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ACC 406

INTERNATIONAL ACCOUNTING

**ACCOUNTING FOR CHANGING PRICE**

Conventional accounting entails the combination of attributes being reflected in the asset section of the statement of financial position. This entails that account receivables and documented in the net amount expected to be received in the future; short-term investments are documented at either their cost or their current market value; inventory is to be carried at the lower cost or it's market value; and the property, plants and equipment are reported at the cost less accumulated depreciation.

Reporting assets on the Statement of Financial position at their historical cost during a period of changes in price can make the information in the Statement of financial position irrelevant.

Inflation is the general increase in the price lovel and decrease in purchasing value of money. Economists often measure inflation by determining the current price of a crate of goods or cost of services in a period compared to the same goods and/or services at an earlier time.

**Impact of Inflation on Financial Statements**

1. An understatement of assets and overstatement of income will differ across companies due to the different rate of inflation employed by each company and this can lead to misinterpretation of financial information.

2. It can cause a negative impact on the company's debt, the assets being understated reduces the collateral of the business.

3. It leads to overstated income which would lead to more taxable income for the government to charge and a rise in demand for dividend by the shareholders.

**Purchasing power gain and losses**

Possessing cash-in-in and receivables during inflations leads to purchasing power loss which having payables during this period leads to purchasing power gain. A net purchasing power gain will occur when an entity maintains monetary liabilities over monetary assets during inflation and vice-versa for net purchasing power liabilities

Methods of accounting for changing prices

Three main methods of asset valuation can be employed, namely:

1. Historical cost accounting

2. General purchasing power accounting

3. Current cost accounting method