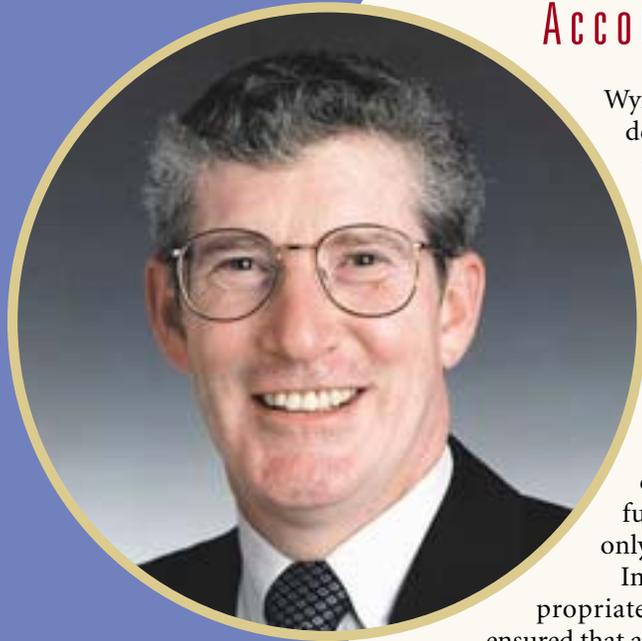


# Accounting: The Key to Success

## Accounting Leads the Way



Wynne Powell is an accounting professional. He is also president and CEO of London Drugs, a business that has millions of dollars in revenues annually and a staff of approximately 6,000. It's a highly stressful position, he admits, but Wynne finds it stimulating. The excitement is in making things happen: taking money and making it grow, providing a return to the owners. "It's like a chess game; somebody makes a move and you carefully develop and adjust your strategy, positioning yourself for the win. It's fun!"

How do you make sure you win in business? According to Wynne, it's pretty basic: you need a thorough understanding of accounting figures; that's what allows a company to fail or flourish. The management team must fully understand how financial information is created; it's only then that they can use it to their advantage.

In Wynne's opinion, businesses begin to fail because of inappropriate or late financial figures. Advances in technology have ensured that accounting information can be available on a real-time basis. Technology has also triggered the evolution of a new breed of accountant whose focus has expanded to every aspect of the business in every corner of the world.

"Accounting knowledge is the key," says Wynne Powell. "It is the *'language of business'* and as such is fundamental to your success in the business world." Accounting leads the way.



## Learning Objectives

- LO<sup>1</sup> Describe accounting and its goals and uses.
- LO<sup>2</sup> Describe forms of business organizations.
- LO<sup>3</sup> Identify users and uses of accounting.
- LO<sup>4</sup> Explain why ethics and social responsibility are crucial to accounting.
- LO<sup>5</sup> Describe how technology is changing accounting.
- LO<sup>6</sup> Identify opportunities in accounting and related fields.
- \*LO<sup>7</sup> Describe the codes of ethics and professional conduct for accountants.

\*APPENDIX 1A

\* An asterisk (\*) identifies appendix material.

## Chapter Preview

A Chapter Preview introduces the importance and relevance of the material, and also links these materials to the opening article to motivate you, the reader.

Accounting is at the heart of business: accounting information pulsates throughout an organization, feeding decision makers with details needed to give them an edge over competitors. Because of new technologies, the increasing speed and quantity of information available makes the task for accountants like Wynne Powell an ever-increasing challenge. Decision makers like Wynne cannot rely on hunches and guesses. Decision makers depend on their knowledge of accounting principles and practices to help identify and take advantage of opportunities discovered from reviewing large volumes of information. Through your studies of this book, you will learn about many of the accounting concepts, procedures, and analyses common to both small and large businesses. This knowledge will provide you with the basics necessary to make better business decisions.

This first chapter serves a dual role. First, it introduces the subject of accounting. It describes accounting, the users and uses of accounting information, the importance of ethics and social responsibility, and opportunities in accounting. This chapter provides a foundation for those students who have little or no understanding of business or the role of accounting in business. Chapter 2 will build on this foundation by focusing on transactions and financial statements.

Chapter 1 also introduces you to each of the learning features found in most chapters. For example, immediately to the left of the first paragraph above is an explanation of purpose regarding the Chapter Preview, and two additional features are described in the lower left margin. Some of the features refer to the “OLC,” the Online Learning Centre, located on the Web at [www.mcgrawhill.ca/college/larson](http://www.mcgrawhill.ca/college/larson). Take the time in this chapter to explore and learn the value of these additional resources.

## What is Accounting?

Accounting knowledge is a powerful tool; it is your key to success, according to Wynne Powell. How does accounting knowledge give you power? What exactly is the focus of accounting? This section answers these fundamental questions.

## Power of Accounting

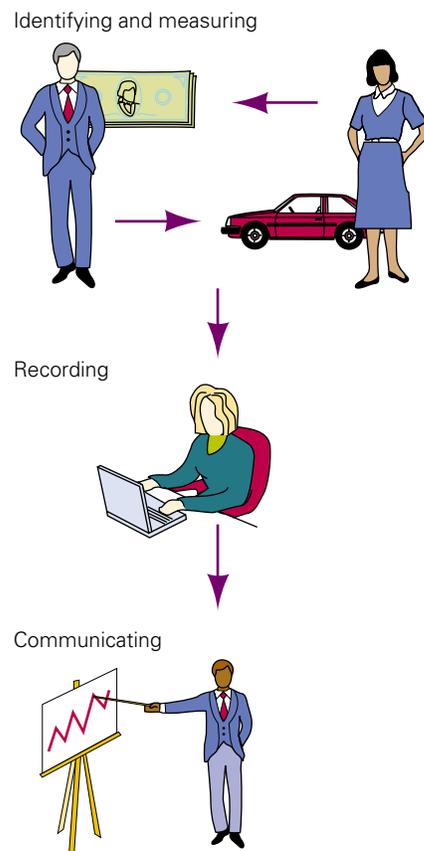
**Accounting** is an information system that identifies, measures, records and communicates relevant, reliable, consistent and comparable information about an organization’s economic activities, as shown in Exhibit 1.1. Its objective is to help people make better decisions. It also helps people better assess opportunities, products, investments, and social and community responsibilities. In addition to reporting on the performance of a business, what the business owns, and what it owes, accounting opens our eyes to new and exciting possibilities.

Boldfaced words or phrases represent new terminology that is explained here and defined in the glossary at the end of the chapter.

LO<sup>1</sup>

Describe accounting and its goals and uses.

