

US GAAP COMPREHENSIVE CHECKLIST







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I. General Accounting Principles under US GAAP – Comprehensive Explanation

CAccrual Basis of Accounting

Requirement:

• Financial statements **must** be prepared using the **accrual basis** (not cash basis) unless an exception is granted.

Meaning:

- Recognize revenues when earned (not necessarily when cash is received).
- Recognize expenses when incurred (not when paid).

Relevant Standard:

- ASC 605 (prior) / ASC 606 (current) for revenue recognition
- Fundamental principle: Matching revenues with expenses.

Checklist for Compliance:

- Are revenues recorded when services are performed or goods delivered?
- Are expenses accrued when obligations arise, even if unpaid?

• Example:

An insurance company bills customers in December 2024 for a policy starting January 2025. Under accrual accounting, revenue is recognized in **2025**, not 2024.

2 Going Concern Assumption

Requirement:

• Companies must assess whether there are substantial doubts about their ability to continue as a going concern for at least one year after the financial statements' issuance date.

Relevant Standard:



• ASC 205-40 ("Presentation of Financial Statements — Going Concern")

Checklist for Compliance:

- Are there indicators of financial distress (e.g., losses, liquidity issues)?
- Has management prepared mitigation plans?
- Is the disclosure appropriate if substantial doubt exists?

• Example:

If a company has recurring losses, negative cash flows, and debt maturities due in 12 months without financing plans — disclosure is **mandatory**.

3 Consistency of Accounting Policies

Requirement:

• Same accounting principles and methods must be applied across periods unless a change is justified and disclosed.

Relevant Standard:

• ASC 250 ("Accounting Changes and Error Corrections")

Checklist for Compliance:

- Has there been any change in methods (e.g., inventory costing, depreciation method)?
- If yes, is it **retrospectively applied** (unless impractical) and disclosed with the reason?
- Are comparatives restated?

• Example:

Switching from **FIFO** to **Weighted Average** for inventory valuation must be disclosed and adjusted retrospectively.

4 Reasonable Estimates

Requirement:

• Many aspects of financial reporting (e.g., impairment, warranty liabilities) **rely on estimates**.



• Estimates must be reasonable, supportable, and based on best available information.

Relevant Standard:

• ASC 250 (for changes in estimates)

Checklist for Compliance:

- Are assumptions reasonable and consistent with market evidence?
- Are estimation techniques documented?
- Are changes in estimates (not errors) treated prospectively?

• Example:

Bad debt provision for receivables based on historical collection experience and forward-looking information.

5 Materiality Considerations

Requirement:

- Only **material** information must be disclosed or adjusted.
- An omission or misstatement is material if it could **influence the decisions** of financial statement users.

Relevant Standard:

 FASB Concepts Statement No. 8, Chapter 3 (Qualitative Characteristics of Useful Financial Information)

Checklist for Compliance:

- Are immaterial corrections avoided unless they aggregate to materiality?
- Are materiality judgments applied quantitatively and qualitatively?
- Have small but qualitatively material errors (like fraud) been addressed?

• Example:

\$1,000 misstatement in a billion-dollar company may be immaterial, but undisclosed related-party transactions — even if small — may be **qualitatively material**.



SQ Quick Table Summary of Section 1

#	Principle	Key Focus	Relevant Standard
1	Accrual Basis	Recognize revenues earned and expenses incurred	Fundamental; ASC 606
2	Going Concern	12 months forward-looking ability	ASC 205-40
3	Consistency	Consistent accounting policies across periods	ASC 250
4	Reasonable Estimates	Based on best available info	ASC 250
5	Materiality	Influence user decisions	Concepts Statement No. 8

o Practical Application Tip

Always document:

- Your going concern evaluation (board minutes, liquidity analysis).
- Any accounting policy changes.
- Critical judgments for estimates.
- Materiality thresholds used for financial reporting.

Proper documentation **strengthens your position** during audit reviews and regulatory inspections.



□ 2. Presentation and Disclosure Requirements under US GAAP – Comprehensive Explanation

D Primary Financial Statements Presentation

Requirement:

• All major financial statements must be prepared and presented.

Mandatory Statements:

- Balance Sheet (Statement of Financial Position)
- Income Statement (Statement of Operations or Profit & Loss)
- Statement of Comprehensive Income (if OCI exists)
- Statement of Changes in Equity (Stockholders' Equity Reconciliation)
- Statement of Cash Flows
- Notes to Financial Statements

Relevant Standard:

• ASC 205 ("Presentation of Financial Statements")

Checklist for Compliance:

- Are all primary statements presented clearly?
- Is each statement properly titled and dated?
- Are captions used consistently across periods?

• Example:

Present "Total Assets" and "Total Liabilities and Stockholders' Equity" with clear subtotals.

2 Comparative Financial Statements

Requirement:

• Companies **must** present comparative financial statements (typically **two years** minimum).



Relevant Standard:

- **Regulation S-X** (for SEC filers)
- General US GAAP practice for private companies.

Checklist for Compliance:

- Are prior periods' corresponding figures shown side-by-side with current periods?
- If restatements exist, are prior periods adjusted accordingly?

• Example:

Present Balance Sheets as of **December 31, 2025**, and **December 31, 2024** side-by-side.

S Cash Flow Statement Preparation

Requirement:

- Cash Flows must be classified into:
 - **Operating activities**
 - Investing activities
 - Financing activities
- Choose Direct Method (preferred but rare) or Indirect Method (common).

Relevant Standard:

• ASC 230 ("Statement of Cash Flows")

Checklist for Compliance:

- Is cash from operations reconciled from net income (if indirect method)?
- Are non-cash investing/financing activities disclosed separately (e.g., lease inception)?

• Example:

Issuing stock to purchase equipment must be disclosed as a **non-cash transaction**, not included in cash flows.

4 Correction of Prior Period Errors



Requirement:

- Material errors must be retrospectively restated.
- Immaterial errors may be corrected prospectively with disclosure.

Relevant Standard:

• ASC 250 ("Accounting Changes and Error Corrections")

Checklist for Compliance:

- Has the nature of the error been explained?
- Is the impact on prior period financials clearly disclosed?
- Is the cumulative adjustment to retained earnings shown?

• Example:

If depreciation expense was materially understated in 2024, restate 2024 figures and adjust opening 2025 retained earnings.

5 Disclosure of Subsequent Events

Requirement:

• Events occurring after balance sheet date but before financials are issued must be evaluated.

V Types of Subsequent Events:

- **Type I**: Recognized events (conditions existed at balance sheet date) → Adjust financials.
- **Type II**: Non-recognized events (conditions arose after balance sheet date) → Disclose only.

Relevant Standard:

• ASC 855 ("Subsequent Events")

Checklist for Compliance:

- Is a review process established up to the financial statement issuance date?
- Are adjusting and non-adjusting events properly identified?
- Are material subsequent events disclosed clearly?



• Example:

Settlement of a lawsuit **after year-end** but related to a pre-existing condition — must be **adjusted**.

• Example:

Major acquisition agreed after year-end — only **disclose**, no adjustment.

#	Principle	Key Focus	Relevant Standard
1	Primary Statements	Full set of required financial statements	ASC 205
2	Comparative Statements	Present side-by-side prior years	Regulation S-X (SEC) / General Practice
3	Cash Flow Statement	Indirect/Direct method, Non- cash disclosures	ASC 230
4	Prior Period Errors	Retrospective restatement	ASC 250
5	Subsequent Events	Adjust/Disclose based on type	ASC 855

SQuick Table Summary of Section 2

OF Practical Application Tip

Before finalizing financials:

- Perform a subsequent events review checklist.
- Conduct a **final consistency check** across all statements and notes.
- Ensure **cross-references** are accurate between primary statements and disclosures.



3. Revenue Recognition (ASC 606) under US GAAP – Comprehensive Explanation

First: Understand ASC 606 — The Core Principle

Revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration the company expects to receive.

I The 5-Step Revenue Recognition Model

Step Description

- 1 Identify the contract(s) with a customer
- 2 Identify the performance obligations in the contract
- 3 Determine the transaction price
- 4 Allocate the transaction price to the performance obligations
- 5 Recognize revenue when (or as) each performance obligation is satisfied

Detailed Step-by-Step Compliance

D Identify the Contract(s) with a Customer

Requirement:

- A contract exists if:
 - It has commercial substance.
 - o Rights and payment terms are identifiable.
 - o It is probable the entity will collect the consideration.

Checklist for Compliance:

Is there a written, verbal, or implied contract?



- Are enforceable rights and obligations clearly identified?
- Are collectability risks evaluated?

• Example:

Signing a subscription agreement for a SaaS platform.

2 Identify the Performance Obligations

Requirement:

- A performance obligation is a **promise** to transfer a distinct good or service.
- Multiple promises may exist analyze if they are separately identifiable.

Checklist for Compliance:

- Are distinct goods/services separated correctly?
- Are bundled services analyzed for separate obligations?

• Example:

A mobile phone with a 2-year service contract — two distinct obligations (device + service).

3 Determine the Transaction Price

Requirement:

• Consider fixed amounts, variable consideration, time value of money, noncash consideration, and consideration payable to the customer.

