**Instructor’s Manual**

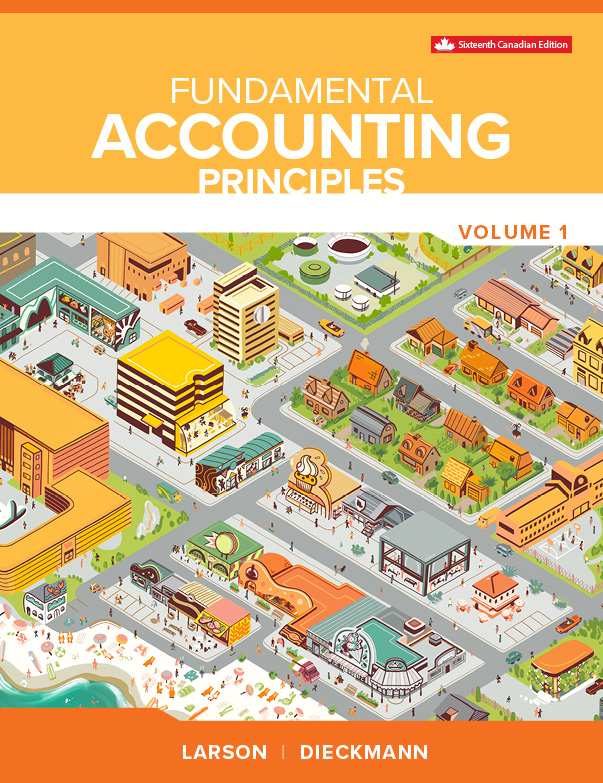
**to accompany**

***Fundamental Accounting Principles*,**

**Chapter 1,**

**16th Edition,**

**By Larson/Dieckmann**



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**CHAPTER 1**

Accounting IN BUSINESS

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| **Related Assignment Materials** | | | |
| Student Learning Objectives | Quick Studies | Exercises | Problems |
| 1. Describe the purpose and importance of accounting. | 1-1, 1-2. |  |  |
| 1. Describe forms of business organization. | 1-3, 1-4. | 1-1 | 1-1A, 1-1B. |
| 1. Identify users and uses of, and opportunities in accounting. | 1-5 | 1-2, 1-3. |  |
| 1. Explain why ethics and social responsibility are crucial to accounting. | 1-6 | 1-4 |  |
| 1. Identify, explain, and apply accounting principles. | 1-7, 1-8, 1-9, 1-15, 1-16, 1-17, 1-18. | 1-5, 1-17. | 1-8A, 1-8B. |
| 1. Identify and explain the content and reporting aims of financial statements. |  | 1-6, 1-7, 1-8, 1-9, 1-10, 1-11, 1-12, 1-13, 1-14, 1-15, 1-18, 1-19, 1-20, 1-22, 1-24. | 1-2A, 1-3A, 1-4A, 1-5A, 1-6A, 1-8A 1-2B, 1-3B, 1-4B, 1-5B, 1-6B, 1-8B. |
| 1. Analyze business transactions by applying the accounting equation. | 1-10, 1-11, 1-12, 1-13,1-14. | 1-15, 1-16 1-17, 1-18, 1-19, 1-20, , 1-22, 1-24. | 1-6A, 1-7A, 1-8A, 1-9A, P1-11A, 1-6B, 1-7B, 1-8B, 1-9B, 1-11B. |
| 1. Prepare financial statements reflecting business transactions. | 1-15,1-16,  1-17, 1-18. | 1-21, 1-23, 1-25. | 1-6A, 1-8A, 1-10A, 1-11A, 1-6B, 1-8B, 1-10B, 1-11B. |