Each chapter is separated into chunks of information called learning objectives (LO). Each LO tells you what needs to be mastered in that section of reading.



## Exhibit 1.1

## Accounting Activities

Exhibits aid in visual learning of key accounting and business topics.

This feature relates the theory to a real-life situation.

### Power of Accounting Information in Small Business

Pete Seerden, owner of ECOF, used to pay thousands of dollars annually in renting warehouse space for his cabinet-making business. "Rent payments were eating into my profits big time. I looked at alternatives and crunched some numbers. I ended up buying my own warehouse. I knew that I was increasing my risk but the upside was that the money I used to pay for rent was now paying for my building. Now, I've expanded my warehouse and am renting a part of it to somebody else."

*Pete Seerden is not an accountant but was able to use his knowledge of accounting information to make a successful business decision.*

### Power of Accounting Information in Big Business

The Toronto-Dominion (TD) Bank teamed up with Starbucks to create an innovative customer experience. The TD Bank became the first major Canadian bank to combine banking with the services of a retailer in one of its branches. In the TD Bank branch at Queen and Bay Streets in downtown Toronto, you can purchase Starbucks products while doing your banking.

*This innovative decision was made through an analysis of information from a variety of sources including the accounting information system. By increasing customer exposure for both parties, profits should be positively affected.*

Did You Know? 

Accounting can provide you with important and interesting learning experiences. You will acquire knowledge and skills that will help you in both business and everyday life. For example, you can use accounting knowledge to make better investment decisions or to help you get a loan for a house.

## Focus of Accounting

Accounting affects many parts of life. Some examples of common contacts with accounting are through credit approvals, chequing accounts, tax forms, and payroll. These experiences are limited and tend to focus on the *recordkeeping* (or *bookkeeping*) parts of accounting. **Recordkeeping**, or **bookkeeping**, is the recording of financial transactions and events, either manually or electronically, for the purpose of creating a reliable bank of data. Accounting *involves* the recordkeeping process but is *much* more.

Accounting also involves designing information systems to provide useful reports to monitor and control an organization's activities. In order to use the reports effectively, decision makers must be able to interpret the information. The skills needed to understand and interpret accounting information come from an insight into each aspect of accounting, including recordkeeping. Because accounting is part of so much that we do in business and our everyday lives, you can enjoy greater opportunities if you understand and are able to use accounting information effectively.

A series of Flashback questions in the chapter reinforces the immediately preceding materials. It gives you feedback on your comprehension before going on to new topics.



Answers—p. 20

1. What is the major objective of accounting?
2. Distinguish between accounting and recordkeeping.

## Forms of Organization

A **business** is one or more individuals selling products or services for profit. Products like athletic apparel (CCM, Bauer, NIKE, Reebok), computers (Dell, Hewlett-Packard, Apple) and clothing (Tilley, Levis, GAP) are part of our daily lives. Services like information communication (Sympatico, AOL Canada, CompuServe, Microsoft), dining (Tim Hortons, Harvey's, McDonald's, Burger King) and car rental (Tilden, Hertz, Budget) make our lives easier. A business can be as small as an in-home childcare service or as large as the Hudson's Bay Company. Nearly 100,000 new businesses are started in Canada each year, with most of them being founded by people who want freedom from ordinary jobs, a new challenge in life, or the advantage of earning extra money.

Most organizations engage in economic activities, such as the business activities of purchasing materials and labour, and selling products and services. They can also involve activities for non-business organizations, more commonly referred to as not-for-profit organizations, such as government, schools, and churches. A common feature in all organizations, both business and non-business, is the power and use of accounting.

## Business Organizations

Businesses take one of three forms: sole proprietorship, partnership, or corporation. For some of the characteristics of each business form, see Exhibit 1.2.

**LO<sup>2</sup>** Describe forms of business organizations.

	Sole Proprietorship	Partnership	Corporation
Business entity	yes	yes	yes
Legal entity	no	no	yes
Limited liability	no	no	yes
Unlimited life	no	no	yes
Business taxed	no	no	yes
One owner allowed	yes	no	yes

## Exhibit 1.2

Characteristics of Business  
Organizations**Sole Proprietorship**

A **sole proprietorship**, or **single proprietorship**, is a business owned by one person. No special legal requirements must be met in order to start this form of business, other than to file for a business licence and register the business name. While it is a separate entity<sup>1</sup> for accounting purposes, it is *not* a separate legal entity from its owner. This means, for example, that a court can order an owner to sell personal belongings to pay a proprietorship's debt. An owner is even responsible for debts that are greater than the resources of the proprietorship; this is known as **unlimited liability**, and is an obvious disadvantage of a sole proprietorship. Because tax authorities do not separate a proprietorship from its owner, the profits of the business are reported and taxed on the owner's personal income tax return. Small retail stores and service businesses often are organized as proprietorships.

**Partnership**

A **partnership** is owned by two or more persons called *partners*. Like a proprietorship, no special legal requirements must be met in order to start a partnership, other than to register the business name and obtain a business licence. To run the business together, the partners need an oral or written agreement that usually indicates how profits and losses are to be shared. A partnership, like a proprietorship, is not legally separate from its owners, therefore each partner's share of profits is reported and taxed on that partner's tax return. Partners are usually subject to *unlimited liability*.

There are two types of partnerships that limit liability. A **limited partnership** includes a general partner(s) with unlimited liability and a limited partner(s) with liability restricted to the amount invested. A **limited liability partnership** restricts partners' liabilities to their own acts and the acts of individuals under their control. This protects an innocent partner from the negligence of another partner, yet all partners remain responsible for partnership debts.

**Corporation**

A **corporation** is a business that is a separate legal entity chartered (or *incorporated*) under provincial or federal laws. A corporation is responsible for its own acts and its own debts. It can enter into its own contracts, and it can buy, own, and sell property. It can also sue and be sued. Not only does separate legal status give a corporation an unlimited life, but it also entitles the corporation to conduct business with the rights, duties, and responsibilities of a person. As a result, a corporation files a tax return and pays tax on its profits. A corporation acts through its

<sup>1</sup> The **business entity principle**, is one of a group of accounting rules, the **Generally Accepted Accounting Principles (GAAP)**, which are discussed in detail in Chapter 2. This principle states that each economic entity or business of the owner must keep accounting records and reports separate from the owner and any other economic entity of the owner.