Checklist for Compliance:

- Have discounts, rebates, penalties, bonuses been considered?
- Are constraints applied where variable consideration is uncertain?

Example:

Performance bonus based on project completion date must be estimated conservatively.

Allocate the Transaction Price to Performance Obligations



Requirement:

- Allocate based on relative standalone selling prices.
- If prices are not directly observable, estimate using appropriate methods (adjusted market assessment, expected cost plus margin, residual approach).

Checklist for Compliance:

- Are allocation methods documented and applied consistently?
- Are discounts or variable amounts allocated properly?

• Example:

Selling software and customization service — allocate total price based on standalone selling prices of each.

5 Recognize Revenue When (or As) Performance Obligations Are Satisfied

Requirement:

- Revenue is recognized either:
 - **Over time** (percentage of completion, e.g., construction)
 - At a point in time (e.g., retail sale)

Checklist for Compliance:

- Have criteria for "over time" recognition been assessed?
- If point-in-time, is transfer of control properly evidenced (e.g., title, physical possession)?

• Example:

A manufacturing company delivers machinery — revenue recognized **when control transfers** to the buyer.

Concept	Explanation
Contract Modifications	Must reassess if new performance obligations are created.

Key Supporting Concepts under ASC 606



Variable Consideration	Estimate using either expected value or most likely amount.
Significant Financing Component	Adjust revenue if payment timing creates financing effect.
Nonrefundable Upfront Fees	Recognized over time, not immediately.
Principal vs. Agent Considerations	Gross vs. net presentation based on control of goods/services.

SQuick Table Summary

#	Step	Key Focus
1	Contract	Existence, enforceability, collectability
2	Performance Obligations	Separately identifiable goods/services
3	Transaction Price	Fixed + variable components
4	Allocation	Standalone selling prices basis
5	Recognition	Over time or at a point in time

Practical Application Tip

- Maintain contract inventories detailed tracking of contracts and performance obligations.
- Document judgments in:
 - Determining significant financing components.
 - Estimating variable consideration.
 - Assessing satisfaction of performance obligations.

+ Important:

ASC 606 requires **extensive disclosures** in the notes — about:

- Disaggregation of revenue,
- Contract balances (receivables, contract assets/liabilities),
- Performance obligations outstanding.



I Examples of Errors Commonly Found

Error	Example
Ignoring variable consideration	Not adjusting revenue for expected rebates.
Misidentifying performance obligations	Bundling installation service with product incorrectly.
Incorrect point of revenue recognition	Recognizing revenue before control is transferred.
Omitting contract modifications	Not reassessing allocation after contract amendments.

Mini Checklist for ASC 606 Compliance

Checkpoint	Status (✔/Ⅹ)
Contract criteria met	
Separate performance obligations identified	
Transaction price reflects expected consideration	
Transaction price properly allocated	
Revenue recognized based on satisfaction of obligation	
Full disclosure of contract balances, judgements, and methods used	

© Conclusion

ASC 606 represents a principle-based, risk-focused model that requires:

- Careful contract analysis,
- Thoughtful application of estimates,
- Strong internal controls for contract modifications and pricing elements,
- Detailed note disclosures.

Failure to comply can lead to significant audit adjustments, SEC comments (for public companies), and loss of investor confidence.





□ 4. Inventory (ASC 330) under US GAAP – Comprehensive Explanation

First: Understand ASC 330 — The Core Principle

Inventory must be stated at the **lower of cost or net realizable value (NRV)** and must reflect **all costs** necessary to bring inventory to its current condition and location.

ASC 330 focuses heavily on **proper valuation, costing methods**, and **loss recognition**.

Detailed Step-by-Step Compliance

D Valuation: Lower of Cost or Net Realizable Value (LCNRV)

Requirement:

- Inventory should be reported at the lower of:
 - **Cost** (historical acquisition/manufacturing cost)
 - Net Realizable Value (NRV) (estimated selling price less costs of completion, disposal, and transportation)

Checklist for Compliance:

- Is NRV assessed regularly (at least annually)?
- Are write-downs recognized immediately in the P&L?
- Are reversals of write-downs prohibited under US GAAP?

• Example:

If inventory cost = \$500 but estimated selling price = \$450 (less \$20 selling costs = \$430 NRV), inventory must be written down to **\$430**.

2 Inventory Costing Methods

Requirement:



• Consistent and appropriate **cost flow assumption** must be selected and applied.

Permissible Methods under US GAAP:

- **FIFO** (First-In, First-Out)
- **LIFO** (Last-In, First-Out)
- Weighted Average Cost
- **Specific Identification** (for unique, high-value items)

Checklist for Compliance:

- Is the costing method disclosed in the financials?
- If LIFO is used, is the LIFO Reserve properly disclosed?
- Are changes in method (e.g., FIFO to Weighted Average) justified and applied retrospectively?

• Example:

A company using **LIFO** must disclose the **difference** between LIFO and FIFO (called **LIFO Reserve**) to provide comparability.

Components of Inventory Cost

Requirement: Inventory cost includes:

- Purchase price
- Conversion costs (labor, manufacturing overhead)
- Other costs necessary to bring inventory to saleable condition and location

Excluded Costs:

- Abnormal wastage
- Storage costs unrelated to production
- Administrative overhead
- Selling costs

Checklist for Compliance:

• Are abnormal costs excluded?



• Are freight-in and handling included appropriately?

• Example:

Freight charges to receive raw materials = **capitalized**; warehousing finished goods = **expensed** unless integral to production.

4 Inventory Obsolescence and Shrinkage

Requirement:

- Inventory must be **reduced** for:
 - Obsolescence (e.g., out-of-date items)
 - Deterioration (e.g., perishable goods)
 - Shrinkage (e.g., theft, loss)

Checklist for Compliance:

- Are periodic physical counts performed and reconciled?
- Is a reserve created for slow-moving or obsolete items?
- Are shrinkage losses recorded promptly?

• Example:

Electronics manufacturer identifies obsolete mobile devices — inventory must be **written down to recoverable value**.

5 Inventory Disclosures

Requirement: Key disclosures include:

- Inventory breakdown (raw materials, work-in-progress, finished goods)
- Costing method (FIFO, LIFO, etc.)
- Significant write-downs and their reasons
- Changes in inventory methods and impacts

Checklist for Compliance:

• Is inventory presented separately in the balance sheet?



• Are material inventory losses/writedowns disclosed?

• Example:

If inventory valued at ₹10M is written down by ₹2M due to obsolescence, disclose the amount and reason in footnotes.

🕸 Quick Table Summary

#	Key Area	Requirements
1	Valuation	Lower of Cost or Net Realizable Value
2	Costing Methods	FIFO, LIFO, Weighted Average, Specific Identification
3	Inventory Costs	Include direct and necessary costs only
4	Obsolescence/Shrinkage	Adjust promptly for losses
5	Disclosures	Cost method, major categories, write-downs

Q Practical Tips for Good Practice

- Review NRV for major inventory items quarterly (not just annually).
- Track slow-moving items separately flag those exceeding aging thresholds.
- Implement cycle counts throughout the year to detect discrepancies early.
- **Document assumptions** used in evaluating obsolescence (e.g., sales history, market conditions).
- If using **LIFO**, monitor and disclose **LIFO** liquidation effects carefully (e.g., when old inventory layers are sold off).

(Common Errors to Avoid



Error	Example
Failing to write down slow-moving stock	Old models of cellphones kept at original cost
Incorrect cost inclusion	Including marketing expenses in inventory cost
Inadequate disclosure of costing method	Not mentioning LIFO or FIFO in notes
Improper treatment of freight charges	Treating outbound shipping costs as part of inventory value

© Conclusion

Inventory is one of the most **manipulated and sensitive areas** in financial reporting. Ensuring proper valuation, costing, and transparent disclosure is **critical** to maintain stakeholder trust and pass audit scrutiny.

Good inventory accounting directly impacts:

- Gross margins
- Working capital
- Valuation of the company



□ 5. Property, Plant, and Equipment (ASC 360) under US GAAP – Comprehensive Explanation

First: Understand ASC 360 — The Core Principle

Property, Plant, and Equipment (PPE) should be recorded at **historical cost** and **depreciated systematically** over their useful lives, with periodic reviews for **impairment** when indicators exist.

PPE is typically the **largest asset group** for manufacturing, service, and infrastructure companies.

Detailed Step-by-Step Compliance

Initial Recognition of PPE

Requirement:

- Record PPE at historical cost, including:
 - Purchase price
 - o Import duties, non-refundable taxes
 - Directly attributable costs to bring the asset to working condition (installation, site prep)

Checklist for Compliance:

- Is the cost of purchase adjusted for discounts and rebates?
- Are directly attributable costs included?
- Are startup/administrative/general costs excluded?

• Example:

Cost of a new machine includes:

Purchase Price + Freight + Installation + Trial Runs — but excludes CEO visit costs.



2 Capitalization vs. Expense

Requirement:

- Capitalize expenditures that:
 - o Increase useful life
 - Increase productivity
 - Increase asset capacity
- Expense routine maintenance and repairs.

