receive something of value.

Stock dividend — large ($\geq 20\text{--}25\%$)

DR Retained earnings Par $\times$ shares

CR Common stock Par $\times$ shares

Where: $\Delta RE = \text{Par} \times \text{shares}$; FMV ignored.

- ▶ A LARGE stock dividend behaves like a split, so it is recorded at PAR. Small = FMV, large = par. That is the entire distinction, and it is worth memorising as a pair.

Governmental fund types (GRaSPP)

General, Special Revenue, Debt Service, Capital Projects, Permanent

Where: All five use MODIFIED accrual and the current financial resources focus.

- ▶ GRaSPP. These funds hold no capital assets and no long-term debt — those appear only in the government-wide statements.

Proprietary fund types

Internal Service (internal customers, cost reimbursement) and Enterprise (external customers)

Where: Full accrual, economic resources focus.

- ▶ An Enterprise fund is REQUIRED if any of: debt is secured by fee revenue, law requires fees to cover costs, or pricing policy targets cost recovery.

Fiduciary fund types

Custodial, Investment Trust, Private-Purpose Trust, Pension/OPEB Trust

Where: Full accrual, economic resources focus.

- ▶ These assets are not the government's — they are held for others. That is why fiduciary funds are EXCLUDED from the government-wide statements entirely.

Modified accrual revenue recognition

Recognise revenue when MEASURABLE and AVAILABLE.

Where: Available = collectible within the current period or within 60 days after year-end.

- ▶ The 60-day rule is the number they test. Expenditures are recorded when the LIABILITY is incurred — not when paid.

Government-wide vs fund-level statements

Government-wide: full accrual, economic resources; ALL assets and liabilities including capital assets and long-term debt

Governmental funds: modified accrual, current financial resources; NO capital assets, NO long-term debt

Where: MD&A is required supplementary information, presented BEFORE the statements.

- ▶ This split is the whole of governmental accounting. Every reconciliation question is just converting one basis to the other.

NFP — three required financial statements

Statement of Financial Position, Statement of Activities, Statement of Cash Flows

Where: Net asset classes: With Donor Restrictions and Without Donor Restrictions.

- ▶ Only TWO net asset classes since ASU 2016-14 — the old three-class model (unrestricted / temporarily / permanently) is gone. Health and welfare NFPs add a Statement of Functional Expenses.

NFP — conditional vs unconditional contributions

Conditional = a BARRIER + a right of return → DEFER; cash received is a Refundable Advance (liability)

Unconditional = no barrier → recognise revenue immediately

Where: Recognise when all barriers are overcome.

- ▶ A barrier is a specified outcome, service level, matching requirement, or outside event. A mere donor RESTRICTION on use is not a condition — restricted revenue is still recognised now.

NFP — cash and unconditional pledge recognition

Pledge receivable = $\sum CF_t / (1 + r)^t$

Where: Multi-year pledges are discounted; the accretion is contribution revenue.

- ▶ Recognise the pledge at present value when the promise is MADE, not when cash arrives. The unwinding of the discount is revenue, not interest income.

NFP donated services (SOME)

Recognise donated services ONLY if ALL of: Specialised skills required, Otherwise needed (would have been purchased), Measurable, Easily valued at fair value

Where: DR Expense / CR Contribution revenue at fair value.

► *SOME. A lawyer donating legal work qualifies; a lawyer stuffing envelopes does not. If the test fails, footnote disclosure only — no entry.*

EXAM TIPS — FINANCIAL REPORTING

- For any cash flow question, ask where the item BELONGS first (operating, investing, financing) and only then worry about the sign. Misclassification costs more than a sign error.
- Governmental accounting is a basis-of-accounting question in disguise. Identify the fund type, and the measurement focus tells you the answer.
- EPS: preferred dividends always come out of the numerator; anti-dilutive securities never go into the denominator. Those two rules resolve most EPS questions.

SELECT BALANCE SHEET ACCOUNTS · 40 formulas

Inventory, receivables, PP&E, leases, pensions, bonds and equity. The journal-entry heartland of FAR.

FIFO vs weighted average

FIFO COGS = oldest costs used first

WA cost/unit = Total cost of goods available / Total units available

WA COGS = WA cost per unit × Units sold

Where: Cost flow assumptions, not physical flow.