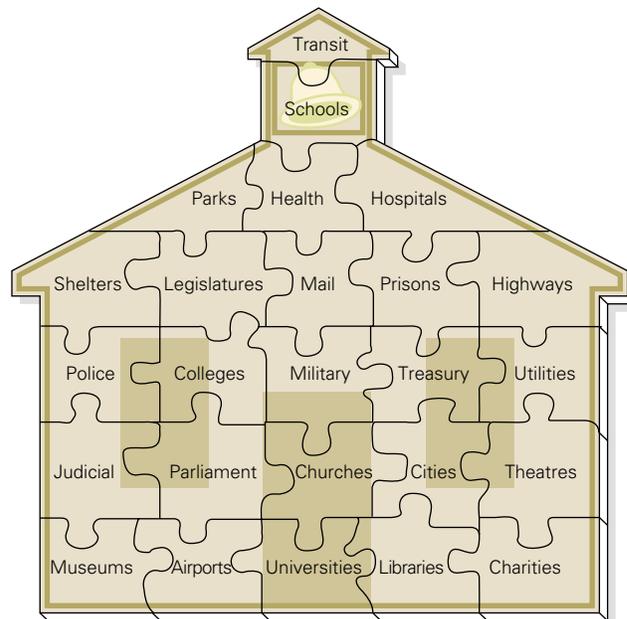
managers, who are its legal agents. Separate legal status also means that the shareholders are not personally liable for corporate acts and debts. Shareholders are legally distinct from the business and their loss is limited to what they invested. This **limited liability** is a key to why corporations can raise resources from shareholders who are not active in managing the business. Ownership, or equity, of all corporations is divided into units called **shares**. Owners of shares are called **shareholders** (the American term for shares is *stock* and for shareholders, *stockholders*). A shareholder can sell or transfer shares to another person without affecting the operations of a corporation. When a corporation issues (or sells) only one class of shares, we call them **common shares**. Air Canada is an example of a Canadian corporation. As of December 31, 2002, Air Canada had issued a total of 79 million common shares to the public. This means that Air Canada's ownership is divided into 79 million units. A shareholder who owns 790,000 shares of Air Canada owns 1% of the company.

## Non-Business Organizations

Non-business organizations plan and operate not for profit but rather for other goals such as health, education, religious services, and cultural and social activities. Examples are public schools meeting the needs of citizens, and community care groups meeting the needs of the poor. Non-business organizations do not have an identifiable owner. Still, the demand for accounting information in these organizations is high since they are accountable to their sponsors. These organizations are accountable to taxpayers, donors, lenders, legislators, regulators and other constituents. Exhibit 1.3 lists a wide range of government and not-for-profit organizations that are affected by the power of accounting. This list is but a sampling of the roughly one-third of Canadian economic activity done by this type of organization. In all of these organizations, accounting captures key information about their activities and makes it available to users both internal and external to the organization.

### Exhibit 1.3

Partial List of Government and Not-for-Profit Organizations



**Entrepreneur**

You and a friend have developed a new design for mountain bikes that improves speed and performance by a remarkable 25% to 40%. You are planning to form a small business to manufacture and market these bikes. You and your friend are concerned about potential lawsuits from individuals who may become injured because of using the speed feature of the bikes with reckless abandon. What form of organization do you set up?

**Judgement Call**

Answer—p. 19

The Judgement Call feature requires you to make accounting and business decisions. It uses role-playing to show the interaction of judgement, the need for business awareness, and the impact of decisions.

3. What are the three common forms of business organizations?
4. Identify examples of non-business organizations.



Answers—p. 20

All chapters have a mid-chapter and end-of-chapter demonstration problem to illustrate and reinforce important topics.

**Mid-Chapter Demonstration Problem**

For each of the following independent situations, identify which type of business organization is being described (sole proprietorship, partnership, or corporation).

- a. \_\_\_\_\_ The owners of JenStar can sell or transfer their ownership to another person without affecting the operations of the business.
- b. \_\_\_\_\_ The 28 owners of InterIsland Tours each have 15,000 shares.
- c. \_\_\_\_\_ Jan Wallace and Roth Winters are subject to unlimited liability in their business.
- d. \_\_\_\_\_ Willis Corsairs is responsible for debts that are greater than the resources of his business.
- e. \_\_\_\_\_ The profits of Perth's Financial Consulting are reported and taxed on the personal tax return of Wytte Perth, the owner.

**SOLUTION TO Mid-Chapter Demonstration Problem**

- a. Corporation
- b. Corporation
- c. Partnership
- d. Sole proprietorship
- e. Sole proprietorship

## Users of Accounting Information



Identify users and uses of accounting.

Accounting is a service activity that serves the decision-making needs of *external* and *internal* users.

### External Information Users

**External users** of accounting information are *not* directly involved in running the organization. They include shareholders, lenders, directors, customers, suppliers, regulators, lawyers, brokers, and the press. Each external user has special information needs that depend on the kind of decision to be made. To make a decision, key questions need to be answered; this is often done using information available in accounting reports. The following table identifies several external users and decisions that require accounting information.

External User Group	Examples of Decisions to be Made	Questions That Require Accounting Information
Lenders (creditors) lend money or other resources to an organization	To lend money or not	Can current loans be repaid? Can additional loans be repaid? What is the future profit outlook?
Shareholders are the owners of a corporation	To invest or not	What is net income for current and past periods? Do loans seem large or unusual? Do expenses fit the level and type of revenues?
External auditors examine financial statements and provide assurance that they are prepared according to GAAP	To determine the reasonableness of a client's statements	Have all expenses been recorded? Do revenues include only those for the current period?
Employees of an organization, or their union representatives	To determine if wages are fair	Is net income large enough to support a request for increased pay?
Regulators, such as Canada Customs and Revenue Agency ( <b>CCRA</b> )*	To determine if payroll deductions are calculated properly	Are all employees being paid through the payroll system?
Others <ul style="list-style-type: none"> <li>Contributors to not-for-profit organizations</li> <li>Suppliers</li> </ul>	To continue financial support of the organization  To determine if goods should be supplied on credit	Are funds being spent in an appropriate manner?  Is the purchaser able to pay for goods purchased?

\*CCRA was formerly known as Revenue Canada.

