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**LEVEL: 400**

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**ASSIGNMENT: Summarise, in not more than 400 words, the note on Segment Reporting. Format**

As companies diversify internationally or in the lines of business in which they operate, the usefulness of consolidated financial statement diminishes. There are different risks and growth potential associated with different parts of the world, just as there are different risks and opportunities associated with different lines of business. The aggregation of all of a company’s revenue, expenses, assets and liabilities into consolidated total masks these difference.

**OPERATING SEGMENTS-THE MANAGEMENT APPROCH**

The management approach to determining segments is based on the way that management disaggregates the enterprise for making operating decisions. These disaggregate components are referred to as operating segments, which should be evident from the enterprise’s organisation structure. An operating segment is a component of an enterprise if;

* It engages in business activities from which it earns revenues and incurs expenses.
* It is operating results are regularly reviewed by the chief operating decision maker to assess performance and make resource allocation decisions.
* Discrete financial information is available for it.

After determining whether any segments are to be aggregated, management next must determine which of its operating segments are significant enough to justify separate disclosure. An operating segment is considered significant if it meets any one of the following tests;

* **REVENUE TEST:** Segment revenues, both external and intersegment, are 10 percent or more of the combined revenue, internal and external, of all reporting segments.
* **PROFIT OR LOSS TEST:** Segment profit or loss is 10 percent or more of the higher (in absolute terms) of the combined reported profit of all profitable segments or the combined reported loss of all segments incurring a loss.
* **ASSET TEST:** Segment assets are 10 percent or more of the combined assets of all operating segments.
* **OVERALL SIZE TEST:** If the combined sales to unaffiliated (external) customers of segments determined to be significant are less than 75 percent of the total company sales, made to outsiders, additional segments must be disclosed separately even though they fail to meet one of the quantitative thresholds, until the 75% mark is reached.

**WHAT HAS TO BE REPORTED?**

The purpose of disclosing segmental information is to provide additional information to the users of the financial statements so that they will be able to evaluate the nature of the entity’s business activities.