► *In rising prices, FIFO leaves the NEWEST (highest) costs in ending inventory, so income is higher. Reason from which costs are left behind, not which are expensed.*

LIFO reserve and LIFO effect

LIFO reserve = FIFO inventory – LIFO inventory

LIFO effect = Change in the LIFO reserve during the period

Where: The extra COGS recognised under LIFO versus FIFO.

► *To convert LIFO to FIFO: ADD the reserve to inventory, and REDUCE COGS by the LIFO effect. This is how you compare a LIFO company to a FIFO peer.*

Lower of cost or NRV (FIFO / weighted average)

NRV = Selling price – Cost to complete and sell

Inventory = min(Cost, NRV)

Where: Applies to FIFO and weighted average.

► *One ceiling, no floor. Simple — which is exactly why the LIFO rule below feels so strange by comparison.*

Lower of cost or market (LIFO / retail)

Market = MIDDLE of (Ceiling, Replacement cost, Floor)

Ceiling = NRV = SP – cost to sell; Floor = NRV – normal profit

Inventory = min(Cost, Market)

Where: Applies ONLY to LIFO and the retail method.

► *Take the MIDDLE value of three, then compare that to cost and take the lower. Two steps, and candidates routinely collapse them into one.*

Dollar-value LIFO

1. Ending inventory at base = EI at current ÷ current index
2. Layer added at base = EI at base – prior EI at base
3. New layer at current = layer × current index
4. DVL inventory = base layer + prior layers at their own indexes + new layer

Where: Each layer keeps the index of the year it was added.

► Convert to base-year dollars to find whether a real layer was added, then re-price only the NEW layer at the current index. Prior layers never get re-priced.

Periodic vs perpetual inventory

- Periodic: $\text{COGS} = \text{Beginning inventory} + \text{Purchases} - \text{Ending inventory}$
 Perpetual: COGS recorded at each sale (DR COGS / CR Inventory)

Where: Periodic requires a physical count to derive COGS.

► Under periodic, COGS is a plug — so shrinkage hides inside it. Under perpetual, shrinkage is visible as a difference from the count. That is the control argument.

Bad debt expense (allowance method)

- Aging / % of AR (balance-sheet): $\text{BDE} = \text{Estimated uncollectible} - \text{Existing allowance credit balance}$
 % of sales (income-statement): $\text{BDE} = \% \times \text{Credit sales}$ (ignores the existing balance)

Where: Two methods, two very different mechanics.

► The aging method SETS the ending allowance to a target, so you must back out what is already there. The % of sales method just adds — no adjustment. Mixing them up is the classic error.

Factoring AR — with vs without recourse

- Without recourse = a true sale → derecognise the AR
 With recourse = a sale ONLY if: (1) control surrendered (2) repurchase obligation reasonably estimable (3) no required repurchase

Where: Otherwise it is a secured borrowing.

► If it fails the test, the receivable STAYS on the books and you record a liability. The economics did not change — the accounting did.

Discounting notes receivable

1. $\text{MV} = \text{Face} + \text{Interest}$
2. $\text{Bank discount} = \text{Discount rate} \times \text{MV} \times \text{time}$
3. $\text{Cash proceeds} = \text{MV} - \text{Bank discount}$
4. $\text{Interest income/expense} = \text{Cash} - \text{Carrying value}$

Where: The bank discount is computed on MATURITY value, not face.

► Step 2 is the trap: the bank charges its rate on what the note will be WORTH, not what it was issued for.

Sales discount — gross vs net method

- Gross: record AR/Sales at full; if the discount is taken, DR Sales Discount (contra-revenue)
 Net: record AR/Sales net of discount; if NOT taken, CR Sales Discount Forfeited (other revenue)

Where: Same cash, different presentation.

► Net is theoretically purer — it records revenue at the amount the company actually expects. Gross is what most companies do anyway.

Straight-line depreciation

- $\text{SL} = (\text{Cost} - \text{Salvage}) / \text{Useful life}$

Where: Constant expense per period.

► The baseline. Note that salvage IS subtracted here — which is exactly what makes double-declining balance so counterintuitive.

Double-declining balance

$$\text{Depreciation}_t = (\text{Cost} - \text{Accumulated depreciation to date}) \times (2 / \text{Useful life})$$

Where: Applied to the declining BOOK value.