### External Reporting

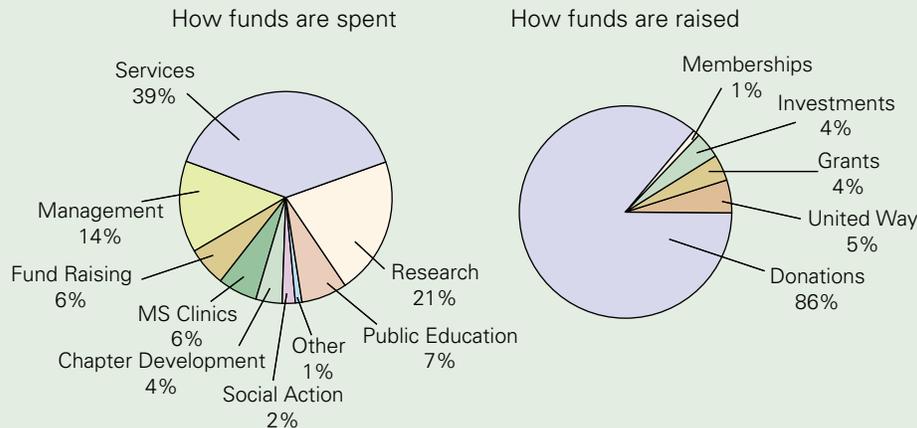
**Financial accounting** is the area of accounting aimed at serving external users. Its primary objective is to provide external reports called *financial statements* to help users analyze an organization's activities. Because external users have limited access to an organization's information, their own success depends on getting external reports that are reliable, relevant, consistent, and comparable. Some governmental and regulatory agencies have the power to get reports in specific forms, but most external users must rely on *general-purpose financial statements*. The term *general-purpose* refers to the broad range of purposes for which external

users rely on these statements. *Generally Accepted Accounting Principles (GAAP)* are important in increasing the usefulness of financial statements to users. We discuss these principles along with the financial statements in Chapter 2.

### Accounting Information at Work

The Multiple Sclerosis (MS) Society of Canada provides assistance and support to individuals with MS, in addition to funding research aimed at finding a cure. Accounting makes it possible for not-for-profit organizations like the MS Society of Canada to present to external users information like the following:

Did You Know? 



SOURCE: [www.mssoc.ca](http://www.mssoc.ca).

## Internal Information Users

**Internal users** of accounting information are those individuals directly involved in managing and operating an organization. The internal role of accounting is to provide information to help internal users improve the efficiency and effectiveness of an organization in delivering products or services.

For example, Kathy Silver, HR Manager Recruitment, Training, and Policy of Shell Canada, says about the role of accounting in the human resources area: “As an HR person, I am often involved in developing proposals for HR initiatives in order to positively affect the company’s profitability. In order to get management to support these proposals, I have to be able to clearly demonstrate in financial accounting terms how the proposed HR activities will impact the bottom line and contribute to business success. In today’s tough competitive business environment, it is critical that HR professionals have an understanding of financial accounting and are able to speak intelligently about financial issues. Otherwise, they have very little credibility with internal business clients and will have difficulty making a valuable contribution. In addition, HR functions must be managed like any other business and this requires a knowledge of financial accounting; the training department must account for all its expenses and revenues; the payroll department must book all the accounting entries for salaries and tax deductions; the pension and benefits department must be able to book accounting entries for benefits and pensions; the recruitment department must account for their recruitment expenses. And all HR departments must manage to a budget and explain variances. HR is not just about people. It is about business and finance and how people can contribute towards business goals. Those who grasp this concept will be much more marketable in the workplace.”

### Internal Reporting

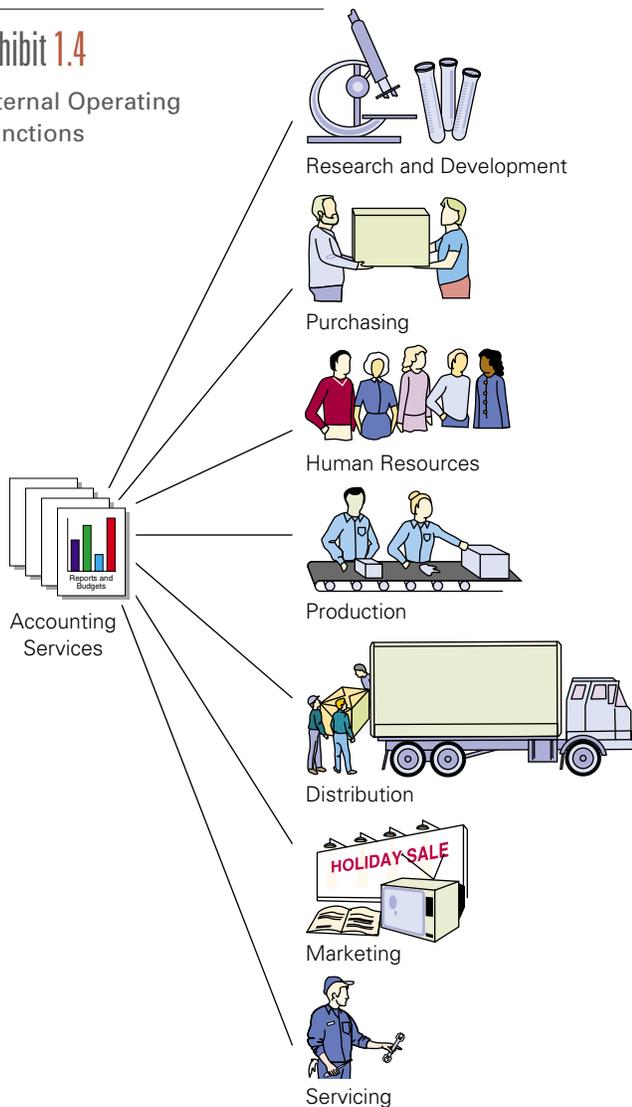
**Managerial accounting** is the area of accounting aimed at serving the decision-making needs of internal users. Managerial accounting provides special-purpose reports customized to meet the information needs of internal users. An example of such a report is a listing of credit customers who are late in paying their accounts. Internal reports aim to answer questions such as:

- What are the manufacturing expenses per unit of product?
- What is the most profitable mix of services?
- What level of revenues is necessary to show net income?
- Which service activities are most profitable?
- Which expenses change with a change in revenues?

This book will help you to learn the skills needed to use accounting information effectively to answer questions like these.

### Exhibit 1.4

#### Internal Operating Functions



### Internal Operating Functions

The responsibilities and duties of internal users extend to every function of an organization. There are at least seven functions common to most organizations, as shown in Exhibit 1.4, and accounting is essential to the smooth operation of each.

