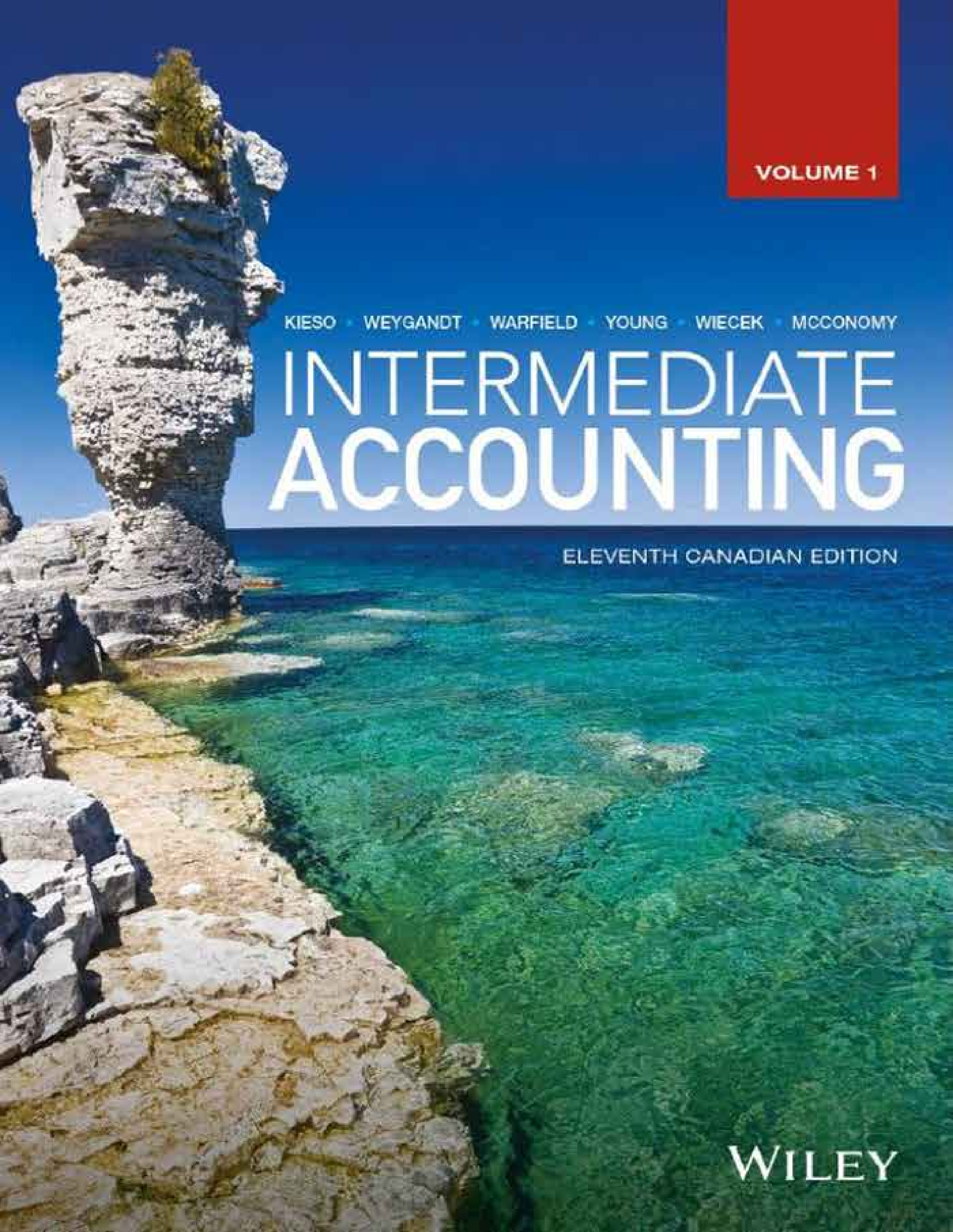


VOLUME 1

KIESO · WEYGANDT · WARFIELD · YOUNG · WIECEK · MCCONOMY

INTERMEDIATE ACCOUNTING

ELEVENTH CANADIAN EDITION

WILEY

Coverage of the CPA Competency Map Knowledge Supplement—The following table maps the knowledge reference list from the CPA Competency Map Knowledge Supplement to *Intermediate Accounting, Eleventh Canadian Edition* (Volumes 1 and 2). The textbook in its entirety covers the knowledge component of the competencies as noted below.

SECTION 1: FINANCIAL REPORTING

Introduction to Accounting	
	Chapters
• Objectives and fundamental accounting concepts and principles (qualitative characteristics of accounting information, basic elements)	1, 2
• Ethical professional judgement	2 and all chapters
• Objectives of financial reporting	1, 2
• Methods of measurement	2, 3
• Difference between accrual accounting and cash accounting	3, 4A
• Framework of standard setting (IFRS and ASPE)	1, 2
• Financial statement users and their broad needs, standard setting, and requirement for accountability	1, 2
• Accounting information systems	3
• The role of information technology in the reporting of information, including real-time access, remote access to information, dashboard, spreadsheet, report generator, and XBRL (eXtensible Business Reporting Language)	3
• Emerging trends in accounting standards and recent updates	All chapters
• Legislation that has an impact on accounting (Sarbanes-Oxley Act, Bill 198)	1
Financial Statements—Process, Design, and Preparation	
• The accounting cycle	3
• Internal control and cash (bank reconciliation, control over cash receipts and disbursements)	7, 7A
• Interim reporting	23
• Reportable segments	23
• Financial statements in accordance with applicable standards	All chapters
• Routine disclosure requirements (notes to financial statements)	All chapters
• Complex disclosure requirements (notes to financial statements)	All chapters
• Role and composition of the MD&A	23
Issues Regarding Items in Financial Statements (under various GAAPs)	
The appropriate accounting treatment for the following:	
• Cash and cash equivalents	7
• Receivables	7
• Inventories	8
• Property, plant, and equipment	10
• Goodwill and intangible assets	12
• Depreciation, amortization, impairment, and disposition/derecognition	11
• Provisions, contingencies, and current liabilities	13
• Long-term liabilities	14
• Owners'/shareholders' equity	15, 16
• Earnings per share (basic, diluted)	4, 17
• Financial instruments	7, 9, 14, 15, 16
• Investments in associates/significant influence	9
• Revenue recognition/revenue from contracts with customers, and accounting for revenue and related expenses	6
• Leases	20
• Changes in accounting policies and estimates, and errors	21
• Foreign currency transactions	16
• Accounting for income taxes	18
• Events after the reporting period	5, 23
• Uncommon capital assets (e.g., natural resources, exchanges of assets, decommissioning costs)	10, 11, 13
• Pension plans and other employee future benefits	19
• Assets held for sale and discontinued operations	4

Issues Regarding Items in Financial Statements (under various GAAPs) *(continued)*	Chapters
• Fair value and cash flow hedges	16
• Foreign currency translation	NA
• Business combination	12
• Consolidated statements on date of acquisition	NA
• Consolidated financial statements subsequent to acquisition date	NA
• Joint ventures: proportionate consolidation or equity method	NA
• Complex financial instruments (e.g., perpetual debt, convertible debt, derivatives)	16
Financial Statement Analysis	
• Vertical and horizontal analysis	5A, 23, and all chapters
• Ratios and benchmarking	5A, 23, and all chapters
• Financial statement results for various users	5A, 23, and all chapters
• Pro forma statements	NA
• Impact of financial results on the whole organization	5A, 23, and all chapters