► *Salvage is IGNORED in the formula — but you stop depreciating once book value reaches salvage. Ignoring salvage entirely, all the way to zero, is the standard mistake.*

Sum-of-years'-digits

$$\text{SYD denominator} = n(n + 1) / 2$$

$$\text{Expense}_t = [(n - t + 1) / \text{SYD}] \times (\text{Cost} - \text{Salvage})$$

Where: n = useful life, t = the year number.

► *Accelerated, and salvage IS subtracted (unlike DDB). Year 1 gets the largest fraction.*

Units-of-production depreciation

$$\text{Depreciation per unit} = (\text{Cost} - \text{Salvage}) / \text{Total estimated units}$$

$$\text{Annual} = \text{Per-unit rate} \times \text{Units produced}$$

Where: Usage-based; ignores the passage of time.

► *Correct when wear tracks output rather than age — machines, vehicles by mileage. An idle asset takes no depreciation, which is the whole idea.*

Composite (group) depreciation

$$\text{Annual depreciation} = \Sigma (\text{Depreciable base of each asset} / \text{its useful life})$$

$$\text{Composite life} = \Sigma \text{Depreciable base} / \text{Annual depreciation}$$

Where: A pool of dissimilar assets depreciated as one.

► *On retirement, NO gain or loss is recognised: DR Cash and Accumulated depreciation, CR Asset. Any difference is buried in accumulated depreciation. That no-gain rule is what makes composite examinable.*

Cost depletion

$$1. \text{Depletion base} = (\text{Land} + \text{Development} + \text{Restoration}) - \text{Residual value}$$

$$2. \text{Rate} = \text{Base} / \text{Estimated recoverable units}$$

$$3. \text{Depletion} = \text{Rate} \times \text{Units EXTRACTED}$$

$$4. \text{COGS} = \text{Rate} \times \text{Units SOLD}$$

Where: Extracted-but-unsold units sit in inventory.

► *Steps 3 and 4 differ. Depletion on units extracted goes to INVENTORY; only the portion sold hits COGS. Skipping that split is a reliable error.*

PP&E capitalisation — land vs plant

LAND (never depreciated): purchase price, broker/title/legal fees, draining swamps, clearing and grading, assumed mortgage and back taxes, razing old buildings less salvage

PLANT (depreciated): construction-period interest, architect fees, excavation and foundation

Where: Get the asset right and the depreciation follows.

► *Razing an old building is a LAND cost — you are preparing the site, not building the structure. This one shows up constantly.*

Capitalised interest on self-constructed assets

$$\text{Capitalised interest} = \min(\text{Actual interest incurred}, \text{Avoidable interest})$$

$$\text{Avoidable} = \text{Weighted-average accumulated expenditures} \times \text{rate}$$

Where: Use the specific borrowing rate first, then the weighted-average rate on other debt.

► *You can never capitalise MORE than you actually paid. The three conditions: expenditures made, activities in progress, interest being incurred — all three, or you capitalise nothing.*

Long-lived asset impairment

HELD FOR USE – Step 1 (recoverability): if UNDISCOUNTED future cash flows $\geq$ carrying value, no impairment. Step 2: Loss = CV – Fair value

HELD FOR SALE: Loss = CV – (Fair value – Cost to sell)

Where: Two steps for held-for-use, one for held-for-sale.

► Step 1 uses UNDISCOUNTED cash flows; Step 2 uses fair value (usually discounted). Using discounted cash flows in the test is the error the examiners are hunting. Held-for-use impairments can never be restored; held-for-sale ones can.

Goodwill impairment test

Step 0 (optional qualitative): is it more likely than not that FV < CV?

Step 1: Loss = Carrying value of the reporting unit – Fair value of the reporting unit

Where: Loss capped at the carrying amount of goodwill.

► Post-ASU 2017-04 there is no more Step 2 implied-goodwill calculation. Compare the unit's FV to its CV and write goodwill down by the difference, capped at goodwill.

Asset retirement obligation — initial recognition

ARO = PV(expected retirement cash outflows), discounted at the credit-adjusted risk-free rate

Where: DR Asset Retirement Cost (capitalised into PP&E) / CR ARO.

► Two things then happen every year: the capitalised cost is DEPRECIATED, and the liability is ACCRETED. Two separate expenses from one event.

ARO accretion expense

DR Accretion expense Beginning ARO $\times$ credit-adjusted risk-free rate

CR Asset Retirement Obligation same amount

Where: The annual unwinding of the discount.

