

- the IFRS model consolidated balance sheet, as presented by Deloitte Touche, puts an emphasis on liquidity.
4. Under IFRS, noncontrolling interests are usually presented as the last item in total equity.
  5. None of these statements would be considered false.

## Cases

### CASE 3-1 CONVENIENCE FOODS

Kellogg Company and Subsidiaries*		
Consolidated Balance Sheet		
(millions, except share data)	2010	2009
Current assets		
Cash and cash equivalents	\$ 444	\$ 334
Accounts receivable, net	1,190	1,093
Inventories	1,056	910
Other current assets	225	221
Total current assets	<u>\$ 2,915</u>	<u>\$ 2,558</u>
Property, net	3,128	3,010
Goodwill	3,628	3,643
Other intangibles, net	1,456	1,458
Other assets	720	531
Total assets	<u>\$11,847</u>	<u>\$11,200</u>
Current liabilities		
Current maturities of long-term debt	\$ 952	\$ 1
Notes payable	44	44
Accounts payable	1,149	1,077
Other current liabilities	1,039	1,166
Total current liabilities	<u>\$ 3,184</u>	<u>\$ 2,288</u>
Long-term debt	4,908	4,835
Deferred income taxes	697	425
Pension liability	265	430
Other liabilities	639	947
Commitments and contingencies		
Equity		
Common stock, \$.25 par value, 1,000,000,000 shares authorized. Issued: 419,272,027 shares in 2010 and 419,058,168 shares in 2009	105	105
Capital in excess of par value	495	472
Retained earnings	6,122	5,481
Treasury stock at cost: 53,667,635 shares in 2010 and 37,678,215 shares in 2009	(2,650)	(1,820)
Accumulated other comprehensive income (loss)	(1,914)	(1,966)
Total Kellogg Company equity	<u>\$ 2,158</u>	<u>\$ 2,272</u>
Noncontrolling interests	(4)	3
Total equity	<u>2,154</u>	<u>2,275</u>
Total liabilities and equity	<u>\$11,847</u>	<u>\$11,200</u>

\*"Kellogg Company, founded in 1906 and incorporated in Delaware in 1922, and its subsidiaries are engaged in the manufacture and marketing of ready-to-eat cereal and convenience foods." 10-K

Source: Kellogg Company and Subsidiaries 2010 10-K

(continued)



**(CASE 3-1 CONTINUED)**

**Kellogg Company and Subsidiaries**  
**Notes to Consolidated Financial Statements (In Part)**

**NOTE 1 ACCOUNTING POLICIES (In Part)*****Basis of presentation***

The consolidated financial statements include the accounts of Kellogg Company and its majority-owned subsidiaries (Kellogg or the Company). Intercompany balances and transactions are eliminated.

The Company's fiscal year normally ends on the Saturday closest to December 31 and as a result, a 53rd week is added approximately every sixth year. The Company's 2010 and 2009 fiscal years each contained 52 weeks and ended on January 1, 2011 and January 2, 2010, respectively. The Company's 2008 fiscal year ended on January 3, 2009, and included a 53rd week. While quarters normally consist of 13-week periods, the fourth quarter of fiscal 2008 included a 14th week.

***Use of estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods reported. Actual results could differ from those estimates.

***Cash and cash equivalents***

Highly liquid investments with remaining stated maturities of three months or less when purchased are considered cash equivalents and recorded at cost.

***Accounts receivable***

Accounts receivable consists principally of trade receivables, which are recorded at the invoiced amount, net of allowances for doubtful accounts and prompt payment discounts. Trade receivables do not bear interest. The allowance for doubtful accounts represents management's estimate of the amount of probable credit losses in existing accounts receivable, as determined from a review of past due balances and other specific account data. Account balances are written off against the allowance when management determines the receivable is uncollectible. The Company does not have off-balance sheet credit exposure related to its customers.

***Inventories***

Inventories are valued at the lower of cost or market. Cost is determined on an average cost basis.

***Property***

The Company's property consists mainly of plants and equipment used for manufacturing activities. These assets are recorded at cost and depreciated over estimated useful lives using straight-line methods for financial reporting and accelerated methods, where permitted, for tax reporting. Major property categories are depreciated over various periods as follows (in years): manufacturing machinery and equipment 5–20; office equipment 4–5; computer equipment and capitalized software 3–5; building components 15–30; building structures 50. Cost includes interest associated with significant capital projects.