Checklist for Compliance:

- Are major overhauls capitalized?
- Are repairs and maintenance costs expensed immediately?
- Are capitalization policies documented?

• Example:

Engine replacement that extends aircraft life — **capitalize**. Oil change for truck — **expense**.

3 Depreciation / Amortization

Requirement:

- Systematically allocate asset cost (less salvage value) over useful life.
- Common methods:
 - Straight-Line (most common)
 - Declining Balance
 - Units of Production

Checklist for Compliance:

- Is the depreciation method reflective of asset use?
- Are useful lives periodically reassessed?
- Is salvage/residual value considered?



• Example:

A machine costing \$100,000, estimated life 5 years, no salvage value:

• Depreciation per year = **\$20,000** (Straight Line).

4 Impairment of PPE

Requirement:

- PPE must be tested for impairment if triggering events occur:
 - o Significant decline in asset market value
 - Changes in use
 - Physical damage
 - Adverse economic/legal factors

Impairment Testing: Two-Step Model (ASC 360):

- Step 1: Recoverability Test → Is carrying amount recoverable based on undiscounted cash flows?
- Step 2: If not recoverable \rightarrow Impair down to fair value.

Checklist for Compliance:

- Are impairment indicators monitored?
- Is impairment loss recognized immediately in P&L?
- Are reversals of impairment prohibited under US GAAP?

• Example:

A manufacturing plant significantly underutilized due to regulatory changes must be **tested for impairment**.

5 Disposal or Retirement of PPE

Requirement:

- Upon disposal:
 - Remove asset cost and accumulated depreciation.



• Recognize any resulting gain or loss in the income statement.

Checklist for Compliance:

- Is disposal properly recorded?
- Are proceeds (if any) matched against carrying value?
- Are gains/losses disclosed separately if material?

• Example:

Sold old equipment for \$5,000; Net Book Value = $4,000 \rightarrow \text{Record } 1,000 \text{ Gain}$.

C Disclosure Requirements for PPE

Mandatory Disclosures Include:

- Classes of PPE assets (buildings, machinery, vehicles, etc.)
- Depreciation methods used
- Useful lives/rate of depreciation
- Accumulated depreciation
- Impairment losses recognized

Checklist for Compliance:

- Are classes of assets disclosed with carrying amounts?
- Are impairments separately disclosed?
- Are material disposals explained?

• Example:

Footnotes must mention that machinery is depreciated over **10–15 years** using the **straight-line method**.

😵 Quick Table Summary

#	Key Area	Requirements
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1	Initial Recognition	Cost + directly attributable costs
2	Capital vs Expense	Capex if useful life/productivity increases
3	Depreciation	Over useful life, appropriate method
4	Impairment	Trigger-based, two-step test
5	Disposal	Record gains/losses
6	Disclosure	Classes, methods, lives, impairments

Q Practical Tips for Good Practice

- Maintain detailed fixed asset registers (FAR) with:
 - Description
 - Purchase date
 - o Original cost
 - \circ Location
 - Useful life
 - Accumulated depreciation
- Conduct annual physical verification of fixed assets.
- Review useful lives during major technological/market changes.
- **Document impairment assumptions and calculations** critical for audit defense.

(Common Errors to Avoid

Error	Example
Capitalizing maintenance	Painting a building treated as asset enhancement
Delayed impairment testing	Ignoring impairment despite known damage
Overstated useful life	Machinery depreciated over 10 years even though obsolete in 5



© Conclusion

Proper management of PPE is **essential** for accurate asset valuation, depreciation expense control, and protection of shareholder value.

US GAAP demands a rigorous and transparent approach toward:

- Recognition,
- Depreciation,
- Impairment, and
- Disclosure.

Errors or manipulation in PPE accounting can materially misstate financial results and attract **regulatory scrutiny**.



6. Leases (ASC 842) under US GAAP – Comprehensive Explanation

First: Understand ASC 842 — The Core Principle

ASC 842 requires **lessees** to recognize **most leases on the balance sheet** as a **Right-of-Use (ROU) asset** and a **Lease Liability**, whether operating or finance leases.

This standard replaced the old ASC 840, which allowed many operating leases to remain "off-balance sheet."

Detailed Step-by-Step Compliance

D Identifying a Lease

Requirement:

- A lease exists if:
 - The contract conveys the **right to control the use** of an identified asset.
 - The customer obtains substantially **all economic benefits** from use.

Checklist for Compliance:

- Is there an identified asset (explicit or implicit)?
- Does the lessee have control over the asset's use?

• Example:

A 5-year agreement to use a specific office space = **lease**.

2 Lease Classification: Finance vs. Operating Lease

Requirement: A lease is a **Finance Lease** if **any one** of the following is met:

- Ownership transfers at end of lease.
- Bargain purchase option exists.
- Lease term covers majority of the asset's useful life.



- PV of lease payments ≈ substantially all fair value.
- Asset is so specialized, no alternative use.

If none, it's an **Operating Lease**.

Checklist for Compliance:

- Have all five tests been evaluated?
- Has lease classification been documented?

• Example:

Lease of machinery for 90% of useful life \rightarrow likely a **Finance Lease**.

Initial Measurement of Right-of-Use (ROU) Asset and Lease Liability

Requirement:

- Lease Liability = Present Value (PV) of lease payments.
- ROU Asset = Lease liability + initial direct costs + prepayments incentives received.

Checklist for Compliance:

- Correct discount rate used (incremental borrowing rate or implicit rate)?
- Are all fixed payments and variable payments included properly?

• Example:

Lease with \$10,000 annual payments over 5 years, discount rate 5%. Calculate PV to book liability.

4 Subsequent Measurement

For Finance Leases:

• Interest expense and amortization expense separately recognized.

For Operating Leases:

• Single lease expense on a straight-line basis over lease term.

Checklist for Compliance:



- Are amortization and lease expense recorded consistently?
- Is remeasurement done if lease terms change (e.g., modification)?

Example:

Renting office space — recognize straight-line lease expense under Operating Lease.

5 Short-Term Lease Exemption

Requirement:

• Leases 12 months or less can be kept off-balance sheet if election is made.

Checklist for Compliance:

- Are short-term leases tracked separately?
- Is the short-term lease policy consistently applied?

• Example:

A 10-month warehouse lease with no renewal option — may remain off-balance sheet.

€ Key Disclosures for Leases

Mandatory Disclosures Include:

- ROU assets and lease liabilities separately in balance sheet.
- Lease cost components (finance leases, operating leases, variable leases).
- Maturity analysis of lease payments.
- Significant assumptions (discount rate, lease term, options exercised).

Checklist for Compliance:

- Are lease expenses broken into categories in the footnotes?
- Are weighted-average remaining lease terms and discount rates disclosed?
- Are sale-leaseback transactions (if any) properly disclosed?

• Example:

Show future minimum lease payments for each of the next 5 years + total thereafter.



🕸 Quick Table Summary

#	Key Area	Requirements
1	Lease Identification	Control over use of asset
2	Classification	Finance vs. Operating
3	Initial Measurement	PV of payments; ROU Asset setup
4	Subsequent Measurement	Amortization (finance) / Lease expense (operating)
5	Short-Term Leases	Exemption if \leq 12 months
6	Disclosures	Lease terms, costs, assumptions

Q Practical Tips for Good Practice

- Create a Lease Inventory Database record all leases centrally.
- Implement lease software or templates to automate PV calculations.
- Set up renewal/termination alerts lease modifications often trigger remeasurement.
- Maintain documentation for discount rate determinations.

(Common Errors to Avoid

Error	Example
Missing embedded leases	Lease elements hidden in service contracts
Wrong discount rate used	Ignoring implicit rate when determinable
Incorrect classification	Classifying finance lease as operating
Forgetting lease modifications	Not updating ROU asset and liability when lease is changed
Incomplete disclosures	Missing maturity analysis or weighted average term

© Conclusion



ASC 842 brings greater transparency and comparability by putting almost all leases on the balance sheet.

A disciplined approach to **lease tracking**, **classification**, **measurement**, **and disclosure** is essential to avoid misstatements.

Companies must **continuously monitor** lease agreements throughout the contract lifecycle — not just at inception.



□ 7. Financial Instruments (ASC 825 and ASC 815) under US GAAP – Comprehensive Explanation

First: Understand the Core Principle

Financial instruments must be **measured**, **presented**, and **disclosed** in a manner that fairly represents their **value**, **risk**, and **economic characteristics**.

Some instruments are also subject to hedge accounting under ASC 815.

This area includes:

- **Debt instruments** (bonds, loans)
- Equity instruments (stocks)
- **Derivatives** (options, swaps, forwards)
- Embedded derivatives

Detailed Step-by-Step Compliance

D Initial Recognition and Measurement (ASC 825)

Requirement:

- Financial assets and liabilities are initially recognized at **fair value** plus (or minus) transaction costs.
- Subsequent measurement depends on classification (amortized cost, fair value through income, fair value through OCI).

Checklist for Compliance:

- Is the initial measurement at fair value?
- Are transaction costs properly accounted for based on classification?