► Accretion is an OPERATING expense, not interest expense — even though it is mathematically identical to interest.

Cloud computing arrangements — 3 phases

1. Preliminary project (requirements, vendor selection): EXPENSE
2. Application development (configuration, customisation): CAPITALISE implementation costs; expense training and data conversion
3. Post-implementation (maintenance, support): EXPENSE

Where: Amortise the capitalised amount over the hosting term.

► Same three-phase shape as internal-use software. Training and data conversion are ALWAYS expensed, in every phase — that is the detail they test.

Cash equivalents — the 90-day rule

A cash equivalent must be BOTH: (1) readily convertible to a known amount of cash AND (2) have an original maturity of 90 days or less FROM THE ACQUISITION DATE.

Where: Qualifies: T-bills, money market funds, commercial paper.

► ORIGINAL maturity, measured from when YOU bought it — not remaining maturity. A 5-year bond with 60 days left is NOT a cash equivalent. Equity securities never qualify (no maturity).

Bank reconciliation (DO + BINS)

BANK side: Balance + Deposits in transit – Outstanding checks = True cash

BOOK side: Balance + Bank collections + Interest – NSF – Service charges = True cash

Where: Both sides must arrive at the same true cash figure.

► Only the BOOK-side adjustments require journal entries — the bank will fix its own side. That is the exam question hiding inside the reconciliation.

Bond issuance — at par, discount, premium

At par (market = coupon): DR Cash = Face; CR Bonds payable = Face
 At a discount (market > coupon): DR Cash (PV), DR Discount (plug); CR Bonds payable (face)
 At a premium (market < coupon): DR Cash (PV); CR Premium (plug), CR Bonds payable (face)

Where: Cash is always the PV at the MARKET rate.

► Market rate ABOVE coupon $\Rightarrow$ the bond is unattractive $\Rightarrow$ it must be discounted. Reason from the investor's perspective and you will never need to memorise the direction.

Bond effective-interest amortisation

Interest expense = Beginning carrying value $\times$ MARKET rate
 Cash interest = Face $\times$ COUPON rate
 Amortisation = |Interest expense - Cash interest|

Where: The required method under GAAP.

► DISCOUNT: expense > cash, so carrying value RISES toward face. PREMIUM: expense < cash, so carrying value FALLS toward face. Both converge on face at maturity — that is your sanity check.

Pension net periodic cost (SIRAGE)

NPPC = Service cost + Interest cost - Expected Return on plan assets + Amortisation of prior service cost + amortisation of Gains/losses + amortisation of Existing (transition) obligation

Where: S I R A G E.

► The R is SUBTRACTED — the expected return reduces the cost. Note it is the EXPECTED return, not the actual: a generous assumption flatters earnings, which is the earnings-quality angle.

Pension funding entry

DR Net periodic pension cost	SIRAGE total	
CR Cash	Plan contribution	
DR/CR Pension liability (or asset if overfunded)	Plug	

Where: The plug reconciles expense to funding.

► Expense and funding are two different decisions. The difference lands on the balance sheet — which is the point of the entry.

Lease liability (lessee) — REPORT

Lease liability = PV of: Required fixed payments, Exercise price of a purchase option (reasonably certain), Purchase price at end, Only index/rate-variable payments, Residual guarantees likely owed, Termination penalties

Where: Discount at the rate implicit in the lease; if not determinable, the incremental borrowing rate.

► REPORT. Note what is EXCLUDED: variable payments based on usage or sales. Those are expensed as incurred and never enter the liability.

ROU asset (lessee)

ROU asset = Lease liability + Initial direct costs + Prepayments - Lease incentives

Where: ROU = the liability if there are no IDC, prepayments or incentives.

► The asset starts from the liability and adjusts. If the question gives you none of the three add-ons, ROU simply equals the liability.

Finance lease criteria (OWNES)

Finance lease if ANY ONE is met: Ownership transfers, Written purchase option (reasonably certain), Net lease term $\geq$ 75% of economic life, Economic PV of payments $\geq$ 90% of fair value, Specialised asset with no alternative use

Where: Otherwise it is an operating lease.

► OWNES. Any ONE triggers finance classification — they are not cumulative.

The 75% and 90% "bright lines"

Under ASC 842 the 75% economic-life and 90% fair-value tests are NOT strict bright lines (they were under ASC 840).

Where: They are "one reasonable approach".