Allan Watt, Vice-President Marketing and Communications of the Edmonton Oilers Hockey Club, emphasizes the internal role of accounting: “We don’t market anything until we look at the numbers. Business is based on accounting information and if any member of our team is unable to demystify and use the numbers, they can’t add value to the process. Accounting numbers dictate absolutely everything that we do in marketing. You can’t get past the breakeven point unless you can prepare, read, and stick to a numbers plan. We could win all sorts of marketing awards if we could spend what we wanted; but we can’t because it has to make sense in terms of the bottom line. How do you know if it makes sense or not unless you understand accounting?”

Managers rely on *internal controls* to monitor operating functions. **Internal controls** are procedures set up to protect assets (like cash, equipment, and buildings), ensure that accounting reports are reliable, promote efficiency, and ensure that company policies are followed. For example, certain actions require verification, such as a manager’s approval before materials enter production. Internal controls are crucial if accounting reports are to provide relevant and reliable information.

## Ethics and Social Responsibility

Ethics and ethical behaviour are important to the accounting profession and to those who use accounting information. We are reminded of this when we find stories in the media of cheating, or when we witness wrongful actions by individuals in business. A lack of ethics makes it harder for people to trust one another. If trust is missing, our lives are more difficult, inefficient and unpleasant. An important goal of accounting is to provide useful information for decision making. For information to be useful, it must be trusted; this demands ethics in accounting. Closely related to ethics is social responsibility. Both are discussed in this section.

### Understanding Ethics

**Ethics** are beliefs that differentiate right from wrong. Ethics and laws often coincide, with the result that many unethical actions (such as theft and physical violence) are also illegal. Yet other actions are not against the law but are considered unethical, such as not helping people with certain needs or deliberately withholding critical information from the user.

Identifying the ethical path is sometimes difficult. The preferred ethical path is to take a course of action that avoids casting doubt on one's decision. For example, as a member of the board for a not-for-profit organization, you are involved in a decision where your brother's company could win a profitable contract to do work for the organization ... do you participate in the decision or do you remove yourself from the discussion? The ethical answer would be to avoid this conflict of interest by not participating. Accountants have ethical obligations in at least four general areas: they are expected to maintain a high level of professional competence, treat sensitive information as confidential, exercise personal integrity, and be objective in matters of financial disclosure.

**LO<sup>4</sup>** Explain why ethics and social responsibility are crucial to accounting.

#### Extend Your Knowledge



1-1

This mouse icon appears when more information about a topic can be found on the Online Learning Centre accompanying this text. Go to [www.mcgrawhill.ca/college/larson](http://www.mcgrawhill.ca/college/larson) to find out more.

#### Ethics are Timeless

The Rotary 4-Way Test, created by Herbert J. Taylor in 1932, is an internationally renowned guideline for making ethical business choices:

"Of the things we think, say or do:

1. Is it the Truth?
2. Is it Fair to all concerned?
3. Will it build goodwill and better friendships?
4. Will it be beneficial to all concerned?"

SOURCE: [www.rotary.org](http://www.rotary.org), accessed March 3, 2003. ©Rotary International. Used with permission.

<http://www.rotary.org>

Did You Know? 



### Organizational Ethics

Organizational ethics are likely learned through management example and leadership. Companies like Shell Canada, The Body Shop, and Royal Bank of Canada work hard to convey the importance of ethics to employees. For example, Shell Canada's code of ethics states that:

“Shell Canada's reputation and credibility are based upon its total commitment to ethical business practices. To safeguard the Shell reputation, employees must conduct themselves in accordance with the highest ethical standards and also be perceived to be acting ethical at all times.”

SOURCE: [www.shell.ca/code/values/commitments/ethics.html](http://www.shell.ca/code/values/commitments/ethics.html)

Ethical practices build trust, which promotes loyalty and long-term relationships with customers, suppliers and employees. Good ethics add to an organization's reputation and its success.



### Did You Know?

#### Bre-X: Organizational Ethics?

Alberta-based mining company Bre-X came into being in 1993, when John Felderhof, a well-known geologist, convinced capital share promoter David Walsh to invest in the Busang mine located in Indonesia. Previous explorations of Busang performed by larger mining companies indicated that it wasn't worth mining. But Bre-X shares were skyrocketing by December 1993, when the company was reporting gold at levels of up to 5.68 grams per tonne—translating into the world's biggest gold find, worth over \$70 billion at today's gold price. But by 1997, Bre-X shareholders were left with nothing after a series of events: a company official committed suicide by throwing himself out of a helicopter; geology reports were destroyed in a mysterious fire; an independent core sample showed gold of 0.06 grams per tonne, bringing into serious question the integrity of the original reports; and millions of dollars were missing.

### Accounting Ethics

Ethics are crucial in accounting. Providers of accounting information often face ethical choices as they prepare financial reports. Their choices can affect both the use and receipt of money, including taxes owed and money shared with owners. Accounting information can affect the price that a buyer pays and the wages paid to workers. It can even affect the success of products, services, and divisions. Misleading information can lead to a wrongful closing of a division, causing workers, customers, and suppliers to be seriously harmed.

Because of the importance of accounting ethics, codes of ethics for accountants are set up and enforced. These codes include those of the Provincial Certified General Accountants' Associations, the Provincial Societies of Management Accountants, and the Provincial Institutes of Chartered Accountants. Samples from these codes are presented in Appendix 1A to this chapter. These codes can be of help when one confronts ethical dilemmas.

Ethics codes are also useful when one is dealing with confidential information. For example, auditors have access to confidential salaries and an organization's strategies. Organizations can be harmed if auditors pass this information to others. To prevent this, auditors' ethics codes require them to keep information confidential. Internal accountants are also not to use confidential information for personal gain.

**Livent: Canada's Enron?**

In October 2002, the RCMP charged Garth Drabinsky and Myron Gottlieb—co-founders of Livent, a once very successful theatre company in Toronto—with 19 counts each of fraud regarding the business's accounting records. The RCMP alleges that Drabinsky and Gottlieb defrauded creditors and private and public investors of about \$500 million between December 14, 1989, and June 23, 1998. The case is still before the courts.

SOURCE: [http://cbc.ca/storyview/CBC/2002/10/22/livent\\_021022](http://cbc.ca/storyview/CBC/2002/10/22/livent_021022)

Did You Know?

**Ethical Challenge**

In our lives, we encounter many situations requiring ethical decisions. We need to remember that accounting must be practised ethically if it is to be useful, and must always ensure that our actions and decisions are ethical.

**Social Responsibility**

**Social responsibility** is a concern for the impact of our actions on society as a whole. It requires that an organization:

1. identify issues,
2. analyze options, and
3. make socially responsible decisions.