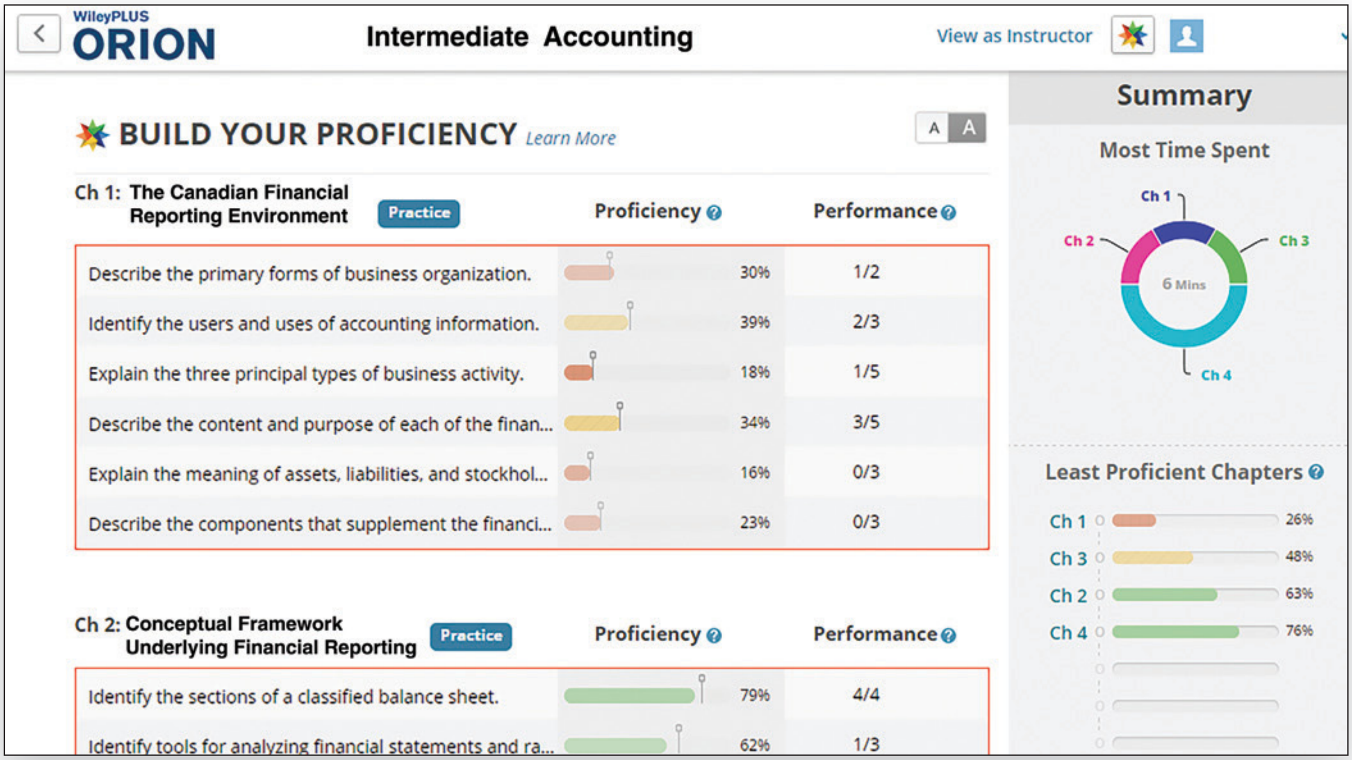
Meeting Financial Reporting Technical Competencies in the CPA Competency Map—The following table maps the financial reporting technical competencies from the CPA Competency Map to *Intermediate Accounting, Eleventh Canadian Edition* (Volume 1). The textbook in its entirety covers the Financial Reporting competencies as noted below. Detailed mapping of specific CPA Financial Reporting competencies to specific textbook Learning Objectives is provided in the charts at the beginning of each chapter. Coverage of other technical competencies (that is, Strategy and Governance, Management Accounting, Audit and Assurance, Finance and Taxation competencies) has also been identified in the charts at the beginning of each chapter and in the end-of-chapter material. Selected enabling competencies have also been identified throughout.

FINANCIAL REPORTING

1.1 Financial Reporting Needs and Systems	Chapters
1.1.1 Evaluates financial reporting needs	1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12
1.1.2 Evaluates the appropriateness of the basis of financial reporting	1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12
1.1.3 Evaluates reporting processes to support reliable financial reporting	3, 8, 12
1.1.4 Explains implications of current trends and emerging issues in financial reporting	2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12
1.1.5 Identifies financial reporting needs for the public sector	10
1.1.6 Identifies specialized financial reporting requirements for specified regulatory and other filing requirements	NA
1.2 Accounting Policies and Transactions	
1.2.1 Develops or evaluates appropriate accounting policies and procedures	1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12
1.2.2 Evaluates treatment for routine transactions	2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12
1.2.3 Evaluates treatment for non-routine transactions	2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12
1.2.4 Analyzes treatment for complex events or transactions	7, 8, 10, 12
1.3 Financial Report Preparation	
1.3.1 Prepares financial statements	1, 3, 4, 5, 6
1.3.2 Prepares routine financial statement note disclosure	4, 5, 6, 7, 8, 9, 10, 11, 12
1.4 Financial Statement Analysis	
1.4.1 Analyzes complex financial statement note disclosure	4, 5, 7, 8, 9, 11, 12
1.4.2 Evaluates financial statements including note disclosures	4, 5, 7, 8, 9, 11, 12
1.4.3 Analyzes and provides input in the preparation of the management communication (e.g., management discussion and analysis (MD&A))	5
1.4.4 Interprets financial reporting results for stakeholders (external or internal)	4, 5, 7, 8, 9, 11, 12
1.4.5 Analyzes and predicts the impact of strategic and operational decisions on financial results	3, 4, 5, 6, 7, 8, 9

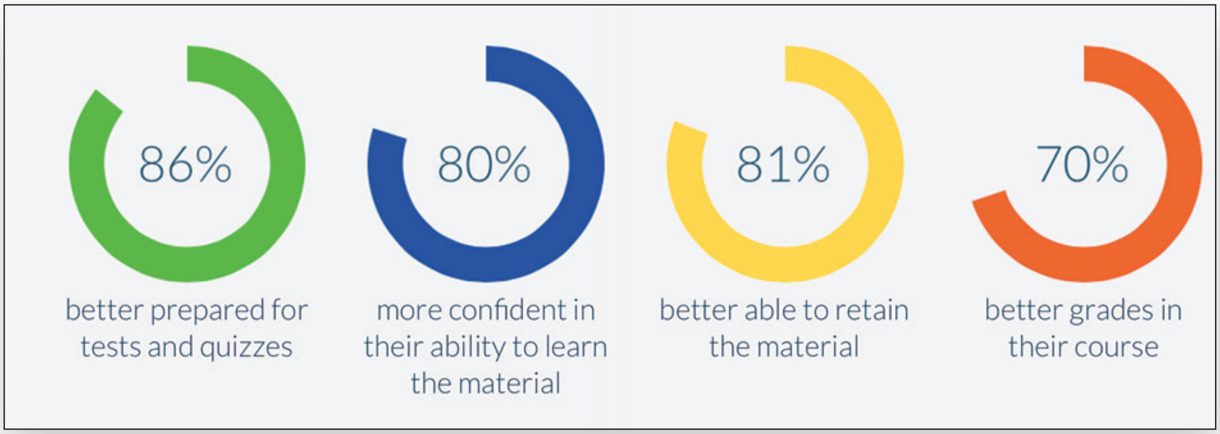
WileyPLUS with ORION

Quickly identify areas of strength and weakness before the first exam, and use the information to build a learning path to success.



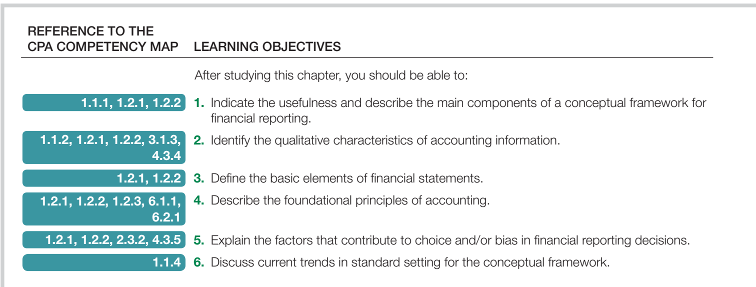
A little time with ORION goes a long way.

Based on usage data, students who engage in ORION adaptive practice—just a few minutes per week—get better outcomes. In fact, students who used ORION five or more times over the course of a semester reported the following results:

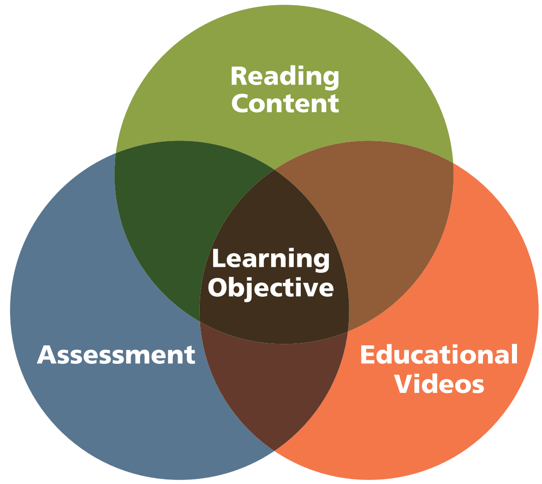


Streamlined Learning Objectives

Easy to follow learning objectives help students make the best use of their time outside of class. Each learning objective is addressed by reading content, watching educational videos, and answering a variety of practice questions, so that no matter where students begin their work, the relevant resources and practice are readily accessible. Learning objectives include references to the CPA competency map. This lets students know which of the CPA competencies they are mastering when they study a particular topic.

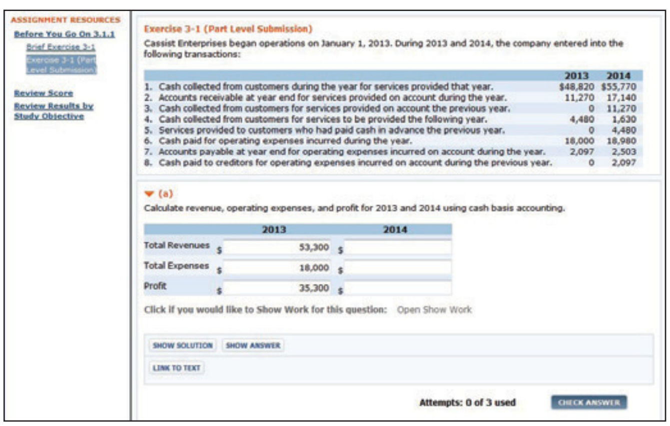


REFERENCE TO THE CPA COMPETENCY MAP	LEARNING OBJECTIVES
	After studying this chapter, you should be able to:
1.1.1, 1.2.1, 1.2.2	1. Indicate the usefulness and describe the main components of a conceptual framework for financial reporting.
1.1.2, 1.2.1, 1.2.2, 3.1.3, 4.3.4	2. Identify the qualitative characteristics of accounting information.
1.2.1, 1.2.2	3. Define the basic elements of financial statements.
1.2.1, 1.2.2, 1.2.3, 6.1.1, 6.2.1	4. Describe the foundational principles of accounting.
1.2.1, 1.2.2, 2.3.2, 4.3.5	5. Explain the factors that contribute to choice and/or bias in financial reporting decisions.
1.1.4	6. Discuss current trends in standard setting for the conceptual framework.