Plant and equipment are reviewed for impairment when conditions indicate that the carrying value may not be recoverable. Such conditions include an extended period of idleness or a plan of disposal. Assets to be disposed of at a future date are depreciated over the remaining period of use. Assets to be sold are written down to realizable value at the time the assets are being actively marketed for sale and a sale is expected to occur within one year. As of year-end 2010 and 2009, the carrying value of assets held for sale was insignificant.

***Goodwill and other intangible assets***

Goodwill and indefinite-lived intangibles are not amortized, but are tested at least annually for impairment. An intangible asset with a finite life is amortized on a straight-line basis over the estimated useful life.



For the goodwill impairment test, the fair value of the reporting units are estimated based on market multiples. This approach employs market multiples based on earnings before interest, taxes, depreciation and amortization, earnings for companies that are comparable to the Company's reporting units and discounted cash flow. The assumptions used for the impairment test are consistent with those utilized by a market participant performing similar valuations for the Company's reporting units.

Similarly, impairment testing of other intangible assets requires a comparison of carrying value to fair value of that particular asset. Fair values of non-goodwill intangible assets are based primarily on projections of future cash flows to be generated from that asset. For instance, cash flows related to a particular trademark would be based on a projected royalty stream attributable to branded product sales, discounted at rates consistent with rates used by market participants.

These estimates are made using various inputs including historical data, current and anticipated market conditions, management plans, and market comparables.

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### *Research and development*

The costs of research and development (R&D) are expensed as incurred and are classified in SGA expense. R&D includes expenditures for new product and process innovation, as well as significant technological improvements to existing products and processes. The Company's R&D expenditures primarily consist of internal salaries, wages, consulting, and supplies attributable to time spent on R&D activities. Other costs include depreciation and maintenance of research facilities and equipment, including assets at manufacturing locations that are temporarily engaged in pilot plant activities.

### *Income taxes*

The Company recognizes uncertain tax positions based on a benefit recognition model. Provided that the tax position is deemed more likely than not of being sustained, the Company recognizes the largest amount of tax benefit that is greater than 50 percent likely of being ultimately realized upon settlement. The tax position is derecognized when it is no longer more likely than not of being sustained. The Company classifies income tax-related interest and penalties as interest expense and SGA expense, respectively, on the Consolidated Statement of Income. The current portion of the Company's unrecognized tax benefits is presented in the Consolidated Balance Sheet in other current assets and other current liabilities, and the amounts expected to be settled after one year are recorded in other assets and other liabilities.

### *Required*

- a. 1. The statement is entitled "Consolidated Balance Sheets." What does it mean to have a consolidated balance sheet?
2. For subsidiaries where control is present, does Kellogg have 100% ownership? Explain.
- b. 1. With this information, can the gross receivables be determined? Explain.
2. What is the estimated amount that will be collected on receivables outstanding at the end of 2010?
- c. 1. What is the total amount of inventory at the end of 2010?
2. What indicates that the inventory is stated on a conservative basis?
3. What is the trend in inventory balance? Comment.
- d. 1. What is the net property and equipment at the end of 2010?
2. What depreciation method is used for financial reporting purposes? Where permitted, what depreciation methods are used for tax reporting? Comment on why the difference in depreciation methods for financial reporting versus tax reporting.
3. What is the accumulated depreciation on land at the end of 2010?
- e. 1. Describe the treasury stock account.
2. What method is used to record treasury stock?
3. Why is treasury stock presented as a reduction in stockholders' equity?

(continued)

**(CASE 3-1 CONTINUED)**

- f. 1. What is the fiscal year?  
2. Comment on the difference in length of fiscal year.
- g. Comment on the use of estimates.
- h. Does it appear that cash and cash equivalents are presented conservatively?
- i. 1. Comment on the source of goodwill.  
2. How are goodwill and indefinite-lived intangibles handled for write-offs?
- j. When is research and development expensed?
- k. Why is a benefit recognition model used for computing income taxes?