► Near the threshold, judgement governs, not the number. A lease at 74% is not automatically operating. Expect this exact nuance to be tested.

Finance vs operating lease — initial entry (lessee)

BOTH record the SAME entry at inception:

DR Right-of-Use Asset	LL + IDC + prepaid – incentives
CR Lease Liability	PV of lease payments
CR Cash	IDC + prepaid – incentives

Where: The difference appears only in SUBSEQUENT expense recognition.

► This surprises candidates: the day-one entry is identical. Finance leases then split expense into amortisation + interest (front-loaded). Operating leases report a SINGLE straight-line expense.

Stock issuance above par

DR Cash	Shares × Issue price
CR Common stock	Shares × Par value
CR APIC – Common	Plug (excess over par)

Where: APIC is always the plug.

► Par value is a legal artefact with no economic meaning. Everything above it is APIC — which is why par is often set at \$0.01.

Treasury stock — cost method buyback

DR Treasury stock	Shares × Repurchase price
CR Cash	Shares × Repurchase price

Where: Treasury stock is a CONTRA-EQUITY account.

► No gain or loss on the buyback — ever. A company cannot profit by trading in its own shares. Gains and losses only surface on reissue or retirement, and even then they go to APIC or RE, never to income.

Treasury stock — par value method buyback

DR Treasury stock	Par × shares
DR APIC – Common	Original APIC per share × shares
DR Retained earnings	Plug, if repurchase > original issue price
CR Cash	Repurchase price

Where: Recognises the "loss" at repurchase.

► The par method reverses the original issuance immediately; the cost method waits. Same economics, different timing of the equity hit.

Treasury stock retirement (cost method)

DR Common stock	Par × shares retired
DR APIC – Common	Original APIC per share × shares
DR Retained earnings	Plug, if a loss
CR Treasury stock	Repurchase cost
CR APIC – Treasury	Plug, if a gain

Where: Reverses the original issuance and removes the treasury shares.

► A "gain" goes to APIC — Treasury Stock. A "loss" goes first against any existing APIC — T/S, then to Retained Earnings. Never to income.

Property dividend (in-kind)

First remeasure the asset to FMV:

DR Investment (if a gain) FMV – CV

CR Gain on appreciation FMV – CV

Then declare:

DR Retained earnings FMV of property

CR Property dividends payable FMV of property

Where: Two steps, in this order.

► The remeasurement gain DOES hit income — which is odd, because the company is giving the asset away. That counterintuitive result is exactly why it is examinable.

Premium liability for sales coupons

DR Premium expense Outstanding claims × Cost per premium

CR Premium liability same amount

Where: Accrued at year-end for coupons expected to be redeemed.

► Estimate the redemptions you expect, not the coupons you issued. It is a classic matching-principle accrual.

EXAM TIPS — SELECT BALANCE SHEET ACCOUNTS

- When a balance sheet question feels hard, write the journal entry. The entry forces the direction, and the direction is usually the question.
- Impairment: undiscounted for the TEST, fair value for the MEASUREMENT. Held-for-use cannot be restored; held-for-sale can. Four facts, and the whole topic falls out.
- Leases: same entry at inception, different expense afterwards. Finance = front-loaded (amortisation + interest). Operating = straight-line.

SELECT TRANSACTIONS · 31 formulas

Revenue, income tax, contingencies, consolidation, fair value and accounting changes.

Revenue recognition — the 5-step model

1. Identify the Contract
2. Identify the Performance obligations
3. Determine the Transaction price
4. Allocate the price to the POs (relative standalone selling price)
5. Recognise revenue as each PO is Satisfied

Where: ASC 606.

► Step 4 is where the marks are: allocate on RELATIVE STANDALONE SELLING PRICE, not on stated contract prices. A discount is spread across all obligations unless it demonstrably belongs to one.

Revenue timing — over time vs point in time

Over time if ANY: (1) the customer controls the asset as it is created, (2) the customer simultaneously receives and consumes the benefit, (3) no alternative use AND an enforceable right to payment for work to date. Otherwise, point in time when control transfers.

Where: Control, not risks and rewards.

► The old risks-and-rewards test is gone. ASC 606 asks who CONTROLS the asset — a genuinely different question, and the examiners know candidates still reach for the old one.