Review and Practice

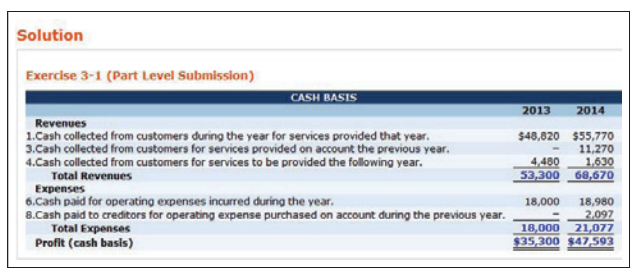
Developing effective problem-solving skills requires practice, relevant feedback, and insightful examples with more opportunities for self-guided practice.

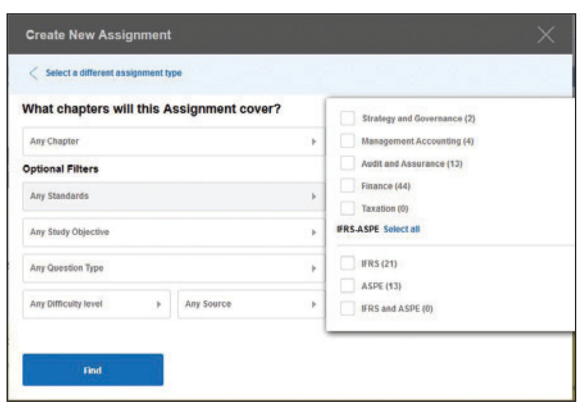


A new bridge course in *WileyPLUS* includes reading content, ORION questions, and practice assignments from introductory accounting to help students refresh their knowledge of basic accounting concepts. A new filtering capability in the assignment area allows instructors to customize assignments by using different filters including criteria related to ASPE and IFRS, CPA competencies, Bloom's Taxonomy, level of difficulty and even learning objectives.

Review and practice opportunities in the text and in *WileyPLUS* include:

- Summary of Learning Objectives
- Glossary Review
- Practice Exercises
- Demonstration Problems
- Applied Accounting Skills Videos
- Office Hour Videos Featuring Core Concept and Problem Walkthroughs





Intermediate Accounting

ELEVENTH CANADIAN EDITION

Intermediate Accounting

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Dedicated to accounting educators in Canada
who, as mentors, are helping the next generation of accountants
develop ethical and integrative frameworks for decision-making.

About the Authors

Canadian Edition

Nicola (Nickie) M. Young, M.B.A., FCPA, FCA, is a Professor of Accounting in the Sobey School of Business at Saint Mary's University, with teaching responsibilities varying from introductory to advanced financial accounting courses to the survey course in the Executive M.B.A. program. She has received teaching awards, and has contributed to the life of the university through membership on the Board of Governors, and the Pension and other committees. Nickie was associated with the Atlantic School of Chartered Accountancy for over 25 years in roles varying from teaching to program development and reform. She has been active in the provincial and national accounting profession, including having served on boards of the CICA (now CPA Canada) dealing with licensure, education, and governance; and has been associated with the Canadian Public Sector Accounting Board and many of its related task forces for almost 25 years. She and Irene Wiecek co-authored the *IFRS Primer: International GAAP Basics* (Canadian and U.S. editions). Nickie is currently working on a phased retirement.

Irene M. Wiecek, FCPA, FCA, is an Associate Professor, Teaching Stream at the University of Toronto, where she is cross-appointed to the Joseph L. Rotman School of Management. She teaches financial reporting in various programs, including the Commerce Program (Accounting Specialist) and the CPA-accredited Master of Management & Professional Accounting Program (MMPA). The Associate Director of the MMPA Program for many years, she co-founded and is Director of the CPA/Rotman Centre for Innovation in Accounting Education, which supports and facilitates innovation in accounting education. Irene has been involved in professional accounting education for over 25 years, sitting on various provincial and national professional accounting organization committees as well as developing and directing the CICA IFRS Immersion Programs for practising accountants. She was appointed a member of the E&Y Academic Resource Center, where she helped to author a new IFRS curriculum for the Americas. In the area of standard setting, she has chaired the CAAA Financial Reporting Exposure Draft Response Committee and is currently a member of the IFRS Discussion Group (IDG). Irene co-authored the *IFRS Primer: International GAAP Basics* (Canadian and U.S. editions) and was the co-editor and contributor for the books *Leveraging Change—The New Pillars of Accounting Education* and *Educating Professionals: Ethics and Judgment in a Changing Learning Environment*. Currently, she co-authors the *Guide to IFRS in Canada* series, which is published by CPA Canada.

Bruce J. McConomy, Ph.D., CPA, CA, is a Professor of Accounting at Wilfrid Laurier University in Waterloo, Ontario. He was a Senior Audit Manager with Deloitte and Touche before returning to Queen's University to obtain his Ph.D. in accounting. Bruce has been the Director of the CPA/Laurier Centre for the Advancement of Accounting Research and Education since it was created in 2005, and is the CPA Ontario Professor of Accounting at Laurier. He has been teaching intermediate financial accounting since the mid-1990s to undergraduates, and since the start of Laurier's CPA Accredited CPA/M.B.A. program (and its predecessor the CMA/M.B.A.) to graduate students. He also teaches in Laurier's Ph.D. in Management program. Bruce has published articles in *Contemporary Accounting Research*, *Journal of Accounting*, *Auditing and Finance*, *Journal of Business*, *Finance and Accounting*, and *Accounting*, *Auditing & Accountability Journal*. He has also published cases in *Accounting Perspectives*, *Issues in Accounting Education*, and *Journal of Accounting Case Research*. Bruce was elected to and served on Council at the Institute of Chartered Accountants of Ontario from 2006 to 2010. Bruce is an Associate Editor of *Accounting Perspectives*.

U.S. Edition

Donald E. Kieso, Ph.D., CPA, received his bachelor's degree from Aurora University and his doctorate in accounting from the University of Illinois. He has served as chair of the Department of Accountancy and is currently the KPMG Emeritus Professor of Accountancy at Northern Illinois University. He has public accounting experience with Price Waterhouse & Co. (San Francisco and Chicago) and Arthur Andersen & Co. (Chicago) and research experience with the Research Division of the American Institute of Certified Public Accountants (New York). He has done post-doctorate work as a Visiting Scholar at the University of California at Berkeley and is a recipient of NIU's Teaching Excellence Award and four Golden Apple Teaching Awards. Professor Kieso is the author of other accounting and business books and is a member of the American Accounting Association, the American Institute of Certified Public Accountants, and the Illinois CPA Society. He is the recipient of the Outstanding Accounting Educator Award from the Illinois CPA Society, the FSA's Joseph A. Silvoso Award of Merit, the NIU Foundation's Humanitarian Award for Service to Higher Education, the Distinguished Service Award from the Illinois CPA Society, and in 2003 received an honorary doctorate from Aurora University.

Jerry J. Weygandt, Ph.D., CPA, is Arthur Andersen Alumni Professor of Accounting at the University of Wisconsin-Madison. He holds a Ph.D. in accounting from the University of Illinois. His articles have appeared in *Accounting Review*, *Journal of Accounting Research*, *Accounting Horizons*, *Journal of Accountancy*, and other academic and professional journals. Professor Weygandt is the author of other accounting and financial reporting books and is a member of the American Accounting Association, the American Institute of Certified Public Accountants, and the Wisconsin Society of Certified Public Accountants. He has been actively involved with the American Institute of Certified Public Accountants and has been a member of the Accounting Standards Executive Committee (AcSEC) of that organization. He also served on the FASB task force that examined the reporting issues related to accounting for income taxes. He is the recipient of the Wisconsin Institute of CPAs' Outstanding Educator's Award and the Lifetime Achievement Award. In 2001, he received the American Accounting Association's Outstanding Accounting Educator Award.

Terry D. Warfield, Ph.D., is the PWC Professor in Accounting at the University of Wisconsin-Madison. He received a B.S. and M.B.A. from Indiana University and a Ph.D. in accounting from the University of Iowa. Professor Warfield's area of expertise is financial reporting, and prior to his academic career, he worked for five years in the banking industry. He served as the Academic Accounting Fellow in the Office of the Chief Accountant at the U.S. Securities and Exchange Commission in Washington, D.C., from 1995–1996. Professor Warfield's primary research interests concern financial accounting standards and disclosure policies. He has published scholarly articles in *The Accounting Review*, *Journal of Accounting and Economics*, *Research in Accounting Regulation*, and *Accounting Horizons*, and he has served on the editorial boards of *The Accounting Review*, *Accounting Horizons*, and *Issues in Accounting Education*. Professor Warfield has served on the Financial Accounting Standards Committee of the American Accounting Association (Chair 1995–1996) and the AAA-FASB Research Conference Committee. He currently serves on the Financial Accounting Standards Advisory Council of the Financial Accounting Standards Board. Professor Warfield has received teaching awards at both the University of Iowa and the University of Wisconsin, and he was named to the Teaching Academy at the University of Wisconsin in 1995. Professor Warfield has developed and published several case studies based on his research for use in accounting classes. These cases have been selected for the AICPA Professor-Practitioner Case Development Program and have been published in *Issues in Accounting Education*.