Socially conscious employees, customers, investors, and others see to it that organizations follow claims of social awareness with action, by placing significant pressure on organizations to contribute positively to society. Organizations like RBC Financial Group take social responsibility seriously. For the past several years, *The Globe and Mail's* 'Most Respected' poll has named RBC Financial Group (the Royal Bank) as the top Canadian corporation in terms of its corporate social responsibility involving charitable giving, employee volunteerism, sponsorships, community involvement, and ethical business practices. RBC has also maintained top standing in terms of financial performance, reinforcing the potential benefits of social responsibility.

5. What is the difference between external and internal users of accounting information?
6. Why are internal controls important?
7. What are the guidelines to use in making ethical and socially responsible decisions?
8. Why are ethics and social responsibility valuable to organizations?
9. Why are ethics crucial to accounting?



Answers—p. 20

**Technology: Creating Change in Accounting**

"The world is shrinking"... "a global economy"... both expressions are rooted in the advancement of communication and information technologies. Technology allows instant access to services, data, and news, as well as financial and non-financial information to aid business operations. For example, if a marine shop on the west coast requires a special part that is manufactured in Ontario, the



Describe how technology is changing accounting.

order can be placed by phone, fax, or e-mail, with the part conceivably being delivered by courier the next working day.

New forms of communication and resultant access to data have created an information superhighway that is redefining business communication. Global computer networks and telecommunications equipment allow access to all types of business information at the press of a button. Knowledge of the system is necessary in order to take advantage of opportunities available as a result of this information.

Over the past several years, demands on the accounting profession and businesspeople in general have expanded considerably because of technology. Spreadsheet and accounting software application skills are now essential. The need for decision makers at all levels to enhance their information technology (IT) knowledge and experience is growing because of new developments such as e-commerce.

Knowing how to utilize the new technologies increases job opportunities.

In the 1990s (1990 to 1999), the seasonally adjusted growth rate for all jobs in Canada was 10.6%. The seasonally adjusted growth rate for jobs in the sector that includes professional and technical services was 57.9% over the same period.

SOURCE: Statistics Canada Cat. No. 71-201-XPB.

This increased employment opportunity is driven by the growing need for individuals with the ability to understand and process information. It is this skill—the understanding and processing of information—which is the core of accounting. This skill will allow you to speak the language of business: accounting.

## Accounting Opportunities

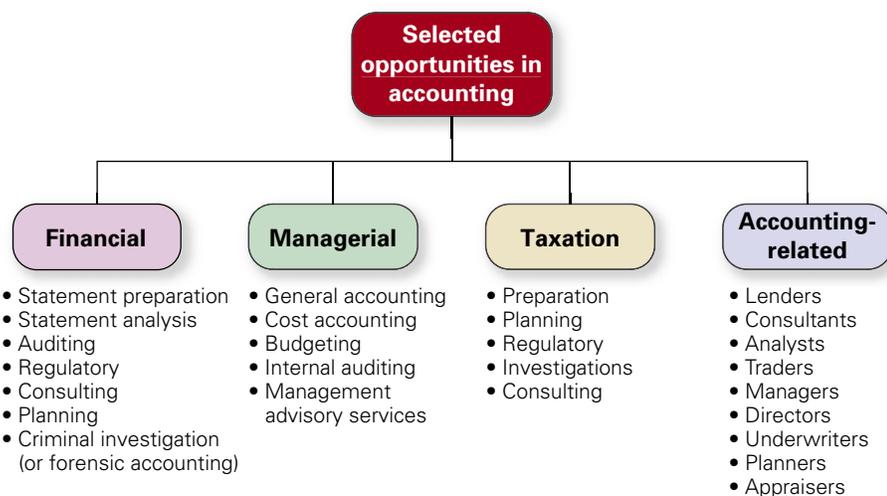
**LO<sup>6</sup>** Identify opportunities in accounting and related fields.

Exhibit 1.5 identifies the countless job opportunities in accounting by classifying accountants according to the kind of work that they perform. In general, accountants work in four broad fields:

- Financial
- Managerial
- Taxation
- Accounting-related

### Exhibit 1.5

Opportunities in Practice



Another way to classify accountants is to identify the kinds of organizations in which they work. Most accountants are **private accountants** and work for a single employer, which is often a business. The services of **public accountants** are available to the public, which means that services are provided to many different clients. **Government accountants** work for local, provincial, and federal government agencies. Exhibit 1.6 shows the average annual salaries for various accounting groups.

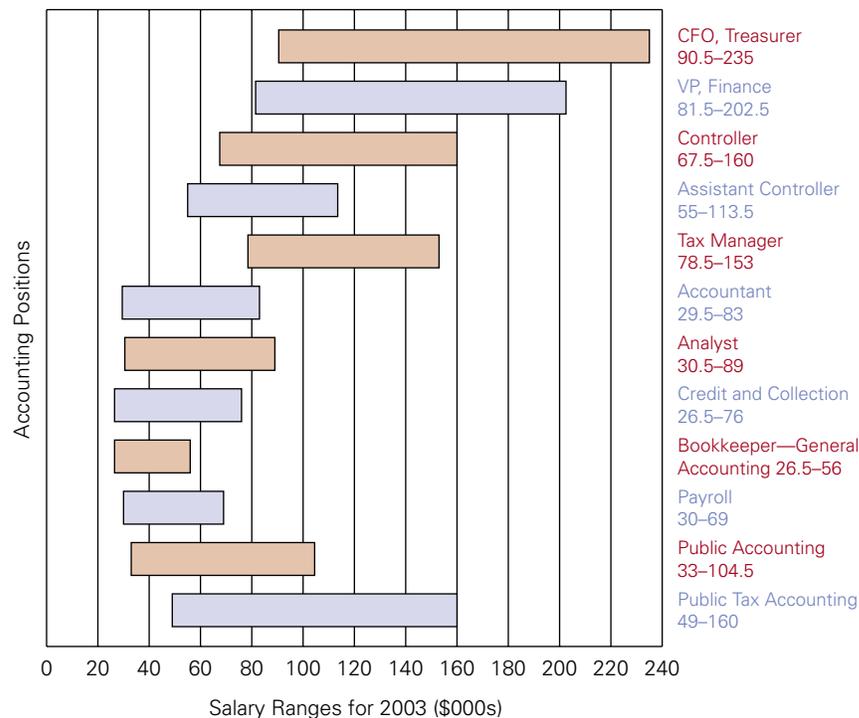


Exhibit 1.6

Average Annual Salaries  
for Accounting Positions



\*These values do not include benefits/bonuses.