Measuring progress — output vs input method

Output: progress = value to the customer (units delivered, milestones, surveys)

Input: progress = the entity's efforts (cost-to-cost, labour hours)

Where: Pick whichever best depicts the transfer of control.

- *Cost-to-cost is the most common input method, but it fails when there are large uninstalled materials on site — you have spent money without transferring anything.*

Long-term contracts — percentage of completion (cost-to-cost)

Progress = Costs to date / Total estimated cost
 Revenue recognised = Progress × Contract price
 Gross profit = Progress × Estimated total profit
 (each less amounts recognised in prior periods)

Where: Cumulative-to-date, then back out the prior periods.

- *An expected total LOSS is recognised IN FULL, IMMEDIATELY — never spread across the contract. That asymmetry (profits spread, losses immediate) is the whole conservatism principle in one rule.*

Variable consideration

Expected value = Σ (probability × outcome) — use when there are MANY possible outcomes
 Most likely amount = the single most probable value — use when there are TWO outcomes

Where: Constrain to the amount that is highly probable not to reverse.

- *Many outcomes $\Rightarrow$ expected value. Binary $\Rightarrow$ most likely amount. Then apply the CONSTRAINT — you may not book variable consideration that could significantly reverse.*

Permanent vs temporary tax differences

PERMANENT (no DTA/DTL): municipal interest, key-man life insurance proceeds and premiums, fines and penalties, 50% of meals, DRD, excess depletion
 TEMPORARY (creates DTA/DTL — it reverses): depreciation, bad debt, warranty, prepaid expenses, equity-method earnings

Where: Only temporary differences create deferred taxes.

- *Ask one question: will this difference EVER reverse? Municipal interest is never taxed, in any year — permanent. Depreciation just shifts timing — temporary.*

DTA vs DTL — the four patterns

INCOME: book first $\rightarrow$ DTL (instalment sales, equity earnings)
 INCOME: tax first $\rightarrow$ DTA (advance rent taxed on receipt)
 EXPENSE: book first $\rightarrow$ DTA (bad debt, warranty)
 EXPENSE: tax first $\rightarrow$ DTL (accelerated tax depreciation, prepaid expenses)

Where: Four combinations, two outcomes.

- *The rule underneath: if you will pay MORE tax later, it is a liability (DTL). If you will pay LESS later, it is an asset (DTA). Derive it and you never memorise the table.*

Uncertain tax positions — two steps

1. Recognition: recognise the benefit only if it is MORE LIKELY THAN NOT (> 50%) to be sustained on examination
2. Measurement: the largest amount that is cumulatively more than 50% likely to be realised

Where: Fail step 1: DR Tax expense / CR Other liabilities (UTP).

- *Two separate hurdles. Passing recognition does not mean you book the full benefit — measurement then cuts it down to the cumulative-50% amount.*

Net operating loss treatment

Post-2017 NOLs: indefinite carryforward, NO carryback, deduction limited to 80% of taxable income
 Pre-2018 NOLs: 2-year carryback, 20-year carryforward, no 80% cap

Where: The TCJA changed this fundamentally.

- *The 80% limitation means a company with a large NOL still pays some tax. Note the vintage of the NOL matters — the question will tell you the year it arose.*

Intraperiod tax allocation

Allocate tax to: (1) continuing operations (2) discontinued operations (3) a retrospective change in accounting principle (4) each OCI item

Where: Each item is presented net of its OWN tax effect.

► Continuing operations gets the tax computed on it; everything else is shown NET. The purpose is to stop a tax benefit in one component from distorting another.

Loss contingency thresholds

Probable AND estimable → ACCRUE the liability and disclose

Reasonably possible → DISCLOSE only

Remote → nothing (except DOG)

Where: ASC 450.

► If a RANGE is given and no amount within it is more likely: accrue the LOWEST end and disclose the range. GAAP takes the low end; IFRS takes the midpoint — a favourite comparison.

Gain contingencies

NEVER accrue. Disclose in the notes only if probable. Recognise in income only when realised or legally certain.

Where: Conservatism.

► The asymmetry with loss contingencies is deliberate: accrue probable losses, never accrue probable gains. That asymmetry IS the answer to most contingency questions.

DOG — the remote-disclosure exception

Disclose even when REMOTE: Debt of others guaranteed; Obligations under standby letters of credit; Guarantees to repurchase receivables sold

Where: The only remote contingencies requiring disclosure.