Preface

In the last decade, we have come through a period of unprecedented change in accounting standards. More recently, in Canada, we have witnessed the evolution of the accounting profession from three main accounting bodies (representing Chartered Accountants, Certified Management Accountants, and Certified General Accountants) into one unified group: Chartered Professional Accountants Canada (CPA Canada). We now have a freshly minted CPA education program, a new CPA Competency Map (CM), a new CPA Knowledge Supplement (KS), and new CPA Common Final Examinations. Many of us have remapped our curricula to the CPA CM and created new courses and programs (some of which have been accredited by the CPA profession). The pace of change for standard setting and related educational requirements for professional accountants sometimes seems staggering! Change has become the new norm for us and things don't seem to be slowing down.

This state of flux has made many of us rethink our learning environments. Some fundamental questions are being revisited. How can we and our students keep up with the changing standards? What does it mean to be a competent accountant? How much do we emphasize the use of technology as a learning platform? And finally, how does what we do fit with the changing professional landscape?

From our perspective, we see the need for

- increased emphasis on helping faculty and students understand how to cope with changes in standards,
- a broadened perspective on what it means to be competent,
- increased use of a variety of technologies to promote learning, and
- renewed acknowledgement that what we do in our classrooms is only part of the journey that students embark on to become professional accountants.

In our roles as educators, many of us increasingly see ourselves as facilitators as opposed to purveyors of knowledge. At the heart of things, we still want to produce good, ethical decision-makers as well as to encourage thoughtfulness and reflection. We also want our graduates to be competent and skilled. Our students have to at least begin to master our complex body of knowledge and also to be competent in applying it. This is a lot to ask, especially when things keep shifting.

This edition is about learning to live with a constantly changing body of knowledge. To this end, we have incorporated new accounting standards where the standards have already been issued (even if they are not yet mandatory). In addition, we have included the "Looking Ahead" section again at the end of each chapter, which signals changes in accounting standards coming down the pipe. We are committed to helping our accounting faculty and students steer their way through standards changes that are issued between editions of this text. To this end, we will continue to issue supplements and updates between editions as we have done for the past few years.

This edition is also about integration along the following dimensions:

- integration of financial reporting with other areas (such as assurance and finance);
- integration of our learning environments and frameworks with those of the accounting profession, including a competency-based framework; and
- increased integration with a learning environment that features technology, including *WileyPLUS* and our new Office Hour Videos.

We have also included charts showing how the textbook integrates with the CPA Competency Map and Knowledge Supplement throughout the text and within *WileyPLUS*. This is discussed in the New Features section that follows. We encourage you to have a quick look. Below is a brief overview that highlights our new and continuing features.

New Features

As noted above, several new features have been added to this edition.

Emphasis on Integration with Related Areas

We have included integration icons in each chapter to help identify key areas of integration (in addition to our existing finance and law icons). Many of our end-of-chapter questions have an integration aspect. For those problems that most directly focus on integration, we also include integration icons so that they are easily identified. We have added an Office Hour Video feature, which provides a short video discussion of selected end-of-chapter questions per chapter, and an additional integration-related topic in most chapters.

Augmented End-of-Chapter Material

End-of-chapter material has been expanded to include questions that provide students with Excel spreadsheets to help them prepare solutions. We also continued our emphasis on having students evaluate the differences in solutions prepared using IFRS versus ASPE. Our new Office Hour Video feature provides a short walkthrough of select questions and solutions.

CPA Competency Map Integration

At the start of each chapter, we now provide a chart linking that chapter's Learning Objectives with the related requirements of the CPA Competency Map. This information will help students planning to obtain their Advanced Certificate in Accounting and Finance (ACAF) or write the Common Final Evaluation (CFE) to link the coverage of intermediate accounting topics to the CPA educational requirements. We have also mapped the content of the book against the Competency Map and Knowledge Supplement. These appear on the inside front cover of the text. In addition, the material in *WileyPLUS* has been more comprehensively mapped.

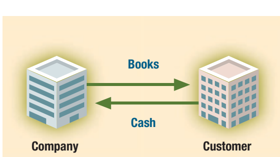
Task-Based Simulations

We have added a new type of question to our end-of-chapter material that is in a format similar to questions used in the CPA Professional Education program. Task-Based Simulations after Chapters 5, 9, 12, 15, 17, and 23 combine material from the current chapter with previous chapters and present it in this new hands-on format. This allows students to become familiar with the new exam format while getting a sense of how the various concepts fit together.

Continuing Features

Many features have contributed to the success of this textbook over the years. The following points outline just a few.

Emphasis on Business



The focus of the feature story that starts each chapter in this edition is on the business models of various companies and industries, along with accounting issues that affect them. The first section of most chapters focuses on **Understanding the Business**, which introduces the accounting topic in the context of everyday business. Many chapters have a **business transactions example box**. In most business transactions, you give something up and receive something. These boxes are meant to help you understand what has been given up and what has been received in the transaction. This is tremendously helpful when you are trying to decide how to account for a transaction or economic event.

Emphasis on IFRS and ASPE

Icons: Individual IFRS and ASPE icons call attention to items treated differently by the two sets of standards. The joint IFRS-ASPE icon indicates a direct comparison between the two approaches.

Side-by-side journal entries: These journal entries illustrate differences in treatment between IFRS and ASPE.

Enhanced comparison charts: The end-of-chapter charts that identify the major differences between IFRS and ASPE include a column with cross-references to relevant illustrations and brief exercises that describe the differences outlined in the comparison chart. As before, where there is a new standard being proposed, we have added a column to the end-of-chapter charts so that you understand what may be in store in the near future, or provided a discussion within the chapter's Looking Ahead feature to alert you to upcoming changes expected.

Emphasis on Professional and Ethical Behaviour

Rather than featuring ethics coverage and problem material in isolation, we use an ethics icon to highlight ethical issues as they are discussed within each chapter. This icon also appears beside exercises, problems, or cases where ethical issues must be dealt with in relation to all kinds of accounting situations.

Emphasis on Readability

The readability of the text has been improved by using fewer abbreviations, plainer language, shorter sentences, numbered lists, and clearer headings. An **end-of-book glossary** provides definitions of key terms highlighted in the text. **Alternative Terminology** notes within the chapter familiarize students with other commonly used terms.

Grounding in Accounting Research and Theory

We have always emphasized concepts and principles, including those that span other disciplines, such as law and finance. In addition to this, the **Accounting Theory** icon calls attention to accounting theory that underpins much of the accounting body of knowledge, introducing students to an accounting research perspective.

Real World Emphasis

Because intermediate accounting is a course in which students must understand the application of accounting principles and techniques in practice, we strive to include as many real-world examples as possible.

Reinforcement of the Concepts

Throughout each chapter, you are asked What Do the Numbers Mean? and are presented with discussions applying accounting concepts to business contexts. This feature builds on the opening feature stories in making the accounting concepts relevant to you. Through current examples of how accounting is applied, you will be better able to relate to and understand the material. The underlying concepts icons in each chapter alert you to remember that the issue under discussion draws on concepts identified in Chapter 2 as part of the conceptual framework. More emphasis has been placed on measuring fair values using the new IFRS 13 standard. In addition, an Analysis section is present in most chapters. This section discusses the effect on the financial statements of many of the accounting choices made by corporate management, alerting you to look behind the numbers. Finally, the accounting equation appears in the margin next to key journal entries to help you understand the impact of each transaction on the company's financial position and cash flows.

Helping Students Practise

The end-of-chapter material is comprehensive. Brief exercises, exercises, and problems focus on quantitative material. Case material allows you to analyze business transactions and apply both IFRS and ASPE, with particular attention to integration being provided by Integrated Case questions. Research and Analysis questions allow you to explore the nature of GAAP differences and understand how different accounting standard setters can arrive at different solutions in terms of standards.

A summary of the Case Primer guiding you through the case study method appears inside the back cover of this text. This is in addition to the full Case Study Primer available on *WileyPLUS* and the Student Website.

DIGGING DEEPER

Analysis doesn't have to be just part of the cases. Our Digging Deeper feature asks you to look more closely at the results you obtain in the problems and exercises. For instance, you might be asked to comment on results or determine how things might be different if one of the original variables were to change. Digging Deeper questions are identified using the icon shown here.

WileyPLUS

WileyPLUS is an innovative, research-based on-line environment for effective teaching and learning. *WileyPLUS* builds students' confidence because it takes the guesswork out of studying by providing students with a clear roadmap: **what to do, how to do it, and if they did it right**. Students will take more initiative so you'll have a greater impact on their achievement in the classroom and beyond.

Among its many features, this on-line learning interface allows students to study and practise using the digital textbook, quizzes, and algorithmic exercises. The immediate feedback helps students understand where they need to focus their study efforts. We have standardized the chart of accounts to reduce complexity and to facilitate on-line practice.

Based on cognitive science, **WileyPLUS with Orion** is a personalized adaptive learning experience that gives students the practice they need to build proficiency on topics while using their study time more effectively. The adaptive engine is powered by hundreds of unique questions per chapter, giving students endless opportunities for practice throughout the course. Orion is available with this text.