SOURCE: Extracted from Robert Half 2003 Salary Guide

## Financial Accounting

Financial accounting serves the needs of external users by providing financial statements. Many organizations, both business and non-business, issue their financial statements only after an audit. An **audit** is an independent review and test of an organization's accounting systems and records; it is performed to add credibility to the financial statements.<sup>2</sup> **External auditors** perform the audit function at the request of the board of directors to protect shareholder interests.

## Managerial Accounting

Managerial accounting serves the needs of internal users by providing special-purpose reports. These special-purpose reports are the result of general accounting, cost accounting, budgeting, internal auditing, and management consulting.

<sup>2</sup> To achieve this result, audits are performed by independent professionals who are public accountants. Little or no credibility would be added to statements if they were audited by a company's own employees.

<b>General accounting</b>	The task of recording transactions, processing the recorded data, and preparing reports for members of the management team such as the <b>controller</b> (the chief accounting officer of an organization).
<b>Cost accounting</b>	The process of accumulating the information that managers need about the various <b>costs</b> within the organization.
<b>Budgeting</b>	The process of developing formal plans for an organization's future activities.
<b>Internal auditing</b>	Function performed by auditors employed within the organization for the purpose of evaluating the efficiency and effectiveness of procedures.
<b>Management consulting</b>	Service provided by external accountants where suggestions are offered for improving a company's procedures; suggestions may concern new accounting and internal control systems, new computer systems, budgeting, and employee benefit plans.

## Taxation

Income tax raised by federal and provincial governments is based on the income earned by taxpayers. These taxpayers include both individuals and corporate businesses. Sole proprietorships and partnerships are not subject to income tax, but owners of these two non-corporate business forms must pay tax on income earned from these business forms. The amount of tax is based on what the laws define to be income. In the field of **taxation**, tax accountants help taxpayers comply with these laws by preparing their tax returns and providing assistance with tax planning for the future. The government (specifically, Canada Customs and Revenue Agency) employs tax accountants for collection and enforcement.

## Professional Certification

Many accountants (financial, managerial, tax, and other) have professional accounting status. Accounting is a profession, like law and medicine, because accountants have special abilities and responsibilities. The professional status of an accountant is often indicated by one or more professional certifications. In Canada, there are several accounting organizations that provide the education and training required in order to obtain professional certification. These include the Certified General Accountants' Association, the Society of Management Accountants, and the Institute of Chartered Accountants. Successful completion of one of the prescribed programs leads to the following professional accounting designations: Certified General Accountant (**CGA**); Certified Management Accountant (**CMA**); or Chartered Accountant (**CA**).

The preceding discussions show how important accounting is for organizations. Regardless of your career goals, you will use accounting information because it is the language of business. The discussion also emphasizes the broad scope and growing number of opportunities available in accounting. This book will help you to take advantage of those opportunities.

Relevant links are included as a source of additional information.

For detailed information regarding professional accounting education programs and journals, refer to the following Web sites:  
[www.cga-canada.org](http://www.cga-canada.org),  
[www.cma-canada.org](http://www.cma-canada.org),  
 and [www.cica.ca](http://www.cica.ca).



Answers—p. 20

10. What is the difference between private and public accountants?
11. What are the four broad fields of accounting?
12. What is the purpose of an audit?
13. Distinguish between managerial and financial accounting.

Each chapter includes a summary of the chapter by learning objective.

## Summary

**LO<sup>1</sup> Describe accounting and its goals and uses.** Accounting is an information and measurement system that aims to identify, measure, record, and communicate relevant, reliable, consistent, and comparable information about economic activities. It helps us better assess opportunities, products, investments, and social and community responsibilities. The power of accounting is in opening our eyes to new and exciting opportunities. The greatest benefits of understanding accounting often come to those outside of accounting, because an improved understanding of accounting helps us to compete better in today's globally focused and technologically challenging world.

**LO<sup>2</sup> Describe forms of business organizations.** Organizations can be classified either as businesses or non-businesses. Businesses are organized for profit, while non-businesses serve us in ways not always measured by profit. Businesses take one of three forms: sole proprietorship, partnership, or corporation. These forms of organization have characteristics that hold important implications for legal liability, taxation, continuity, number of owners, and legal status.

**LO<sup>3</sup> Identify users and uses of accounting.** There are both internal and external users of accounting. Some users and uses of accounting include: (a) management for control, monitoring and planning; (b) lenders for making

decisions regarding loan applications; (c) shareholders for making investment decisions; (d) directors for overseeing management; and (e) employees for judging employment opportunities.

**LO<sup>4</sup> Explain why ethics and social responsibility are crucial to accounting.** The goal of accounting is to provide useful information for decision making. For information to be useful, it must be trusted. This demands ethics and socially responsible behaviour in accounting. Without these, accounting information loses its reliability.

**LO<sup>5</sup> Describe how technology is changing accounting.** Technology has increased the access to, and processing speed and quantity of, accounting information. Accountants have had to enhance their information technology knowledge and experience in order to compete. However, accountants who possess strong information technology skills are in high market demand and, as a result, earn large salaries.

**LO<sup>6</sup> Identify opportunities in accounting and related fields.** Opportunities in accounting and related fields are numerous. They encompass traditional financial and managerial accounting, and taxation, but also include accounting-related fields such as lending, consulting, managing and planning.

## GUIDANCE ANSWERS TO Judgement Call



### Entrepreneur

You should probably form your business as a corporation if potential lawsuits are of prime concern. The corporate form of organization would protect your personal property from law-

suits directed at the business, and would place only the corporation's resources at risk. You should also examine the ethical and socially responsible aspects of starting a business where you anticipate injuries to others.



1. Accounting is an information and measurement system that identifies, measures, records, and communicates relevant, reliable, consistent, and comparable information to people that helps them in making better decisions. It helps people in business to identify and react to investment opportunities, and better assess opportunities, products, investments, and social and community responsibilities.
2. Recordkeeping is the recording of financial transactions and events, either manually or electronically. While recordkeeping is essential to data reliability, accounting is this and much more. Accounting includes identifying, measuring, recording, reporting, and analyzing economic events and transactions. It involves interpreting information, and designing information systems to provide useful reports that monitor and control an organization's activities.
3. The three common forms of business organizations are sole proprietorships, partnerships, and corporations.
4. Non-business organizations include airports, libraries, museums, religious institutions, municipal governments, law enforcement organizations, postal services, colleges, universities, bus lines, utilities, highways, shelters, parks, hospitals, and schools.
5. External users of accounting information are not directly involved in running the organization. Internal users of accounting information are those individuals directly involved in managing and operating an organization.
6. Internal controls are procedures set up to protect assets, ensure that accounting reports are reliable, promote efficiency, and encourage adherence to company policies.