| Learning Objective |
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| **What is Accounting (LO1)**  Accounting is at the heart of business. Accounting knowledge is a powerful tool. |
| 1. Power of Accounting Accounting *is* an information and measurement system that identifies, measures, records and communicates relevant, reliable, consistent and comparable information about an organization’s economic activities. | |
| 1. Focus of Accounting   Recordkeeping or bookkeeping is the recording of financial transactions, either manually or electronically, for the purpose of creating a reliable bank of data that is complete, neutral and free from error. Accounting *involves* the recordkeeping process but is much more. Accounting is also designing information systems to provide useful reports that monitor and control an organization’s activities. Decision makers must be able to interpret the information. | |
| Forms of Organization (LO2) | |
| Business Organization A business organization is one or more individuals selling products or services for profit. The three forms to be examined are: sole proprietorship, partnership and corporation. | |
| 1. *Sole Proprietorship –* a business owned by one person who is subject to unlimited liability. The business is not subject to an income tax but the owner is responsible for personal income tax on the profit of the entity.  2. *Partnership –* a business owned by two or more people, called partners, who aresubject to unlimited liability. The business is not subject to an income tax but the owners are responsible for personal income tax on the profit of the entity. | |
| 3. *Corporation* – a business that is a separate legal entity whose owner(s) is/are called shareholder(s). The owners have limited liability. The entity is responsible for a business income tax and the owner(s) are responsible for personal income tax on profits that are distributed to them in the form of dividends. | |
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| Users of Accounting Information (LO3) | |
| 1. External information users are those not directly involved in running the organization. Financial Accounting provides external reports called financial statements to help users analyze an organization’s activities. Generally Accepted Accounting Principles (GAAP) are the underlying concepts that make up acceptable accounting practices. GAAP in Canada follow International Financial Reporting Standards. (IFRS) | |
| 1. Internal information users are directly involved in managing and operating an organization. They include managers, officers, and other important internal decision-makers. The role of internal accounting is to help internal users improve efficiency and effectiveness of an organization in delivering products or services. | |
| Managerial accounting is aimed at serving decision making needs of internal users. Special purpose reports may be designed at any time by management accountants as a part of their role to serve internal users’ needs. These needs may vary over time.  Internal operating functions common to most organizations may include purchasing, production, human resources, distribution, marketing and research and development. | |
| Internal controls are procedures set up to protect assets and to ensure that accounting reports are free from error are neutral and complete. Accounting reports should promote efficiency and ensure that company polices are followed.  Accounting Opportunities   |  | | --- | | There are four broad fields in accounting, as well as accounting related fields. | | 1. *Financial Accounting* serves the needs of external users by providing financial statements, auditing, analysis and planning information. Forensic (criminal investigation) accounting also falls into this category.  2. *Managerial Accounting* serves the needs of internal users by providing special-purpose reports. | | Major managerial reporting areas include:  a. General Accounting  b. Cost Accounting  c. Budgeting  d. Internal Auditing  e. Management Consulting   1. *Taxation Accounting* involves preparation, planning, regulatory and investigational work and consulting in the tax field. 2. *Accounting-Related Opportunities* include lenders, consultants, managers planners and virtually any role in any segment of the economy in traditional or nontraditional roles. | |  | | *Professional Certification* In Canada, Chartered Professional Accountants of Canada **(CPA Canada)** is the national accounting organization certifying prospective students with a CPA designation. Students may prefer to take an alternative route, ACAF - the Advanced Certificate in Accounting and Finance. Visit <https://www.cpacanada.ca/en> for further information. | | |
| Ethics and Social Responsibility (LO4) | |
| A. Understanding Ethics—Ethics are beliefs that differentiate right from wrong and are sometimes referred to as accepted standards of good and bad behaviour. Ethics can often coincide with the law, with unethical behavior being illegal. | |
| 1. Accountants have ethical obligations in 4 primary areas. (high level of professional competence, confidentiality, personal integrity and objectivity). Good organizational ethics build trust, which promotes loyalty and long-term relationships with customers, suppliers and employees. Ethical practices complement an organization’s reputation.  2. Ethics are crucial in accounting if the information it provides is to be trusted. Codes of ethics for accountants are set up and enforced by provincial bodies. (CPA Canada and provincial bodies)  B. Social responsibility is a concern for the impact of our actions on society as a whole. Organizations need to identify issues, analyze options and make socially responsible decisions. | |