• Example:

Issuing a bond: record proceeds received (net of issuance costs) and set up liability at fair value.



2 Fair Value Measurement Hierarchy (ASC 820 link)

Requirement:

- Level 1: Quoted prices in active markets.
- Level 2: Observable inputs other than quoted prices.
- Level 3: Unobservable inputs (internal models).

Checklist for Compliance:

- Has the instrument been classified into Level 1, 2, or 3?
- Are fair value techniques consistently applied?
- Are valuation models documented for Level 3 items?

• Example:

Quoted shares \rightarrow Level 1. Interest rate swaps priced using yield curves \rightarrow Level 2. Complex private equity valuations \rightarrow Level 3.

Credit Loss Allowance (CECL Model – ASC 326)

Requirement:

- Apply the Current Expected Credit Loss (CECL) model to:
 - o Loans
 - Trade receivables
 - Debt securities carried at amortized cost

Checklist for Compliance:

- Are lifetime expected losses estimated?
- Are historical experience, current conditions, and forward-looking info considered?
- Is the methodology documented?



• Example:

Estimate expected credit loss for customer receivables even if there are **no actual defaults** yet — proactive provisioning.

4 Accounting for Derivatives (ASC 815)

Requirement:

- All derivatives must be recognized as either assets or liabilities at fair value.
- Hedge Accounting may be applied only if specific stringent criteria are met.

Types of Derivatives:

- Forwards
- Futures
- Options
- Interest rate swaps
- Commodity swaps

Checklist for Compliance:

- Are derivatives recognized on the balance sheet (not off-balance sheet)?
- Are embedded derivatives separated and accounted separately if needed?
- Is documentation for hedge accounting (designation, effectiveness testing) maintained?

• Example:

An interest rate swap contract hedging a variable rate debt — must be recorded at fair value, with hedge effectiveness tested periodically.

Hedge Accounting Rules (Optional and Complex)

Three Main Types:

- Fair Value Hedge (hedging changes in asset/liability fair value)
- Cash Flow Hedge (hedging variability of cash flows)
- Net Investment Hedge (hedging foreign operations)



Checklist for Hedge Accounting Compliance:

- Has the hedge relationship been documented at inception?
- Is hedge effectiveness evaluated and documented (qualitative or quantitative)?
- Are ineffective portions properly recognized in P&L?

• Example:

Hedging forecasted foreign currency sales — changes in derivative's fair value deferred in OCI and reclassified when the sale occurs.

6 Disclosures Requirements

Mandatory Disclosures Include:

- Carrying amounts and fair values of financial instruments.
- Fair value hierarchy levels (Level 1, 2, 3).
- Derivative instruments and hedging activities details.
- Credit risk concentration disclosures.
- CECL assumptions and sensitivities.

Checklist for Compliance:

- Are gross and net exposures disclosed (for derivatives)?
- Are risks and strategies behind hedging disclosed?
- Is the impact of credit losses disclosed in a clear manner?

• Example:

Footnotes describing methods used for fair value, carrying value vs. market value for bonds, qualitative discussion of credit loss drivers.

😵 Quick Table Summary

#	Key Area	Requirements
1	Initial Recognition	Fair value + transaction costs
2	Fair Value Hierarchy	Level 1, 2, 3 classification



3	Credit Losses	CECL model (forward-looking loss estimate)
4	Derivatives	Fair value on balance sheet
5	Hedge Accounting	Documentation, effectiveness testing
6	Disclosures	Fair value, risk exposures, CECL, derivatives

Practical Tips for Good Practice

- Create a Financial Instrument Inventory: List all debt, equity, derivatives.
- **Centralize Fair Value Assumptions**: Build a repository of valuation models and market inputs.
- **Document Hedging Strategies**: Always prepare clear contemporaneous documentation.
- **Perform Sensitivity Analysis**: Evaluate how changes in key assumptions affect fair value and CECL reserves.

Error	Example
Ignoring embedded derivatives	Not bifurcating derivatives in hybrid contracts
Incomplete hedge documentation	Failing effectiveness testing documentation
Misapplying fair value hierarchy	Classifying illiquid securities as Level 1
Late recognition of credit losses	Waiting until default happens rather than estimating proactively

(Common Errors to Avoid

© Conclusion

Financial instruments accounting under US GAAP emphasizes **fair value transparency**, **credit risk assessment**, and **comprehensive disclosure**. It requires **technical precision** in valuation, **rigorous internal controls** for derivative contracts, and **clear explanations** in financial reporting.



Missteps here could not only lead to **material misstatements** but also trigger **regulatory scrutiny** (especially for public companies and financial institutions).



□ 8. Financial Instruments (ASC 825 and ASC 815) under US GAAP – Comprehensive Explanation

First: Understand the Core Principle

Financial instruments must be **measured**, **presented**, and **disclosed** in a manner that fairly represents their **value**, **risk**, and **economic characteristics**.

Some instruments are also subject to hedge accounting under ASC 815.

This area includes:

- Debt instruments (bonds, loans)
- Equity instruments (stocks)
- **Derivatives** (options, swaps, forwards)
- Embedded derivatives

Detailed Step-by-Step Compliance

D Initial Recognition and Measurement (ASC 825)

Requirement:

- Financial assets and liabilities are initially recognized at **fair value** plus (or minus) transaction costs.
- Subsequent measurement depends on classification (amortized cost, fair value through income, fair value through OCI).

Checklist for Compliance:

- Is the initial measurement at fair value?
- Are transaction costs properly accounted for based on classification?

• Example:

Issuing a bond: record proceeds received (net of issuance costs) and set up liability at fair value.



2 Fair Value Measurement Hierarchy (ASC 820 link)

Requirement:

- Level 1: Quoted prices in active markets.
- Level 2: Observable inputs other than quoted prices.
- Level 3: Unobservable inputs (internal models).

Checklist for Compliance:

- Has the instrument been classified into Level 1, 2, or 3?
- Are fair value techniques consistently applied?
- Are valuation models documented for Level 3 items?

• Example:

Quoted shares \rightarrow Level 1. Interest rate swaps priced using yield curves \rightarrow Level 2. Complex private equity valuations \rightarrow Level 3.

Credit Loss Allowance (CECL Model – ASC 326)

Requirement:

- Apply the Current Expected Credit Loss (CECL) model to:
 - o Loans
 - Trade receivables
 - Debt securities carried at amortized cost

Checklist for Compliance:

- Are lifetime expected losses estimated?
- Are historical experience, current conditions, and forward-looking info considered?
- Is the methodology documented?



• Example:

Estimate expected credit loss for customer receivables even if there are **no actual defaults** yet — proactive provisioning.

4 Accounting for Derivatives (ASC 815)

Requirement:

- All derivatives must be recognized as either assets or liabilities at fair value.
- Hedge Accounting may be applied only if specific stringent criteria are met.

Types of Derivatives:

- Forwards
- Futures
- Options
- Interest rate swaps
- Commodity swaps

Checklist for Compliance:

- Are derivatives recognized on the balance sheet (not off-balance sheet)?
- Are embedded derivatives separated and accounted separately if needed?
- Is documentation for hedge accounting (designation, effectiveness testing) maintained?

• Example:

An interest rate swap contract hedging a variable rate debt — must be recorded at fair value, with hedge effectiveness tested periodically.

Hedge Accounting Rules (Optional and Complex)

Three Main Types:

- Fair Value Hedge (hedging changes in asset/liability fair value)
- Cash Flow Hedge (hedging variability of cash flows)
- Net Investment Hedge (hedging foreign operations)



Checklist for Hedge Accounting Compliance:

- Has the hedge relationship been documented at inception?
- Is hedge effectiveness evaluated and documented (qualitative or quantitative)?
- Are ineffective portions properly recognized in P&L?

• Example:

Hedging forecasted foreign currency sales — changes in derivative's fair value deferred in OCI and reclassified when the sale occurs.

6 Disclosures Requirements

Mandatory Disclosures Include:

- Carrying amounts and fair values of financial instruments.
- Fair value hierarchy levels (Level 1, 2, 3).
- Derivative instruments and hedging activities details.
- Credit risk concentration disclosures.
- CECL assumptions and sensitivities.

Checklist for Compliance:

- Are gross and net exposures disclosed (for derivatives)?
- Are risks and strategies behind hedging disclosed?
- Is the impact of credit losses disclosed in a clear manner?

• Example:

Footnotes describing methods used for fair value, carrying value vs. market value for bonds, qualitative discussion of credit loss drivers.

હેરુ	Quick	Table	Summary
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#	Key Area	Requirements
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6	Disclosures	Fair value, risk exposures, CECL, derivatives

Q Practical Tips for Good Practice

- Create a Financial Instrument Inventory: List all debt, equity, derivatives.
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Error	Example
Ignoring embedded derivatives	Not bifurcating derivatives in hybrid contracts
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© Conclusion



Financial instruments accounting under US GAAP emphasizes **fair value transparency**, **credit risk assessment**, and **comprehensive disclosure**. It requires **technical precision** in valuation, **rigorous internal controls** for derivative contracts, and **clear explanations** in financial reporting.