► DOG. Every other remote contingency gets nothing at all. This narrow exception exists because guarantees are invisible on the balance sheet.

Consolidation adjustments (CARIN BIG)

Eliminate the sub's: Common stock, APIC, Retained earnings; and the parent's Investment in sub. Create NCI at fair value.

Then: adjust the sub's Balance sheet to fair value; record Identifiable intangibles at fair value; Goodwill is the plug.

Where: CARIN BIG.

► Goodwill is always the PLUG. If it comes out negative, it is a BARGAIN PURCHASE GAIN recognised in income immediately — never a negative asset.

Acquisition method — goodwill

Goodwill = Consideration transferred + FV of NCI + FV of previously held interest - FV of identifiable net assets

Where: All four components.

► Do not forget the previously held interest (a step acquisition) — it is remeasured to fair value at the acquisition date, and that remeasurement produces a gain or loss in income.

Intercompany inventory elimination

DR Sales (intercompany)	Full intercompany sales price
CR COGS (intercompany)	Intercompany COGS
CR Inventory	Unrealised profit in ending inventory

Where: Eliminate the full sale plus any unrealised profit on goods still on hand.

► You cannot profit by selling to yourself. Only the profit on goods STILL ON HAND at year-end is unrealised — goods sold on to outsiders are fine.

Intercompany bond extinguishment

DR Bonds payable	Face value
CR Investment in bonds	Parent's carrying value
DR/CR Gain or loss on extinguishment	Plug

Where: The bond is CONSTRUCTIVELY retired when the parent buys it.

► From the consolidated group's view, the debt is gone — even though neither legal entity retired it. The gain or loss appears only in consolidation.

Equity method — carrying value

Ending = Beginning + (% × Investee NI) – (% × Dividends) – Amortisation of FV/CV differences

Where: Significant influence, generally 20–50% ownership.

► Dividends REDUCE the investment — they are a return OF the investment, not income. Recording dividends as revenue is the single most common equity-method error.

Fair value hierarchy

- Level 1: quoted prices in ACTIVE markets for IDENTICAL assets (most reliable)
- Level 2: observable inputs – similar items, inactive-market quotes, observable rates
- Level 3: unobservable inputs – the entity's own models (least reliable)

Where: Maximise observable inputs, minimise unobservable ones.

► Level 1 requires BOTH identical AND active. A quoted price for a similar asset drops you to Level 2 — the word "identical" is doing real work.

Fair value techniques (MIC)

Market (comparable transactions), Income (PV of future cash flows / DCF), Cost (current replacement cost less obsolescence)

Where: MIC.

► The technique and the hierarchy LEVEL are different things. An income approach can use Level 2 or Level 3 inputs — the level depends on the inputs, not the method.

Principal vs most advantageous market

Principal market = the market with the greatest VOLUME and activity. Its price is fair value – EVEN IF another market would pay more.

If there is no principal market: most advantageous = the highest price NET of transaction costs.

Where: Transaction costs are considered in identifying the market, but are NOT part of fair value.

► The principal market wins even when it is worse for you. That counterintuitive rule is exactly what gets tested.

Highest and best use

The use that maximises fair value, judged from a MARKET PARTICIPANT view – not the entity's own intended use. Must be physically possible, legally permissible and financially feasible.

Where: Applies to non-financial assets.

► If you own land you use as a car park but the market would build flats on it, fair value reflects the FLATS. Your intentions are irrelevant.

Change in accounting PRINCIPLE — retrospective

1. Adjust the opening balance of retained earnings for the earliest period presented (net of tax)
2. Restate all prior periods shown
3. Disclose the effect on income, EPS and RE

Where: Exceptions treated PROSPECTIVELY: a change TO LIFO, and a change in depreciation method.

► Those two exceptions exist because the prior-period effect is impracticable to compute. A change in DEPRECIATION METHOD is treated as an estimate change — prospective — which candidates find surprising every time.

Change in accounting ESTIMATE — prospective

1. No restatement of prior periods
2. Apply the new estimate from the current period forward
3. Disclose the effect on NI and EPS

Where: Examples: useful life, salvage value, allowance for doubtful accounts, warranty rate.

► Principle $\Rightarrow$ retrospective. Estimate $\Rightarrow$ prospective. Error $\Rightarrow$ restatement. Three changes, three treatments — and telling them apart IS the question.