| Generally Accepted Accounting Principles (GAAP) (LO5)  |  | | --- | | The underlying concepts that make acceptable accounting practices are referred to as Generally Accepted Accounting Principles (GAAP). The responsibility for standard setting in Canada has changed because of the adoption of IFRS. To improve the comparability of accounting information, the International Accounting Standards Board, (IASB) was established to find a common set of accounting standards, (IFRS) which could be used globally. The ultimate goal of the IASB is to have all countries use IFRS. The Accounting Standards Board (AcSB) has developed Accounting Standards for Private Enterprise (ASPE) for use in Canada.  Primary purpose of GAAP is to ensure usefulness of financial information. | | Fundamental Building Blocks of Accounting Include both general and specific principles which are discussed throughout the book. The principles discussed in this chapter are: | | 1. *Business entity principle*—every business is to be accounted for separately and distinctly from its owner or owners. 2. *Cost constraint—*all transactions are recorded based on actual cash amount received or paid. A cash-equivalent amount may be given in the absence of cash. 3. *Going-concern assumption*—financial statements are to reflect the assumption that the business will continue operating instead of being closed or sold, unless evidence shows that it will not continue. 4. *Currency*—transactions and events must be expressed in monetary, or money, units which is generally the currency in which it operates. Accounting assumes a stable monetary unit, meaning that no adjustments are made to account for inflation or currency value changes. 5. *Revenue recognition principle—*revenue is recognized at the time it is earned regardless of whether cash or another asset has been exchanged. The amount of revenue should be measured as the cash plus the cash equivalent (market value) of any other assets received. 6. *Measurement –* identifies four (4) key methods for recording financial transactions as follows: historical cost, current cost, realizable value and present value*.* | | | | |
| Communicating Through Financial Statements (LO6)  |  | | --- | | Financial statements are an organization’s primary means of financial communication and are the result of a process, or cycle, that begins with a business transaction like a sale. There are four major financial statements – the income statement, statement of changes in equity, balance sheet and the statement of cash flows. | | 1. An income statement (statement of profit or loss) reports all revenues earned less all expenses incurred by a business over a period of time. Revenues are the value of assets exchanged for products and services provided to customers as part of a business’s main operations. Expenses reflect the using up of assets or the incurrence of liabilities that result in decreases in equity (other than direct distributions to owners or shareholders). 2. Statement of Changes in Equity reports on changes in equity over the reporting period. This statement starts with beginning equity and adjusts it for transactions that (a) increase it (investments by the owner and profit), and (b) decrease it (owner withdrawals and losses). 3. The balance sheet, or statement of financial position, reports the financial position of a business at a point in time, usually at the end of a month or year. Assets are the properties or economic resources controlled by a business as a result of past events. Liabilities are debts or obligations of a business to transfer cash or another economic resource as a result of past events. Equity is the owner’s claim on the assets of a business. It represents the assets that remain after deducting liabilities, also called net assets. 4. The statement of cash flows describes the sources and uses of cash for a reporting period. It also reports the amount of cash at both the beginning and the end of a period. The statement of cash flows is organized by a company’s major activities: operating, investing, and financing. | | |
| The Accounting Equation (LO7) Investing=Financing. Accounting equation is also called the balance sheet equation. It shows how the assets, liabilities and equity of an entity are related. Equal amounts of investment and financing have to occur in order for the accounting equation to remain balanced. Point out that this is the fundamental equation that will be referred to in all accounting related courses in their careers.  Transaction analysis is begun in this section. It is very important to stress to students at this point that ultimately everything will “balance out.” Students find some of the technical terminology to be difficult as well. With the continued use of technology, it is a good time to point out that a fundamental understanding of what is going on in transaction analysis will improve the students’ ability to comprehend more complex accounting in later courses/careers.  Demonstration of a complete problem is essential here to reinforce the concept of balancing. Be sure to point out the different transactions such as: (not a complete list)   1. Assets increase and equity increases 2. One asset increases and another asset decreases. 3. Assets increase and liabilities increase.   Using the transaction analysis sheet here is great at getting students started. However, they often want to include equity in every transaction. Point out that equity only increases in 2 circumstances (investment and revenue) and decreases in 2 circumstances (expense and withdrawal). | |
| Financial Statements (LO8)  |  | | --- | | Financial Statements are prepared from transaction analysis in the following order using the procedure indicated: | | * 1. Income Statement – information about revenues and expenses is taken from the equity column. Total revenues minus total expenses equals profit or loss. Notice withdrawals and investments are not part of measuring profit or loss. (This is a very common mistake for students at this point.) | | * 1. Statement of changes in equity -- the beginning equity is taken from the equity column and any investments of owner showed in this column are added. The profit, from the income statement is added (or the loss is subtracted) and finally the owner’s withdrawals, which are found in the equity column, are subtracted to arrive at the ending capital. (Point out that balance is already known from the transaction sheet.) | | * 1. Balance Sheet -- the ending balance of each asset is listed and the total of this listing equals total assets. The ending balance of each liability is listed and the total of this listing equals total liabilities. The ending capital, taken from the statement of changes in equity, is listed and added to total liabilities to get total liabilities and equity. Both sides of the accounting equation must equal. | | |
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