Missteps here could not only lead to **material misstatements** but also trigger **regulatory**



8. Liabilities, Provisions, and Contingencies (ASC 450) under US GAAP – Comprehensive Explanation

First: Understand ASC 450 — The Core Principle

A **liability** must be recognized when a **present obligation** exists due to a **past event**, and **payment is probable**, and the amount can be **reasonably estimated**.

ASC 450 governs the treatment of:

- Loss contingencies (lawsuits, warranties, guarantees)
- Gain contingencies (rare disclosure only)
- Provisions (similar to liabilities but often with more uncertainty)

Detailed Step-by-Step Compliance

C Recognition of Loss Contingencies

Requirement: Recognize a liability **only when both**:

- It is probable that a liability has been incurred, and
- The amount can be **reasonably estimated**.

Checklist for Compliance:

- Is the loss probable (i.e., likely to occur)? (>70% likelihood by practice)
- Can the amount or range of loss be estimated?
- Are legal opinions or internal assessments documented?

• Example:

Pending litigation where lawyers assess a 90% chance of losing and estimated damages between $2M-3M \rightarrow Recognize$ best estimate.

2 Measurement of Loss Contingencies



Requirement:

- If a single amount appears best estimate \rightarrow recognize that amount.
- If no amount is a better estimate than others → recognize **minimum amount** in the range and **disclose** the possibility of additional loss.

Checklist for Compliance:

- Has best estimate or minimum value been used appropriately?
- Are potential maximum exposures disclosed if material?

• Example:

If no clear best estimate, and possible loss range is \$100,000–\$300,000, recognize **\$100,000** and disclose possibility of more.

3 Disclosure of Loss Contingencies

Requirement: Even if no liability is recognized, disclosure is required if:

- Loss is **reasonably possible** (more than remote but less than probable), or
- An estimate cannot be made.

Checklist for Compliance:

- Is the nature of contingency described?
- Is an estimate of possible loss disclosed or a statement that it cannot be estimated?

• Example:

Ongoing patent infringement case assessed as reasonably possible \rightarrow disclose in notes with estimated exposure.

4 Treatment of Gain Contingencies

Requirement:

- **Do not recognize gain contingencies** until **realized** (i.e., the gain is virtually certain).
- **Disclose** only if probability is high and realization is approaching.



Checklist for Compliance:

- Are gain contingencies properly held off balance sheet?
- Are any disclosures made cautiously to avoid misleading users?

• Example:

Winning a lawsuit with pending appeal \rightarrow **do not record** a gain yet.

5 Common Examples of Contingent Liabilities

Example	Likely Treatment
Lawsuits	Recognize if probable and estimable; disclose otherwise
Product warranties	Recognize based on historical experience
Guarantees on third-party debt	Recognize when probable
Environmental cleanup obligations	Recognize if law requires cleanup and cost is estimable

Checklist for Compliance:

- Are product warranties estimated based on past experience?
- Are guarantees reviewed for contingent obligations?
- Are regulatory enforcement actions monitored?

© Subsequent Events Impact

Requirement:

- Reassess contingencies for **subsequent events** (after reporting date but before financial statement issuance).
- Update recognition or disclosure based on new information.

Checklist for Compliance:

- Has a major litigation settlement occurred after year-end?
- Have contingent liabilities been updated accordingly?



• Example:

If a lawsuit settled for \$5M after year-end but before issuance — adjust financials if conditions existed at reporting date.

🕸 Quick Table Summary

#	Key Area	Requirements
1	Loss Contingency Recognition	Probable + Reasonably estimable
2	Loss Measurement	Best estimate or minimum of range
3	Loss Disclosure	Reasonably possible losses disclosed
4	Gain Contingency	No recognition until virtually certain
5	Examples	Lawsuits, warranties, guarantees
6	Subsequent Events	Update estimates post-reporting date

Q Practical Tips for Good Practice

- Set up Legal Review Meetings each quarter with the legal team to track ongoing litigations.
- **Maintain a Contingency Log** listing each contingent item, probability assessment, and value.
- **Cross-check** pending litigation with insurance claims to evaluate recoveries separately.
- **Train internal teams** to identify contingent events early (e.g., contracts with indemnities).

(Common Errors to Avoid

Error	Example
Recognizing gain contingencies	Recording anticipated insurance
prematurely	recoveries early



Failing to accrue probable, estimable losses	Ignoring warranty claims in product- heavy industries
Misclassifying remote risks as disclosures	Disclosing highly improbable lawsuits unnecessarily
Not updating contingencies after major subsequent events	Final court decisions not reflected

© Conclusion

ASC 450 ensures that liabilities and risks are **properly reflected** in financial statements — protecting users from misleading information.

It requires **professional judgment**, **legal collaboration**, and **timely updates** for accurate reporting.

Handling contingencies carefully is essential to maintain **audit credibility**, **investor trust**, and **regulatory compliance**.



9. Income Taxes (ASC 740) under US GAAP – Comprehensive Explanation

First: Understand ASC 740 — The Core Principle

Income tax accounting aims to properly recognize:

- Current tax expense/benefit (based on taxable income)
- **Deferred tax assets/liabilities** (based on temporary differences between financial and tax bases)

It also requires identifying **uncertain tax positions** and applying **valuation allowances** when needed.

Detailed Step-by-Step Compliance

Current Tax Calculation

Requirement:

- Calculate income taxes **payable/refundable** for the current year based on **taxable income** determined per the tax laws.
- Checklist for Compliance:
 - Is taxable income correctly calculated based on IRS/local regulations?
 - Are current tax liabilities/receivables properly recorded?
 - Are credits and carryforwards (e.g., R&D credits, minimum tax credits) applied properly?

• Example:

Taxable profit = \$500,000, Corporate Tax Rate = $21\% \rightarrow$ **\$105,000** tax expense.

2 Deferred Tax Assets (DTA) and Deferred Tax Liabilities (DTL)

Requirement:



• Arise due to **temporary differences** between financial reporting and tax bases of assets and liabilities.

Checklist for Compliance:

- Have all temporary differences been identified?
- Are tax rates applied based on expected future periods when reversal occurs?
- Are DTAs and DTLs classified as **noncurrent** on the balance sheet?

• Example:

Depreciation for tax faster than book depreciation \rightarrow **DTL** created now, reversing over future years.

1 Common Examples of Temporary Differences

Temporary Difference	Result
Accelerated tax depreciation	DTL
Warranty expense accrued for book, deductible when paid	DTA
Allowance for doubtful accounts	DTA
Prepaid expenses deductible when paid	DTL

Valuation Allowance for Deferred Tax Assets

Requirement:

 A valuation allowance must be recorded against DTAs if it is more likely than not (>50%) that some or all of the DTA will not be realized.

Checklist for Compliance:

- Are cumulative losses an indicator for valuation allowance?
- Is positive evidence (e.g., projected future taxable income, tax planning strategies) evaluated?
- Is the valuation allowance reassessed annually?



• Example:

A startup with \$2M DTA but recurring losses \rightarrow full or partial **valuation allowance** likely needed.

5 Uncertain Tax Positions (FIN 48 / ASC 740-10)

Requirement:

• Must recognize a tax benefit **only if** it is **more likely than not** to be sustained upon examination.

W Two-Step Model:

- Recognition Step: Is the tax position more-likely-than-not to be sustained?
- Measurement Step: Measure the largest amount of benefit likely to be realized.

Checklist for Compliance:

- Has each material tax position been reviewed?
- Are reserves recorded for uncertain positions?
- Is a roll-forward of unrecognized tax benefits maintained?

• Example:

Claimed an aggressive deduction — assess if it is defensible. If not likely sustained, **set up a tax reserve**.

C Presentation in Financial Statements

Requirement:

- Current tax assets/liabilities presented separately from Deferred tax assets/liabilities.
- Deferred taxes always classified as **noncurrent** (even if reversing within 12 months).

Checklist for Compliance:

- Are net current taxes presented separately from deferreds?
- Are DTAs and DTLs offset only if specific conditions (same tax jurisdiction, legal right) are met?



• Example:

Do not net a DTA in India with a DTL in USA. Different jurisdictions.

T Required Disclosures

Mandatory Disclosures Include:

- Components of income tax expense (current and deferred separately).
- Reconciliation between effective tax rate and statutory tax rate.
- Components of DTAs and DTLs.
- Unrecognized tax benefits (roll-forward).
- Valuation allowance details.

Checklist for Compliance:

- Is a tax rate reconciliation disclosed (typically in % terms)?
- Are significant temporary differences described in notes?
- Are uncertain tax positions summarized annually?

• Example:

Effective Tax Rate = 17% vs Statutory $21\% \rightarrow$ reconcile items like tax credits, foreign income, permanent differences.

🕸 Quick Table Summary

#	Key Area	Requirements
1	Current Tax Expense	Based on taxable income
2	Deferred Tax Recognition	Temporary differences
3	Valuation Allowance	For unrealizable DTAs
4	Uncertain Tax Positions	More-likely-than-not recognition test
5	Presentation	Current vs. Deferred, Noncurrent classification
6	Disclosures	Rate reconciliation, DTA/DTL details, tax reserves



Q Practical Tips for Good Practice

- Coordinate tax and accounting teams early to identify all book-tax differences.
- Maintain a Deferred Tax Asset/Liability Schedule with detail by account.
- **Document all valuation allowance analyses** thoroughly auditors scrutinize this area heavily.
- Set quarterly review processes to monitor uncertain tax positions and changes in tax law.