Currency and Accuracy

SIGNIFICANT CHANGE

As in past editions, we have endeavoured to make this edition the most current and accurate text available. Everywhere there has been a significant change in the accounting standard or how it is applied, it has been highlighted with a significant change icon. Where change is on the horizon, we have noted this at the end of each chapter under the Looking Ahead section. We are also committed to issuing brief update supplements on *WileyPLUS* when new standards are issued.

The following list outlines the revisions and improvements made to the chapters in Volume One of this text.

Chapter 2 Conceptual Framework Underlying Financial Reporting

- The revenue recognition principle has been updated to incorporate IFRS 15.
- New information has been added on common forms of business including those for professionals.
- A section on how the concept of materiality is used in audits has been added.
- The material on measurement has been moved from the appendix to Chapter 3.
- The Looking Ahead feature gives a brief update on the impact of proposed changes to the conceptual framework and the June 2014 IASB Exposure Draft entitled the "Disclosure Initiative (Proposed amendments to IAS 1)."

Chapter 3 The Accounting Information System and Measurement Issues

- The revised chapter has been split into two parts plus appendices for ease of use and flexibility.

- The start of this chapter continues to provide students with an overview and review of accounting transactions, journal entries, and other aspects of the accounting cycle. For instructors who like to emphasize a 10-column work sheet approach to assist with financial statement presentation, this material is now in the self-contained Appendix 3A.
- A new section (Part II) has been developed for this chapter emphasizing measurement issues. This section covers valuation techniques, how to calculate value in use, and measuring fair value under IFRS 13.
- A new appendix has been added on present value techniques. Appendix 3B illustrates how to perform present value calculations using formulas, tables, financial calculators, and spreadsheets.

Chapter 4 Reporting Financial Performance

- The definition for discontinued operations has been updated.
- The function versus nature discussion has been streamlined and examples given, illustrating the fact that many companies use a mixed approach.
- The example and discussion relating to the statement of changes in shareholders' equity has been updated.
- Material on calculating a price/earnings ratio has been added.

Chapter 5 Financial Position and Cash Flows

- More emphasis has been placed on presentation under IFRS. (For instance, there are more examples of Canadian companies using IFRS.)
- A detailed discussion has been added in the Looking Ahead section of the impact of proposed changes to the conceptual framework and the June 2014 IASB Exposure Draft entitled the "Disclosure Initiative (Proposed amendments to IAS 1)."

Chapter 6 Revenue Recognition

- The chapter has been rewritten to incorporate IFRS 15 *Revenue from Contracts with Customers*. The chapter includes more detailed discussions of how to identify performance obligations, how to measure them, and when to recognize revenues. Select material on the earnings approach under ASPE has been retained.
- The discussion on accounting for long-term contracts has been moved to an appendix.
- The chapter includes more detailed discussion on specific items, such as rights of returns, repurchase agreements, principal and agent, and warranties.
- Summaries have been added, which capture the new 5-step revenue recognition process as well as other more complex revenue recognition issues.

Chapter 7 Cash and Receivables

- There is more focus on the requirements of IFRS 9 and a reduced emphasis on IAS 39 for areas such as impairment, as the IASB continues to move toward a forward-looking impairment model.
- A discussion has been added of the IFRS standards on derecognition of financial assets, which are now complete. A brief discussion of the likely impact of the IFRS changes for companies following ASPE has also been added.

Chapter 8 Inventory

- The chapter has been refreshed and streamlined, including updating for an interface with Chapter 6 and IFRS 15.
- The section on biological assets has been updated to introduce the concept of bearer biological assets.

Chapter 9 Investments

- The chapter has been rewritten to incorporate changes to IFRS 9 *Financial Instruments*. Select references to IAS 39 have been retained but de-emphasized.
- Material has been added to deal with FV-OCI accounting for debt instruments (with recycling).
- The section on impairments has been updated and augmented as it relates to the expected loss model. Numerical examples and a decision tree have been added.
- Additional information has been included regarding disclosure requirements.

Chapter 10 Property, Plant, and Equipment: Accounting Model Basics

- A more detailed discussion of the full cost and successful efforts methods of accounting for natural resource properties is now included.
- Appendix 10B—Revaluation: The Proportionate Method has been expanded to provide more details of the calculations behind the numerical example of this method.
- The chapter and Looking Ahead section discuss a change to IAS 16 regarding accounting for *Agriculture: Bearer Plants*, effective for annual periods beginning on or after January 1, 2016.

Chapter 11 Depreciation, Impairment, and Disposition

- The chapter and Looking Ahead section discuss a change to IAS 16 regarding restrictions on the use of depreciation methods based on revenue generated by companies.
- Changes to disclosure requirements for impairment of assets under IAS 36 are discussed. (The changes became effective on January 1, 2014, and tie in to new requirements for the fair value hierarchy under IFRS 13.)

Chapter 12 Intangible Assets and Goodwill

- The chapter and Looking Ahead section discuss a change to IAS 38 regarding additional items that could indicate commercial or technological obsolescence.
- New (and updated) examples have been provided, including a discussion of challenges faced by companies as set out in a recent Financial Executives Institute Goodwill Impairment Study.

Special Student Supplements

The ***Study Guide to Accompany Intermediate Accounting***, Eleventh Canadian Edition, provides a solid review of the concepts presented in the intermediate accounting course, and gives students strategies for dealing with the complexities of applying those concepts. The following are included in this guide to help you make your way through each chapter.

To Help Gain a Solid Understanding of the Concepts

- A chapter **Overview** introduces the reader to the topics covered and their importance.
- **Study Steps** review the business transaction under discussion; show how to recognize, measure, and disclose issues related to that transaction; and demonstrate how to then make the appropriate calculations and apply the appropriate accounting methods.
- **Tips** alert learners to common pitfalls and misconceptions and to remind students of important terminology, concepts, and relationships.
- A **Toolkit** printed on cards can be detached from the guide and referred to throughout the course. These cards present material such as a review of the conceptual triangle from the book, a glossary of definitions, and summary of key ratios.

To Aid in Applying Concepts Successfully

- **Exercises and Multiple-Choice Questions** allow students to practise using material that is representative of homework assignments and exam questions they are likely to encounter.
- **Purposes** identify the essence of each exercise or question and link it to the text material.
- **Solutions** show students the appropriate worked-out solutions for each exercise and multiple-choice question.
- **Explanations** give users the details of how selected solutions were derived and explain why things are done as shown.
- **Approaches** coach students on the particular model, computational format, or other strategy to be used to solve particular problems.

The Intermediate Accounting Simulation Practice Set by Fred Pries will help students see how the individual topics they study in intermediate accounting are related to the accounting systems of an organization and to the financial statements as a whole. Students play the role of a newly hired accountant for Woodlawn Engineering, an owner-managed company, and prepare a full set of financial statements starting from an unadjusted trial balance. Each module of the simulation is linked to a particular topic covered in the intermediate accounting course and introduces new information. Students analyze this information, recommend what adjustments are needed to the books and financial statements of the company, and write reports to the chief financial officer explaining the basis for their recommendations.

Canadian Financial Accounting Cases by Camillo Lento and Jo-Anne Ryan provides additional cases at the intermediate level that may be used either for assignment purposes or for in-class discussion. The cases are keyed to various topics covered by the two volumes of *Intermediate Accounting* and have been developed using IFRS and ASPE.

Acknowledgements

We thank the users of our tenth edition, including the many instructors, faculty, and students who contributed to this revision through their comments and instructive criticism.

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It takes many people and coordinated efforts to get an edition off the ground. Many thanks to the team at John Wiley & Sons Canada, Ltd., who are superb: Zoë Craig, Executive Editor; Daleara Hirjikaka, Developmental Editor; Veronica Visentin, V.P. and Director, Market Solutions; Karen Staudinger, Editorial Manager, who has been an integral part of the last six editions; Luisa Begani, Media Editor, for managing this increasingly important aspect of the text; Deanna Durnford, Supplements Coordinator; Anita Osborne, Senior Marketing Manager; Kaitlyn Sykes, Editorial Intern; and Sara Veltkamp, Kristen Vanderkooy, and Duncan Moore, Digital Solutions Managers. Their enthusiasm and support have been invaluable. The editorial contributions of Laurel Hyatt, Zofia Laubitz, Merrie-Ellen Wilcox, and Belle Wong are also very much appreciated.

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We thank CPA Canada and the IFRS Foundation for allowing us to quote from their materials and Brookfield Asset Management for permitting us to use its 2014 financial statements for our specimen financial statements.

We appreciate the opportunity to reach out to so many colleagues and students through this book. Your conversations and input have greatly helped shape the book and make it all it can be. We are thankful to be part of a group of such dedicated educators! Let's keep the conversation going.

Suggestions and comments are always appreciated. We have striven to produce an error-free text, but if anything has slipped through the variety of checks undertaken, please let us know so that corrections can be made to subsequent printings.