Change in reporting ENTITY — retrospective

Restate ALL prior periods presented as if the new entity had always existed. Adjust opening RE. Disclose the effect on income, EPS and RE.

Where: Examples: a change in consolidation scope.

► The most aggressive of the three treatments — you rewrite history entirely, because otherwise the comparatives describe a company that no longer exists.

Error correction — prior period adjustment

1. Restate the prior periods presented
2. Adjust the OPENING retained earnings of the earliest period presented (net of tax) for the cumulative effect on periods not presented
3. Disclose the nature of the error and its effect per period

Where: Errors: mathematical mistakes, misapplied GAAP, oversight, non-GAAP to GAAP.

► A change FROM a non-GAAP method TO a GAAP method is an ERROR CORRECTION, not a change in principle. That reclassification is a favourite trick.

Dividends-received deduction tiers

- < 20% ownership $\rightarrow$ 50% DRD
- 20% to < 80% $\rightarrow$ 65% DRD
- $\geq$ 80% (affiliated) $\rightarrow$ 100% DRD

Where: A PERMANENT difference, not a temporary one.

► Taxable portion = Dividend $\times$ (1 – DRD%). Because it is permanent, it creates NO deferred tax — it just changes the effective rate.

Software costs — internal use

1. Preliminary stage: EXPENSE
2. Application development: CAPITALISE direct costs (coding, configuration, testing); expense training
3. Post-implementation: EXPENSE

Where: ASC 350-40. Amortise straight-line over the useful life.

► Only the MIDDLE phase is capitalised. Training is expensed in every phase, always.

Software costs — sale to others

- Pre-technological feasibility: EXPENSE as R&D
- Post-technological feasibility: CAPITALISE
- Post-release: amortise at the GREATER of (a) straight-line over economic life or (b) current revenue / total expected revenue

Where: ASC 985-20.

► Technological feasibility (a working model or detailed program design) is the switch. And the amortisation takes the GREATER of two methods — a conservatism rule unique to this topic.

R&D costs

- ASC 730 default: EXPENSE as incurred.

Where: Capitalise only when: (1) a tangible asset with an alternative future use, (2) software costs after technological feasibility, (3) IPR&D acquired in a business combination.

► The default is expense, and the exceptions are narrow. IPR&D acquired in a combination becomes an INDEFINITE-life intangible until the project completes or is abandoned.

Warranty liability

DR Warranty expense	Estimated cost of warranties on sales made
CR Warranty liability	same amount

(then, as claims are honoured: DR Warranty liability / CR Cash or Inventory)

Where: Accrued in the period of SALE, not of repair.

► A textbook matching accrual, and a textbook TEMPORARY difference: the book expense comes now, the tax deduction comes when the repair is actually performed — so it creates a DTA.

EXAM TIPS — SELECT TRANSACTIONS

- Contingencies: accrue probable losses, never accrue gains, and disclose remote items only under DOG. Three rules, and the topic is finished.
- Accounting changes: principle $\Rightarrow$ retrospective; estimate $\Rightarrow$ prospective; error $\Rightarrow$ restatement. The question is almost always which bucket the change falls into, not how to do the mechanics.
- Deferred tax: ask whether the difference will ever reverse. If not, it is permanent and creates no DTA/DTL — regardless of how large it is.

PASSING FAR

What FAR actually rewards

- Volume of practice, not depth of theory. FAR is the broadest section; the winning strategy is coverage plus repetition.
- Journal entries. If you can write the entry, you can answer the question — including questions that never mention an entry.
- Speed. There is a lot of content and not much time. Recognition must be automatic.

The highest-yield areas

- Leases, pensions and deferred tax — heavily tested, mechanically hard, and where most candidates lose ground.
- Governmental accounting — roughly 10% of the exam, entirely learnable, and routinely under-prepared because it feels alien.
- Consolidation and the equity method. Know when dividends reduce an investment and when they are income.
- Revenue recognition (ASC 606). The five steps, and especially the relative-standalone-selling-price allocation.

The traps that cost people the exam

- Gains SUBTRACTED in the indirect method cash flow statement.
- Impairment: undiscounted for the test, fair value for the measurement.
- Small stock dividend at FMV; large stock dividend at par.
- Original maturity (not remaining) for the 90-day cash equivalent rule.
- Aging method backs out the existing allowance; % of sales does not.
- Anti-dilutive securities are excluded — and in a loss year, everything is anti-dilutive.

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