(Common Errors to Avoid

Error Example

Missing valuation allowance Overstating DTAs for companies with cumulative losses

Improper DTA/DTL offsetting Netting assets/liabilities across jurisdictions

Ignoring uncertain positions No reserves for aggressive deductions taken

Wrong classification Deferred tax shown as current asset/liability

© Conclusion

ASC 740 demands **precision**, **judgment**, and **full documentation** because tax-related accounting can significantly affect:

- Net Income,
- Equity,
- Cash Flows, and
- Audit Opinions.

Income tax disclosures provide critical insights into a company's tax strategies, risks, and future obligations.

🔔 Tip:

Tax issues are often **material audit points** — so early identification and proactive management are crucial.





□ 10. Consolidations (ASC 810) under US GAAP – Comprehensive Explanation

First: Understand ASC 810 — The Core Principle

Consolidated financial statements present the **parent** and its **subsidiaries** as a **single economic entity**.

Consolidation is required when the parent **controls** the subsidiary, either through **majority voting interest** or **special control mechanisms** like **Variable Interest Entities (VIEs)**.

Detailed Step-by-Step Compliance

CASSESSING Control – When to Consolidate

Requirement:

- A parent must consolidate a subsidiary if:
 - o It directly or indirectly owns more than 50% of voting shares, or
 - o It has **control** through contractual arrangements (VIE model).

Checklist for Compliance:

- Does the parent own >50% voting rights?
- Are there agreements that provide control without majority ownership (VIE indicators)?
- Is the entity a legal subsidiary or a VIE requiring consolidation?

• Example:

Owning 60% of an operating company = consolidate.

Controlling a leasing company through guaranteed returns without owning it = VIE consolidation.

2 Variable Interest Entities (VIEs)



Requirement:

- An entity may be a **VIE** if:
 - Equity investors lack power, or
 - $_{\circ}$ Equity at risk is insufficient (<10% of total capital), or
 - Equity investors don't control major decisions.

Checklist for VIE Compliance:

- Is the entity funded mainly by debt-like instruments?
- Does the sponsor guarantee returns or absorb losses disproportionately?
- If yes, consolidate if you are the **primary beneficiary** (i.e., have power + significant economic exposure).

• Example:

Sponsor sets up a special purpose entity (SPE) to hold receivables and guarantees returns to outside investors \rightarrow likely a VIE.

3 Consolidation Procedures

Requirement: In preparing consolidated financial statements:

- Combine like assets, liabilities, equity, income, and expenses.
- Eliminate intercompany transactions and balances in full.
- Recognize noncontrolling interests separately in equity.

Checklist for Compliance:

- Are all intercompany receivables/payables eliminated?
- Are intercompany sales/profit in inventory eliminated?
- Is noncontrolling interest presented correctly in consolidated equity and income?

• Example:

Parent sells \$1M goods to subsidiary — eliminate both sales revenue and cost of goods sold for consolidation.

4 Noncontrolling Interests (NCI)



Requirement:

- Noncontrolling interest represents the portion of equity in a subsidiary not attributable to the parent.
- Present NCI within equity, not as a liability.

Checklist for Compliance:

- Is NCI clearly presented separately within equity on the balance sheet?
- Is NCI's share of subsidiary net income presented on the income statement?

• Example:

Parent owns 80% of subsidiary \rightarrow remaining 20% shown as NCI in consolidated balance sheet and income statement.

5 Changes in Ownership Interest Without Loss of Control

Requirement:

• If parent changes ownership % (buys/sells stake) but **retains control**, treat as an **equity transaction**, not gain/loss recognition.

Checklist for Compliance:

- Is change recorded directly in equity?
- No gain or loss recognized in income statement?

• Example:

Selling 10% of a subsidiary but retaining $70\% \rightarrow$ record transaction directly in consolidated equity.

C Loss of Control Over a Subsidiary

Requirement:

- When control is lost:
 - Derecognize all assets, liabilities, and NCI.
 - Recognize gain or loss on disposal in income statement.
 - Recognize any retained investment at fair value.



Checklist for Compliance:

- Are derecognition entries correct?
- Is remaining interest remeasured at fair value?

• Example:

Selling entire 60% stake in a subsidiary — recognize gain/loss and record any retained minority interest at fair value.

SQuick Table Summary

#	Key Area	Requirements
1	Control Assessment	Voting interest >50% or VIE primary beneficiary
2	VIE Analysis	Assess power and risks/benefits
3	Consolidation Procedure	Eliminate intercompany balances and transactions
4	Noncontrolling Interest	Present separately within equity
5	Change without Loss of Control	Record in equity, no P&L impact
6	Loss of Control	Derecognize and remeasure remaining interest

Q Practical Tips for Good Practice

- Prepare a Group Structure Chart and update it regularly.
- **Perform VIE Analysis annually** especially for joint ventures, partnerships, structured entities.
- Track ownership changes closely minor equity changes can trigger different accounting.
- Automate elimination entries using consolidation software if managing multiple subsidiaries.

Common Errors to Avoid



Error	Example
Failing to consolidate a VIE	Ignoring control via contracts and guarantees
Incomplete elimination	Leaving intercompany interest income and expense
Misclassifying NCI	Presenting NCI outside equity
Incorrect treatment of partial disposal	Recognizing gain/loss when only equity transaction occurred

© Conclusion

Proper consolidation under ASC 810 is crucial for **presenting a true and fair view** of a group's financial position and results.

Failure to consolidate properly can result in **material misstatements**, **audit qualifications**, and **regulatory penalties** — especially for public companies.

👃 Tip:

Always involve legal and finance teams when setting up new entities, SPEs, partnerships, or JV structures to **assess control and consolidation requirements early**.



□ 11. Share-Based Compensation (ASC 718) under US GAAP – Comprehensive Explanation

First: Understand ASC 718 — The Core Principle

Share-based payment arrangements, including **stock options**, **restricted stock units (RSUs)**, **performance shares**, and similar awards, must be **measured at grant-date fair value** and **recognized as an expense** over the vesting period.

ASC 718 governs both equity-classified and liability-classified awards.

Detailed Step-by-Step Compliance

C Scope and Types of Share-Based Awards

Covered Transactions:

- Employee stock options (ESOPs)
- RSUs (Restricted Stock Units)
- Performance-based stock awards
- Share Appreciation Rights (SARs)
- Stock purchased at discount under employee share purchase plans (ESPPs)

Checklist for Compliance:

- Are all share-based payment arrangements identified?
- Is classification between equity-settled vs. cash-settled properly determined?

• Example:

Options settled by issuing shares \rightarrow Equity-classified. Cash-settled SARs \rightarrow Liability-classified.

2 Grant-Date Fair Value Measurement

Requirement:



- Measure share-based awards at fair value on the grant date using:
 - **Option Pricing Models** (e.g., Black-Scholes for options)
 - **Market price** for simple RSUs.

Key Assumptions Needed:

- Stock price at grant date
- Exercise price (for options)
- Expected life
- Expected volatility
- Risk-free interest rate
- Expected dividends

Checklist for Compliance:

- Has a reasonable valuation methodology been applied?
- Are assumptions well-supported and documented?

• Example:

Black-Scholes Model used to value employee stock options at grant.

1 Expense Recognition Over Vesting Period

Requirement:

• Recognize the total grant-date fair value as compensation expense over the vesting period (service period).

Checklist for Compliance:

- Is expense recognized **straight-line** unless graded vesting requires accelerated method?
- Are forfeitures estimated (or actual forfeitures accounted if elected)?
- Are performance conditions evaluated continuously?

• Example:

An RSU grant vests over 4 years — recognize 25% expense annually.



Performance-Based and Market-Based Awards

Requirement:

- **Performance Conditions** (e.g., achieving revenue target) → Recognize expense **only if probable** that the condition will be met.
- Market Conditions (e.g., stock price targets) → Considered in fair value at grant; expense even if not ultimately achieved.

Checklist for Compliance:

- Are performance metrics assessed quarterly?
- Are market conditions embedded in initial fair value calculation?

• Example:

Stock awards vesting if stock price exceeds \$100 \rightarrow fair value at grant captures the difficulty; no need to reverse if missed.

5 Modification of Awards

Requirement:

- If terms of award change (e.g., repricing options, extending expiry), treat as a **modification**.
- Measure incremental fair value and recognize additional expense.

Checklist for Compliance:

- Are all modifications approved/documented properly?
- Is incremental cost measured and expensed over new vesting period?

• Example:

Repricing underwater options — calculate incremental value and account for extra compensation cost.

C Liability-Classified Awards

Requirement:

• Cash-settled awards must be **remeasured at fair value** at each reporting date until settlement.



Checklist for Compliance:

- Are fair values updated every quarter?
- Is settlement method determined clearly (cash vs stock)?