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Brief Contents

VOLUME ONE

VOLUME TWO

Contents

CHAPTER 1

THE CANADIAN FINANCIAL REPORTING ENVIRONMENT

LEARNING OBJECTIVES

REFERENCE TO THE CPA COMPETENCY MAP	LEARNING OBJECTIVES
	After studying this chapter, you should be able to:
1.1.1, 1.2.1, 5.2.3	1. Explain how accounting makes it possible to use scarce resources more efficiently.
1.1.1, 1.1.2	2. Explain the meaning of "stakeholder" and identify key stakeholders in financial reporting, explaining what is at stake for each one.
1.1.1, 1.1.2	3. Identify the objective of financial reporting.
1.1.1, 1.1.2	4. Explain how information asymmetry and bias interfere with the objective of financial reporting.
1.1.1, 1.1.2	5. Explain the need for accounting standards and identify the major entities that influence standard setting and financial reporting.
1.1.1, 1.1.2, 1.2.1	6. Explain the meaning of generally accepted accounting principles (GAAP) and the significance of professional judgement in applying GAAP.
1.1.1, 1.1.2, 1.2.1, 1.3.1	7. Discuss some of the challenges and opportunities for accounting.

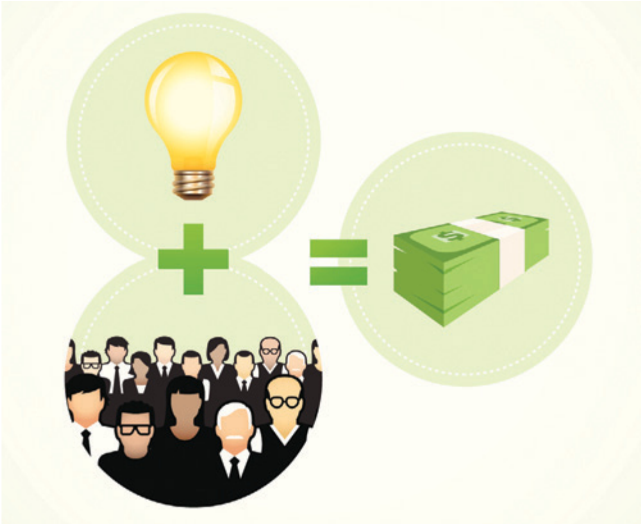
CAPITALIZING ON FINANCIAL REPORTING

EVERY BUSINESS—from the lawn-mowing service you may have operated in high school to a multinational corporation—needs capital to survive. You likely borrowed money from your parents to buy a weed trimmer, while the corporation issued millions of shares to raise capital from the public. But what about all the small and medium-sized enterprises (SMEs) in the middle? How do they get money to launch and grow?

The TMX Group, which operates the Toronto Stock Exchange (TSX) for publicly traded companies and the TSX Venture Exchange for companies to raise money from venture capital funds, recognizes the need to help SMEs raise capital through other means. While there are 3,900 companies listed on the TMX's two public exchanges, there are about 1.1 million private companies—more than 98% of them considered SMEs.

In late 2014, the TMX Group launched TSX Private Markets, which allows companies to trade securities in the exempt market. This means these companies, called private issuers, are exempt from the rigorous requirements of public issuers to file a prospectus, a document disclosing financial and other business information. "For companies that don't wish to go public, exempt markets fill an important need for capital and liquidity," said Thomas Kloet, then-CEO of the TMX Group. "The private companies that access the platform are vetted, but there are fewer requirements than for exchange-listed companies."

The TMX Group is looking into another way that SMEs can get capital: crowdfunding. It started as an on-line way for the public to donate to a cause or project without expecting to get anything in return. Now, both not-for-profits and businesses raise billions of dollars through crowdfunding sites such as Kickstarter and Indiegogo. The Ontario Securities Commission recently proposed rules that would allow small companies to issue shares in exchange for money on on-line portals registered with securities regulators, raising up to $1.5 million a year. At the time that Mr. Kloet spoke to the Economic Club of Canada



Matt Chalwell/Getty Images

in the spring of 2014, the TMX Group wanted to somehow get involved in this burgeoning equity crowdfunding. “It is generally understood that we don’t know exactly where this financing method will go, but it is also understood that, in time, this will be a very important capital raising tool for Canadian entrepreneurs, particularly for the smallest companies. Given that Canada is truly a nation of SMEs, it could be transformational,” Mr. Kloet said.

What does raising capital have to do with financial reporting? No matter how big the company, no matter how it raises money, it needs to present its financial information to potential investors and other stakeholders accurately and consistently with financial reporting standards—using a common “language” that investors understand. “Investor confidence is the cornerstone of financing small businesses,” Mr. Kloet said.

Sources: “TMX Group Launches TSX Private Markets,” TMX Group news release, November 14, 2014; Speech by Thomas Kloet to the Economic Club of Canada, May 27, 2014; “Exempt Market Review,” Ontario Securities Commission backgrounder, March 20, 2014.

PREVIEW OF CHAPTER 1

North American financial reporting systems are among the best in the world. Our commitment to keeping our financial reporting systems strong is as intense as ever, because in this changing business world, information must be relevant and reliable for our capital markets to work efficiently. This chapter explains the environment of financial reporting and the many factors that affect it. It provides the theory and concepts underpinning the topics covered in the rest of the chapters, giving you the foundation to exercise professional judgement in the many issues that require it.

The chapter is organized as follows:

THE CANADIAN FINANCIAL REPORTING ENVIRONMENT

Financial Statements and Financial Reporting	Standard Setting	Generally Accepted Accounting Principles	Challenges and Opportunities for the Accounting Profession
▪ Accounting and capital allocation ▪ Stakeholders ▪ Objective of financial reporting ▪ Information asymmetry	▪ Need for standards ▪ Parties involved in standard setting	▪ GAAP hierarchy ▪ Professional judgement	▪ Oversight in the capital marketplace ▪ Centrality of ethics ▪ Standard setting in a political environment ▪ Principles versus rules ▪ Impact of technology ▪ Integrated reporting ▪ Conclusion

Financial Statements and Financial Reporting

Like other human activities and disciplines, accounting is largely a product of its environment. This environment includes conditions, constraints, and influences that are social, economic, political, and legal—all of which change over time. As a result, accounting theory and practices have always evolved and need to continue to evolve in order to remain relevant.

Over the past decade or two, the accounting landscape has changed dramatically, being shaped by many things—some good and some not so good. These include:

REAL WORLD EMPHASIS

- spectacular business failures, including **WorldCom Inc., Enron**, and **Arthur Andersen**;
- capital market failures, including the subprime lending crisis and bank failures;
- near bankruptcies of several countries;

- globalization of capital and other markets;
- globalization of financial reporting standards;
- increasing use of more sophisticated technology; and
- increasing access to information.[1]

All of these factors, as well as many others, provide accountants with great challenges but also great opportunities!

Accounting is defined best by describing its three essential characteristics. Accounting is (1) the identification, measurement, and communication of financial information (2) about economic entities (3) to interested persons.

Financial accounting (**financial reporting**) is the process that culminates in the preparation of financial reports that cover all of the enterprise's business activities and that are used by both **internal and external** parties. Users of these financial reports include investors, creditors, and others. In contrast, **managerial accounting** is the process of identifying, measuring, analyzing, and **communicating financial information** to **internal** decision-makers. This information may take varied forms, such as cost-benefit analyses and forecasts that management uses to plan, evaluate, and control an organization's operations. This textbook focuses on financial accounting, while managerial accounting is covered in other courses.

Financial statements are the principal way of communicating financial information to those who are outside an enterprise. These statements give the firm's history, quantified in terms of money. The most frequently provided financial statements are the:

1. **statement of financial position,**
2. **statement of income/comprehensive income,**
3. **statement of cash flows,** and
4. **statement of changes in equity**.

ALTERNATIVE TERMINOLOGY

These financial statements are also sometimes called:

1. balance sheet,
2. income statement, and
3. cash flow statement.

Under ASPE, the comparable statement to the statement of changes in equity is the statement of retained earnings, which is a different statement.

In addition, **note disclosures** are an important part of each financial statement. Some financial information cannot be expressed in the financial statements or is better expressed through other means. Examples include the president's letter and supplementary schedules in the corporate annual report, prospectuses, reports filed with government agencies, news releases, management forecasts, and descriptions of an enterprise's social or environmental impact. Such information may be required by a pronouncement by an authority, or a regulatory rule[2] or custom, or because management wants to disclose it voluntarily. The main focus of this textbook is the basic financial statements (including notes).

Accounting and Capital Allocation

Objective 1
Explain how accounting makes it possible to use scarce resources more efficiently.

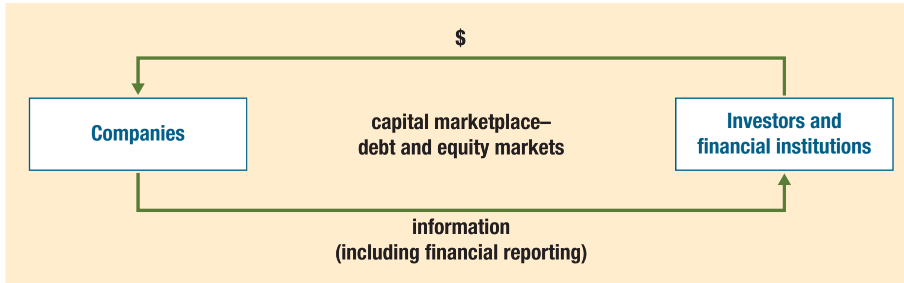
Because **resources** are limited, people try to conserve them, use them effectively, and identify and encourage those who can make efficient use of them. Through an **efficient use of resources**, our standard of living increases.

