NAME: NSIMBEHE SONIA JOSEPH

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ASSIGNMENT: SUMMARY OF NOTE ON SEGMENT REPORTING

The usefulness of consolidated financial statements began to diminish as companies diversified internationally or in the lines of business in which they operate. This brought about segment reporting as far back as 1960 where several groups began to request that consolidated amounts be disaggregated and disclosed on a segment basis in order to facilitate the analysis and evaluation of financial statements.

THE MANAGEMENT APPROACH

The management approach to determining segments is based on the way that management disaggregates the enterprise in order to make operating decisions. These disaggregated components are referred to as operating segments, which should be evident from the enterprise’s organization structure. An operating segment is a component of an enterprise if

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

After a company has identified its operating segments based on its internal reporting system, management must decide which of these segments should be reported separately. Then 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:

1. Revenue test

2. Profit or loss test.

3. Asset test

4. Overall size test.

All segments that are not separately reported and are not combined should be included in the segment reporting disclosures as an unallocated reconciliation item or in an “all other” category.

Where a segment was separately reported in the previous period, it should continue to be reported separately even if the thresholds are not met in the current period. Also, where a segment meets the 10% threshold in the current period it should be separately reported for both the current and the previous period even if it was not separately reported in the previous period, assuming that it is practicable to do so.