• Example:

Stock appreciation rights payable in cash \rightarrow mark-to-market every quarter.

Z Required Disclosures for Share-Based Compensation

Mandatory Disclosures Include:

- General description of share-based plans.
- Number of options/RSUs granted, vested, forfeited, expired.
- Assumptions used in valuation models.
- Total share-based compensation cost recognized.
- Unrecognized compensation cost and expected amortization period.

Checklist for Compliance:

- Are award types and terms clearly described?
- Is valuation methodology for options disclosed?
- Are future unrecognized costs reported?

Example:

Disclosure of unrecognized stock compensation expense of \$5M to be amortized over next 3 years.

🔆 Quick Table Summary

#	Key Area	Requirements
1	Scope	Stock options, RSUs, SARs, ESPPs
2	Measurement	Fair value at grant date
3	Recognition	Over vesting period; forfeiture policy applied



4	Performance/Market	Different recognition rules
	Conditions	
5	Modifications	Measure incremental value
6	Liability-Classified Awards	Remeasure at fair value each period
7	Disclosures	Plan terms, assumptions,
		recognized/unrecognized costs

Q Practical Tips for Good Practice

- Centralize all grant documentation Board approvals, employee grant letters, etc.
- Align HR, legal, and finance teams each impacts grant data.
- Use external valuation experts when dealing with complex performance or market condition awards.
- **Periodically reconcile share-based expense** to HR stock ledger (granted, vested, forfeited).

(Common Errors to Avoid

Error	Example
Wrong valuation date	Using approval date instead of grant date
Incorrect forfeiture estimates	Failing to adjust expense based on actual forfeitures
Missing incremental expense on modifications	Ignoring accounting when repricing options
Underdisclosure	Not providing assumptions or unrecognized compensation cost

© Conclusion

ASC 718 ensures that the **economic cost of employee and non-employee incentives** is properly reflected in financial statements.



It demands careful valuation, accurate tracking of vesting, continuous assessment of conditions, and robust disclosure.

👃 Tip:

Even **private companies** offering equity compensation (e.g., startups) must comply — especially if preparing GAAP-compliant financials for funding or IPO readiness.



12. Foreign Currency (ASC 830) under US GAAP – Comprehensive Explanation

First: Understand ASC 830 — The Core Principle

Foreign currency matters in accounting deal with two separate but related processes:

- **Remeasurement**: Converting foreign transactions into the entity's **functional currency**.
- **Translation**: Converting financial statements of a **foreign operation** into the **reporting currency** (usually USD).

The goal is to correctly reflect currency impacts on:

- Income,
- Assets/Liabilities,
- Equity.

Detailed Step-by-Step Compliance

Determine the Functional Currency

Requirement:

• The **functional currency** is the currency of the primary economic environment where the entity operates.

Checklist for Compliance:

- Where does the entity generate and spend cash?
- What currency influences sales prices, costs, and financing activities?
- Is the local currency used, or is another currency more dominant?

Example:

A Mexican subsidiary selling only in US dollars \rightarrow likely **USD** functional currency.

2 Foreign Currency Transactions (Remeasurement)



Requirement:

- Transactions denominated in a foreign currency (e.g., sales, purchases, loans) must be **remeasured** into the functional currency:
 - At spot exchange rate on transaction date for initial recognition.
 - At balance sheet date rate for monetary items.
 - **At historical rate** for nonmonetary items.

Checklist for Compliance:

- Are monetary items (cash, receivables, payables) updated to spot rate at reporting date?
- Are nonmonetary assets/liabilities (inventory, fixed assets) kept at historical rate?

Example:

A loan payable in Euros by a US company — remeasured at year-end exchange rate.

1 Foreign Currency Translation (Financial Statements of Foreign Operations)

Requirement:

- If the functional currency of the foreign operation ≠ reporting currency (e.g., USD), financial statements must be **translated**:
 - Assets and liabilities → at current exchange rate at balance sheet date.
 - \circ Equity items \rightarrow at historical exchange rate.
 - Income and expenses \rightarrow at average exchange rate for the period (or approximate rate).

Checklist for Compliance:

- Is translation methodology consistent?
- Is the cumulative translation adjustment (CTA) recognized in Other Comprehensive Income (OCI)?

• Example:

Indian subsidiary's financials (functional currency INR) \rightarrow translate to USD for parent consolidation.



Accounting for Translation Adjustments

Requirement:

• All translation gains/losses are recorded in **Other Comprehensive Income** (**OCI**) until the foreign operation is sold.

Checklist for Compliance:

- Is the CTA shown in the equity section separately?
- Are translation adjustments reclassified into P&L upon disposal of the foreign operation?

Example:

Cumulative \$1M translation loss recognized in OCI; upon selling the subsidiary, the \$1M is "recycled" into net income.

5 Accounting for Remeasurement Gains or Losses

Requirement:

• **Remeasurement** gains/losses affect current-period income statement immediately.

Checklist for Compliance:

- Are gains/losses from remeasurement posted to Other Income/Expense?
- Are impacts on earnings volatility assessed and disclosed if material?

• Example:

FX gain on remeasuring a foreign currency payable — record in current year's income.

6 Special Cases

Hyperinflationary Economies:

If the foreign entity operates in a hyperinflationary economy (inflation > 100% over 3 years), remeasure its financials into the reporting currency using current rates, not normal translation.



Checklist for Compliance:

- Are hyperinflation indicators monitored (especially for subsidiaries in Venezuela, Argentina, etc.)?
- Has the remeasurement approach been shifted appropriately if needed?

🕸 Quick Table Summary

Process	Application	Where the Gain/Loss Goes
Remeasurement	Foreign transactions into functional currency	Income Statement (P&L)
Translation	Foreign operations into reporting currency	OCI (Equity)

Q Practical Tips for Good Practice

- Maintain separate ledgers for local and reporting currency where possible.
- Automate FX rate updates using reputable sources for consistency.
- Segregate remeasurement gains/losses in GL accounts for clean reporting.
- Train local finance teams on distinguishing monetary vs nonmonetary items.

(Common Errors to Avoid

Error	Example
Wrongly treating nonmonetary items	Remeasuring inventory at year-end rate instead of historical
Mixing remeasurement with translation	Posting translation adjustment to P&L instead of OCI
Inconsistent FX rates	Using different average rates for revenue and expenses



Missing reclassification on	Forgetting to recycle CTA to P&L when selling a
disposal	subsidiary

© Conclusion

Correctly applying ASC 830 ensures that foreign currency effects are properly **isolated**, **transparent**, and **fairly presented** in financial statements.

It protects stakeholders from misreading operating results distorted by exchange rate volatility.



Companies with multiple global subsidiaries **must set robust internal policies** for FX accounting early to avoid year-end surprises and audit challenges.



□ 13. Business Combinations (ASC 805) under US GAAP – Comprehensive Explanation

First: Understand ASC 805 — The Core Principle

Business combinations must be accounted for using the Acquisition Method.

This method requires identifying the **acquirer**, measuring the **fair value** of consideration transferred, recognizing and measuring **acquired assets and liabilities at fair value**, and recognizing **goodwill** or a **gain from bargain purchase**.

Detailed Step-by-Step Compliance

D Identify the Acquirer

Requirement:

• The acquirer is the entity that obtains control of the acquiree.

Checklist for Compliance:

- Who holds majority voting rights post-transaction?
- Who appoints a majority of the board members?
- Who initiated the combination?
- Who dominates the management team?

• Example:

Company A acquires 80% of Company B \rightarrow Company A is the **acquirer**.

2 Determine the Acquisition Date

Requirement:

- The acquisition date is when the **acquirer gains control** of the acquiree usually the **closing date**.
- Checklist for Compliance:



- Is the legal closing date the same as the accounting acquisition date?
- Are control conditions met (e.g., cash transferred, shares issued)?

• Example:

Agreement signed on March 1, 2025; closing completed on April 30, $2025 \rightarrow \text{April 30}$, 2025 is the acquisition date.

3 Measure the Consideration Transferred

Requirement:

- Measure at **fair value** as of the acquisition date.
- Consider all forms of consideration:
 - o Cash
 - Equity shares issued
 - Contingent consideration (earnouts)
 - Liabilities assumed

Checklist for Compliance:

- Has contingent consideration been fair valued?
- Are any payments to sellers properly classified (compensation vs purchase)?

• Example:

If part of consideration depends on future profits (earnout), estimate its fair value at acquisition and record.

Recognize and Measure Identifiable Assets and Liabilities

Requirement:

- Recognize separately all identifiable:
 - Assets acquired
 - Liabilities assumed
- At fair value at acquisition date.



Checklist for Compliance:

- Have intangible assets (e.g., customer relationships, trademarks) been separately identified and valued?
- Are contingent liabilities (e.g., lawsuits) recognized if fair value can be reliably measured?

• Example:

Customer contracts not recorded by the seller \rightarrow must be valued and recorded by the acquirer.

1 Recognize Goodwill or Bargain Purchase Gain

Requirement:

- **Goodwill** = (Consideration transferred + NCI + Fair Value of any previously held interest) Net identifiable assets acquired.
- If the net assets acquired exceed the consideration transferred → recognize **bargain purchase gain** in P&L immediately.