Markets, free enterprise, and competition determine whether a business will succeed and thrive. The accounting profession has the important responsibility of **measuring**

TREASURY MANAGEMENT
5.2.3

company performance accurately and fairly on a timely basis. The information provided by accounting enables investors and creditors to **compare** the income and assets of companies and thus **assess the relative risks and returns** of different investment opportunities. Based on their assessments, investors and creditors can then channel their resources (that is, invest in these companies or lend them money) more effectively. Illustration 1-1 shows the process of **capital allocation**.

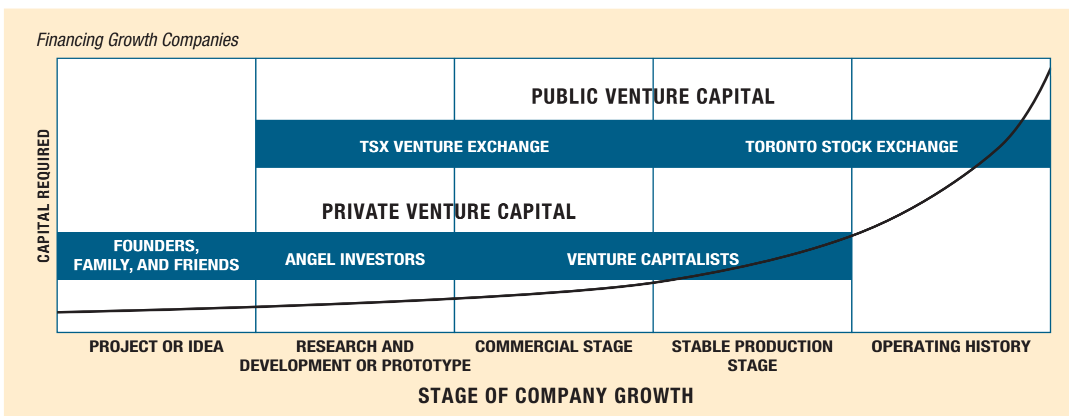
Illustration 1-1
Capital Allocation Process



In Canada, the primary exchange mechanisms for allocating resources are **debt and equity markets**,[3] as well as **financial institutions** such as banks.[4] The debt and equity marketplace includes both public stock markets/exchanges and private sources.

Illustration 1-2 shows the sources of capital in Canada for various stages of company growth.

Illustration 1-2
Sources of Capital



Providing an effective system to facilitate capital allocation is critical to a healthy economy. Efficient capital markets promote productivity, encourage innovation, and provide a platform for buying and selling securities and obtaining and granting credit.[5] Unreliable and irrelevant information leads to **poor capital allocation**, which hurts the securities markets and economic growth. The accounting numbers that companies report affect the **transfer of resources** among companies and individuals. Consider the fact that stock prices generally rise when positive news (including financial information) is unexpectedly released. In addition, **credit rating agencies** use accounting and other information to rate companies' financial stability.[6] This gives investors and creditors **additional independent information** to use when making decisions. For companies, a good rating can mean greater access to capital and at lower costs.

Objective 2
Explain the meaning of "stakeholder" and identify key stakeholders in financial reporting, explaining what is at stake for each one.

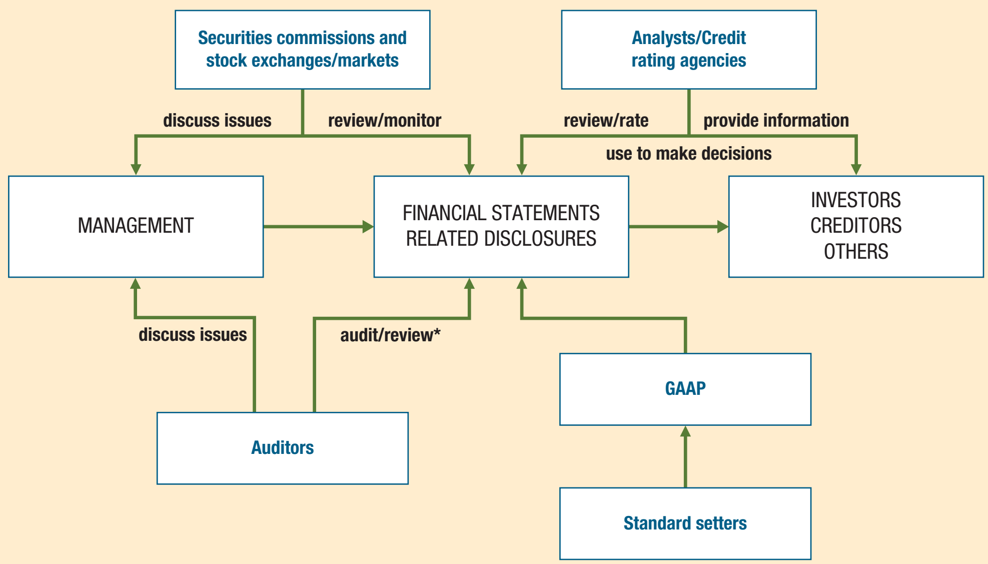
Stakeholders

Stakeholders are parties who have something at risk in the financial reporting environment, such as their salary, job, investment, or reputation. Key stakeholders in the financial reporting environment include **traditional users** of financial information as well as others. In the stakeholder context, **users** may be more broadly defined to include not only parties who are relying directly on the financial information for resource allocation (such as investors and creditors) but also others who help in the efficient allocation of resources (such as financial analysts and regulators).

The broader definition of users includes anyone who **prepares**, **relies on**, **reviews**, **audits**, **or monitors financial information**. It includes investors, creditors, analysts, managers, employees, customers, suppliers, industry groups, unions, government departments and ministers, the public in general (such as consumer groups), regulatory agencies, other companies, and standard setters, as well as auditors, lawyers, and others. Illustration 1-3 shows the relationships among these stakeholders.

Illustration 1-3

Selected Key Stakeholders in the Financial Reporting Environment



* Not all financial statements are required to be audited. In general, all companies whose shares or debt are **publicly traded** must have an audit and therefore comply with generally accepted accounting principles (GAAP). Private companies may decide not to have an audit but must have unanimous shareholder consent according to the Canada Business Corporations Act. For private companies, the decision to have an audit or not may depend on whether the statements' users would find audited GAAP statements more useful.

Various stakeholders have specific functions in the financial reporting environment. Company management **prepares** the financial statements. It has the best insight into the business and therefore knows what should be included in the financial statements. The statements are then **audited** by auditors, who may discuss with management how economic events and transactions have been communicated in the financial statements. The value that auditors add to the statements lies in the auditors' independence. They act on behalf of the shareholders to ensure that management is accounting properly for the economic transactions. The auditors also **review** the information to ensure that it reflects sound accounting choices.

Investors and creditors **rely on** the financial statements to make decisions. It is up to these parties to carefully examine the information given. Standard setters **set** **generally accepted accounting principles (GAAP)**. Securities commissions and stock exchanges **monitor** the financial statements to ensure full and plain disclosure of material information and to determine whether the companies may continue to list their shares on stock exchanges. Finally, the credit rating agencies and analysts **monitor and analyze** the information produced by the company, looking for signs of change; that is, an improved or weakened financial condition.

LAW

Illustration 1-4 identifies what is at stake for each stakeholder. This is not meant to be a complete list. Rather, it identifies the major stakeholder groups.

Illustration 1-4

What Is at Stake for Each Stakeholder?

STAKEHOLDER	WHAT IS AT STAKE?
Investors/creditors	Investment/loan
Management	Job, bonus, reputation, salary increase, access to capital markets by company
Securities commissions and stock exchanges	Reputation, effective and efficient capital marketplace
Analysts and credit rating agencies	Reputation, profits
Auditors	Reputation, profits (companies are their clients)
Standard setters	Reputation
Others	Various

As noted in Illustration 1-3, the system provides **checks and balances** to ensure that the people with capital—the investors and creditors—have good information to use when deciding where best to invest or allocate their capital. The system does not always work, however. Because the system involves people, human behaviour is often a key unpredictable variable. People often act in their own **self-interest** rather than in the **best interest of the capital marketplace, and by extension, the economy**.

WHAT DO THE NUMBERS MEAN?

Consider the much-publicized crisis that arose when large numbers of borrowers with lower-quality, "subprime" mortgages defaulted, which was partly responsible for destabilizing the capital markets and the economy, starting in 2007. What was this all about and how did it trigger a global recession? Much has to do with individuals and entities acting in their own self-interest and a lack of transparency or lack of understanding of the true risks involved.

Financial institutions regularly securitize pools of assets in order to access the cash that is tied up in the assets. As a general rule, the securitization involves selling the assets to a separate entity, often for cash. The entity then sells units or shares in the pool of assets to investors. The following are the steps in a normal securitization of mortgage assets:

1. Lender lends money to customers to buy homes.
2. Lender sells pool of mortgage assets from the above loans to a separate entity (often referred to as a special purpose entity or SPE).
3. SPE sells units or shares in the pool of mortgages to investors.

ETHICS

There is nothing inherently wrong with this structure and it can work very well for all parties as long as they understand the risks involved. It is good for borrowers because it makes funds more accessible. It is good for lenders because they are able to get their cash out of the mortgage assets. It is good for SPEs because they earn interest on the pool of assets. Finally, it is good for investors because they earn a return on their investment. What went wrong in the subprime lending situation, then?

First, the lenders or their designated mortgage brokers loaned money aggressively, in the hopes of higher profits, to borrowers who may not have been creditworthy.

Second, many of the loans were adjustable-rate notes, which meant that, initially, the interest rates were low—often below the prime lending rate, which is where the term "subprime" comes from. But afterwards, the rates reset themselves according to the loan agreement, often becoming significantly higher. Therefore, even though the borrowers may have been able to afford the loan payments initially, many could no longer afford them once the interest rates became higher. The borrowers borrowed the funds anyway because they wanted to buy houses, even though they knew or should have known that they might not be able to keep up with the loan payments in future.

Third, many investors in the SPE did not understand the risks they were taking on by investing in this type of pool of assets, which was systemically risky due to the creditworthiness of the borrowers and the mortgages' interest rate reset feature.

Things began to unwind when the mortgages' interest rates were set higher. This caused many borrowers to default on their mortgages and lose their homes. These homes were repossessed and flooded the market, driving house prices down. Many borrowers found that the amounts of their mortgages were now higher than the value of their homes and they walked away from their debt, causing more homes to go on sale in an already depressed market. The investors in the SPE suffered large losses due to the defaulted loans. All this contributed to a depressed housing market and economy.

From a financial reporting perspective, a few lessons were learned:

1. Many capital market participants act in their own self-interest to the potential harm of others.
2. The amount and nature of risk are not always properly communicated to investors.
3. Investors do not always understand what they are investing in.

Stakeholders in the capital marketplace are working to ensure that this type of situation does not happen again.

Objective of Financial Reporting

Objective 3
Identify the objective of financial reporting.

What is the **objective of financial reporting**? The objective of **general-purpose financial statements** is to **provide financial information about the reporting entity that is useful to present and potential equity investors, lenders, and other creditors in making decisions in their capacity as capital providers**. (This is referred to as the **decision-usefulness approach** to financial reporting.) Information that is decision-useful to capital providers may also be useful to other users of financial reporting who are not investors and creditors. Let's examine each of the elements of this objective.[7]

THEORY

As part of the objective of general-purpose financial reporting, an **entity perspective** is adopted. Companies are viewed as separate and distinct from their owners (present shareholders) using this perspective. The assets of incorporated entities such as companies listed on stock exchanges are viewed as assets of the company and not of a specific creditor or shareholder. Investors and creditors have claims on a company's assets in the form of equity or liability claims. The entity perspective is common today, because most companies that report their financial information have substance distinct from their investors (both shareholders and creditors). Thus, the perspective that financial reporting should be focused only on the needs of shareholders—often referred to as the **proprietary perspective**—is not considered appropriate.

As mentioned earlier, investors are interested in assessing (1) the company's ability to generate net cash inflows and (2) management's ability to protect and enhance the capital providers' investments. Financial reporting should therefore help investors assess the amounts, timing, and uncertainty of prospective cash inflows from dividends or interest, and the proceeds from the sale, redemption, or maturity of securities or loans. In order for investors to make these assessments, they must understand the economic resources of an enterprise, the claims to those resources, and the changes in them. Financial statements and related explanations should be a primary source for determining this information.

The emphasis on "assessing cash flow prospects" does not mean that the cash basis is preferred over the accrual basis of accounting. Information based on accrual accounting generally better indicates a company's present and future ability to generate favourable cash flows than does information limited to the financial effects of cash receipts and payments. Recall from your first accounting course the objective of **accrual-basis accounting**. It ensures that a company records events that change its financial statements in the periods in which the events occur, rather than only in the periods in which it receives or pays cash. Using the accrual basis to determine net income means that a company recognizes revenues when it provides the goods or services rather than when it receives cash. Similarly, it recognizes expenses when it incurs them rather than when it pays them. Under accrual accounting, a company generally recognizes revenues when it makes sales. The company can then relate the revenues to the economic environment of the period in which they occurred. Over the long run, trends in revenues and expenses are generally more meaningful than trends in cash receipts and disbursements.

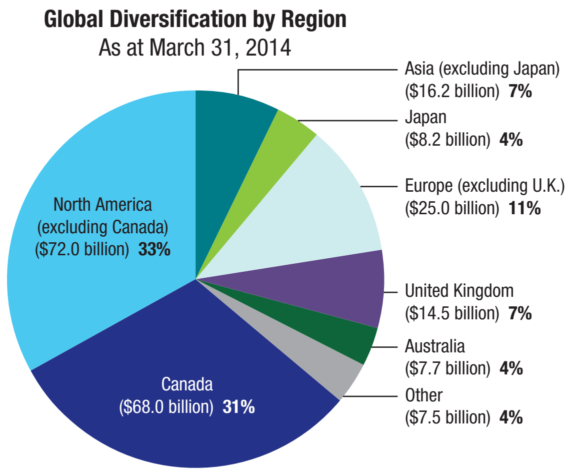
Providing information that is useful to users is a challenging task since they have **different needs and levels of knowledge**. **Institutional investors**,[8] such as the Canada Pension Plan, hold an increasing percentage of equity share holdings[9] and generally put a lot of their resources into managing their investment portfolios. Can those who prepare financial information therefore assume that the average individual investor has the same needs and knowledge level as an institutional investor when it comes to business and financial reporting? Likely not. We will discuss this issue further in Chapter 2.

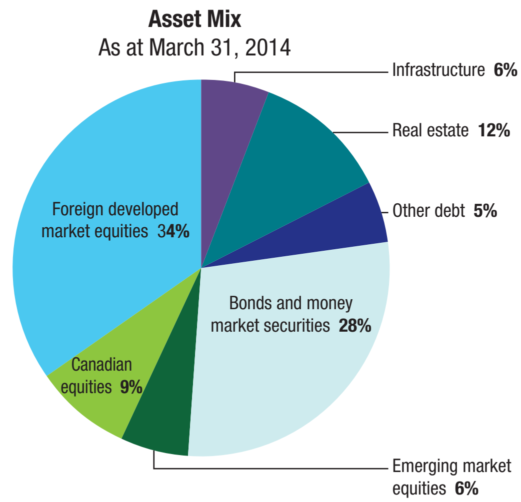
WHAT DO THE NUMBERS MEAN?

The Canada Pension Plan (CPP) is one of the top 10 largest retirement funds in the world according to its website. Over 18 million Canadians participate in the plan. The plan is managed by the Canada Pension Plan Investment Board (CPPIB), which decides how to invest the CPP funds. Its mandate is to "maximize returns without undue risk of loss."

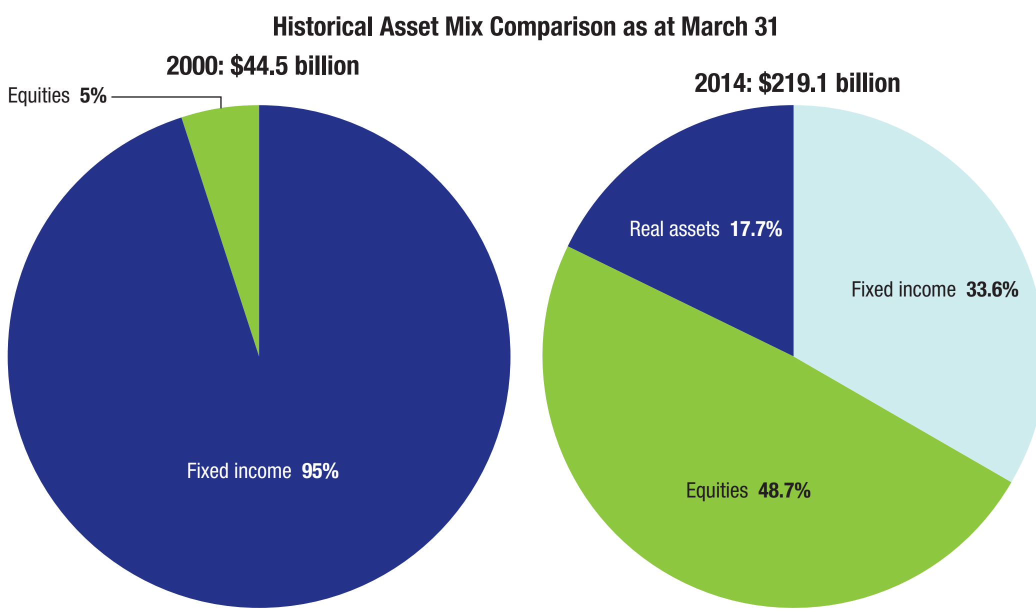
The chart below shows where the money is invested by region and then by type of asset.

REAL WORLD EMPHASIS





The fund stood at $219.1 billion as at March 31, 2014 and experienced a 16.5% rate of return for 2014. CPPIB had 1,000 full-time employees in 2014, many of whom are professionals, including accountants and lawyers. As you can see below, the composition of types of assets has shifted from primarily fixed income to primarily equities—shares in publicly traded corporations. As a large institutional investor with substantial equities holdings, the CPP is a significant stakeholder in how publicly traded companies report their financial information.



Information Asymmetry

Objective 4
Explain how information asymmetry and bias interfere with the objective of financial reporting.

Ideally, to facilitate the flow of capital in the most efficient and effective manner, all stakeholders should have equal access to all relevant information. In other words, there should be symmetry of access to information (**information symmetry**). This is nice in theory but it does not always work in practice. Management may feel that disclosure of too much