Checklist for Compliance:

- Is goodwill properly computed and recorded?
- Has bargain purchase gain been substantiated (rare, usually audited intensively)?

• Example:

Paid \$8M for net identifiable assets worth $10M \rightarrow record 2M$ bargain purchase gain in income statement.

C Noncontrolling Interests (NCI) Measurement

Requirement:

- NCI can be measured at:
 - o Fair value, or
 - **Proportionate share** of the acquiree's identifiable net assets.

Checklist for Compliance:



- Is the selected method disclosed and consistently applied?
- Are minority interests appropriately presented in consolidated equity?

• Example:

If 80% acquired, 20% NCI measured at either fair value or net assets proportionate share.

Z Contingent Consideration (Earnouts)

Requirement:

- Recognize contingent payments at fair value on acquisition date.
- Adjustments post-acquisition:
 - Generally through **P&L**, unless it's equity-classified.

Checklist for Compliance:

• Are subsequent changes in contingent consideration properly reflected?

• Example:

An earnout liability based on performance targets must be remeasured at each reporting date if liability-classified.

8 Measurement Period Adjustments

Requirement:

• If initial accounting is incomplete, acquirer has up to **one year** to adjust provisional amounts.

Checklist for Compliance:

- Are measurement period adjustments recognized **retrospectively** as if recorded on acquisition date?
- Are disclosures made about provisional amounts and adjustments?

Example:

After 6 months, acquirer finalizes valuation of acquired patents — adjust assets and goodwill retrospectively.



🔆 Quick Table Summary

#	Key Area	Requirements
1	Identify Acquirer	Who gains control
2	Acquisition Date	Date control obtained
3	Measure Consideration	Fair value including contingent consideration
4	Recognize Assets/Liabilities	Fair value measurement
5	Goodwill/Bargain Purchase	Residual after fair value allocation
6	Noncontrolling Interests	Fair value or proportionate method
7	Contingent Consideration	Initial recognition and later adjustments
8	Measurement Period	1-year retrospective adjustment window

Q Practical Tips for Good Practice

- Engage third-party valuation experts early for complex fair value assessments (especially for intangibles and earnouts).
- Prepare a detailed Purchase Price Allocation (PPA) schedule.
- Keep separate files for provisional accounting entries vs measurement period adjustments.
- Disclose assumptions (e.g., discount rates, future cash flows) transparently.

(Common Errors to Avoid

Error	Example
Missing intangible assets	Not separately valuing customer lists, tradenames
Incorrect goodwill calculation	Forgetting to include contingent consideration in total consideration
Ignoring contingent liabilities	Failing to recognize probable litigation exposures at fair value
Delayed measurement adjustments	Not updating financials retrospectively within the 1- year window

© Conclusion

ASC 805 ensures that **business combinations** are accounted for with a **fair value-based**, **transparent approach**, allowing investors to understand:

- What was acquired,
- What was paid,
- What risks and synergies exist.

👃 Tip:

Acquisitions typically undergo **heightened audit and SEC review** — so **strong documentation**, **fair value support**, and **clear disclosures** are critical.



14. Internal Controls and SOX Compliance under USGAAP – Comprehensive Explanation

First: Understand the Core Principle

Companies, especially **public companies**, must establish, maintain, and evaluate **Internal Control over Financial Reporting (ICFR)**.

These controls are meant to **reasonably assure** that:

- Transactions are properly authorized,
- Assets are safeguarded,
- Financial reporting is reliable, and
- Financial statements are prepared in accordance with US GAAP.

Sarbanes-Oxley Act (SOX) mainly governs this through:

- Section 302 Management Certification.
- Section 404 Management and Auditor Assessment of ICFR.

Detailed Step-by-Step Compliance

Understanding Internal Control over Financial Reporting (ICFR)

Requirement:

ICFR is designed to provide reasonable assurance regarding the reliability of financial reporting.

Checklist for ICFR Compliance:

- Are entity-level controls in place (e.g., tone at the top, ethics policies)?
- Are transaction-level controls in place (e.g., approval of journal entries)?
- Is segregation of duties maintained?
- Are automated system controls tested and working?



• Example:

Controls ensuring all revenue transactions are properly recorded and unauthorized journal entries are prevented.

2 Management Responsibility under SOX 302

Requirement:

- CEO and CFO must certify quarterly and annually that:
 - Financial statements are fairly presented.
 - They have designed, or caused to be designed, disclosure controls and procedures.
 - They have evaluated the effectiveness of controls within 90 days prior to the report.

Checklist for Compliance:

- Are CEO/CFO certifications documented and updated each quarter?
- Are disclosure controls tested and documented separately from operational controls?

• Example:

CEO/CFO certify through Forms 10-Q and 10-K filings to the SEC.

I Management Assessment of ICFR (SOX 404a)

Requirement:

• Management must **annually** assess and report the **effectiveness of internal controls**.

Checklist for Compliance:

- Has management documented key controls?
- Has a risk assessment been performed to identify significant accounts and risks?
- Have controls been tested for design and operating effectiveness?



• Example:

Company maintains detailed Risk Control Matrices (RCMs) linking risks, controls, and test plans.

4 Auditor Attestation of ICFR (SOX 404b)

Requirement:

- For accelerated filers and large accelerated filers, external auditors must independently:
 - Test ICFR.
 - Issue an opinion on the effectiveness of ICFR.

Checklist for Compliance:

- Has the auditor selected entity-level and transaction-level controls to test?
- Have identified deficiencies been evaluated for material weaknesses?

• Example:

Auditor performs walkthroughs, tests samples, and issues separate ICFR opinion along with audit report.

5 Deficiencies, Significant Deficiencies, and Material Weaknesses

Definitions:

- **Control Deficiency:** Minor problem; no material impact.
- Significant Deficiency: Important but not material individually or combined.
- **Material Weakness:** Reasonable possibility that material misstatement will not be prevented or detected.

Checklist for Compliance:

- Are deficiencies categorized appropriately?
- Are material weaknesses disclosed in 10-K filings?

Example:

Failure to reconcile bank accounts monthly \rightarrow Significant Deficiency. Failure to detect revenue cut-off errors \rightarrow Material Weakness.



C Designing a Strong SOX Program

Key Components:

- Control Environment: Ethical culture, Code of Conduct.
- **Risk Assessment**: Identify risks to reliable financial reporting.
- **Control Activities**: Specific policies and procedures.
- Information & Communication: Proper communication of controls and incidents.
- Monitoring Activities: Regular evaluations and updates to control systems.

Checklist for Compliance:

- Are roles and responsibilities assigned clearly?
- Are periodic evaluations conducted?
- Is SOX documentation (RCMs, flowcharts, test plans) maintained?

ઈંડે	Quick	Table	Summary
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#	Key Area	Requirements
1	SOX 302 Certification	CEO/CFO responsibility for financial statements and disclosure controls
2	SOX 404a	Management evaluation of ICFR
3	SOX 404b	Auditor evaluation of ICFR (for larger companies)
4	Deficiency Classification	Control deficiency vs significant vs material weakness
5	SOX Program Structure	COSO-based components implemented

Practical Tips for Good Practice

• Use the COSO 2013 Framework for designing and evaluating ICFR.



- Maintain a central repository of risk and control matrices (RCMs).
- **Use technology** (e.g., GRC tools like Workiva, AuditBoard) for SOX testing and documentation.
- Hold quarterly SOX meetings involving finance, compliance, internal audit, and external audit teams.
- Perform pre-close control testing each quarter before earnings release.

Error	Example
Not updating controls for changes	Implementing a new ERP system but not redesigning controls
Weak segregation of duties	Same person initiating, approving, and recording payments
Incomplete risk assessment	Ignoring IT General Controls (ITGCs) for critical systems
Ignoring small deficiencies	Minor control failures accumulating into a significant deficiency or material weakness

Common Errors to Avoid

© Conclusion

Internal Controls over Financial Reporting (ICFR) and **SOX compliance** are critical for:

- Protecting financial reporting integrity,
- Reducing fraud risk,
- Enhancing investor confidence.

Companies must document, test, monitor, and improve controls proactively to avoid:

- Adverse audit opinions,
- SEC sanctions,
- Reputational damage.



👃 Tip:

Even private companies planning IPOs or private equity exits should **start SOXreadiness early** to avoid last-minute chaos.

Weighted: Quick Recap of Sections Completed:

Section	Status
1. General Accounting Principles	~
2. Presentation and Disclosure	~
3. Revenue Recognition (ASC 606)	~
4. Inventory (ASC 330)	~
5. PPE (ASC 360)	~
6. Leases (ASC 842)	~
7. Financial Instruments (ASC 825/815)	~
8. Liabilities and Contingencies (ASC 450)	~
9. Income Taxes (ASC 740)	~
10. Consolidations (ASC 810)	~
11. Share-Based Compensation (ASC 718)	~
12. Foreign Currency (ASC 830)	~
13. Business Combinations (ASC 805)	~
14. Internal Controls and SOX	~