Internal controls are crucial if accounting reports are to provide relevant and reliable information.
7. The guidelines for ethical and socially responsible decisions are threefold: (1) identify ethical and/or social issue; (2) analyze options, considering both good and bad consequences for all individuals affected; and (3) make ethical/socially responsible decision, choosing the best option after weighing all consequences.
8. Ethics and social responsibility are important for people because, without them, existence is more difficult, inefficient, and unpleasant. They are equally important to organizations, for this same reason. In addition, they often translate into higher profits and a better working environment.
9. Accounting aims to provide useful information for decision making. For information to be useful, it must be trusted. Trustworthiness of information demands ethics in accounting.
10. Private accountants work for a single employer, which is often a business. A public accountant is available to the public, which means that services are provided to many different clients.
11. The four broad fields of accounting are: financial, managerial, taxation, and accounting-related.
12. The purpose of an audit is to add credibility to the financial statements.
13. Managerial accounting is for internal users, while financial accounting is for external users.

## Demonstration Problem

Rupert Jones works in a public accounting firm and hopes to be a partner eventually. The management of ShadowTech Company invited Jones to prepare a 'bid' to audit ShadowTech's financial statements. In discussing the audit's fee, ShadowTech's management suggests a fee range where the fee amount depends on the reported profit of ShadowTech. The higher its profit, the higher the audit fee paid to Jones' firm.

### Required

1. Identify the parties potentially affected by this situation.
2. What are the ethical factors in this situation?
3. Would you recommend that Jones accept this audit fee arrangement? Why?
4. Describe some of the factors guiding your recommendation.
5. Go to the following Web sites and read the sections noted regarding conflict of interest: <http://www.cga-alberta.org/images/PDF/RAPACodeofEthics2002.pdf> and read pages 11 to 14; [http://www.cma-alberta.com/Resources/view\\_document.asp?id=675588a2f3504f3aa05c8a6db8fb941b](http://www.cma-alberta.com/Resources/view_document.asp?id=675588a2f3504f3aa05c8a6db8fb941b) and read Article IV; and [http://www.icao.on.ca/multimedia/PDFs/handbook/rules\\_web.pdf](http://www.icao.on.ca/multimedia/PDFs/handbook/rules_web.pdf) and read Section 210.

### SOLUTION TO Demonstration Problem

1. Several parties are affected. They most directly include the users of financial statements, such as shareholders, lenders, investors, analysts, suppliers, directors, unions, regulators, and others. They also include the accounting firm (which can be sued if party to misleading statements), and Mr. Jones's business colleagues and family.
2. The value of an auditor's report stems from the auditor's independence. If an auditor accepts a fee that increases when the client's reported profit increases, the auditor is (or is at least perceived to be) interested in higher profits for the client. This compromises the auditor's independence.
3. To avoid compromising his independence, Jones should not accept this fee arrangement. Further, codes of professional conduct would forbid an auditor from accepting contingent fees that depend on amounts reported in a client's financial statements.
4. Ethical considerations guiding this decision include the potential harm to affected parties by allowing such a fee arrangement to exist. Ethical considerations also guard the profession against unethical actions that could undermine its real and perceived value to society.
5. Type in the Web site URLs and read the noted pages, or go to the respective bodies for your province and search for the Code of Ethics.

## 1A

# Codes of Ethics and Professional Conduct

Many chapters have one or more appendices containing information that is directly related to that chapter but that fits better in a separate location.

LO<sup>7</sup>

Describe the codes of ethics and professional conduct for accountants.

## Selection from the Certified General Accountants of Alberta's Code of Ethical Principles and Rules of Conduct<sup>1</sup>

### Code of Ethical Principles

#### (a) Responsibilities to Society

Members have a fundamental responsibility to safeguard and advance the interests of society. This implies acting with trustworthiness, integrity and objectivity. This responsibility extends beyond a member's own behaviour to the behaviour of colleagues and to the standards of the Association and the profession.

#### (b) Trust and Duties

Members shall act in the interest of their clients, employers, and interested third parties, and shall be prepared to sacrifice their self-interest to do so. Members shall honour the trust bestowed on them by others, and shall not use their privileged position without their principal's knowledge and consent. Members shall avoid conflicts of interest.

#### (c) Due Care and Professional Judgement

Members shall strive to continually upgrade and develop their technical knowledge and skills in the areas in which they practice as professionals. This technical expertise shall be employed with due professional care and judgement.

#### (d) Deceptive Information

Members shall not be associated with any information which the member knows, or ought to know, to be false or misleading, whether by statement or omission.

<sup>1</sup> The Certified General Accountants of Alberta, *Code of Ethical Principles and Rules of Conduct*. The complete code can be found at: [www.cga-alberta.org](http://www.cga-alberta.org).

### (e) Professional Practice

Members shall act openly and fairly towards others in the practice of their profession.

### (f) Responsibilities to the Profession

Members shall always act in accordance with the duties and responsibilities associated with being members of the profession, and shall carry on work in a manner which will enhance the image of the profession and the Association.

## Selection From the Code of Ethics for Certified Management Accountants<sup>2</sup>

A profession is distinguished by certain characteristics including:

- (a) mastery of a particular intellectual skill, acquired by training and education;
- (b) acceptance of duties to society as a whole in addition to duties to the Employer or Client;
- (c) an outlook which is essentially objective; and
- (d) a high standard in the conduct and performance of personal service.

People who use professional services usually find it difficult to assess the specialized knowledge and skills of professionals. That is why professional organizations lay down technical and ethical standards for their members. By enforcing these standards, professional organizations protect the public interest, and users can confidently rely on professionals.

Two important principles underlie this Code, as well as the rules and guidelines, and form a common thread throughout its provisions.

First, a Member must establish and maintain a reputation for integrity, the most basic attribute of a member of the accounting profession. Integrity includes trustworthiness, loyalty, fairness, honour and honesty.

Second, a Member must reject inappropriate conduct, both on a professional and personal level. A Member also has a duty to refrain from behaviour which, while legal, is inconsistent with the high standards of the profession, or calls into question the Member's fitness as a professional. A Member who violates either of these principles will lose the respect and confidence of the public and other accountants.

Through legislation, the accounting profession is self-governing. The privilege of self-governance carries with it special responsibilities. The rationale for the Code of Ethics ("the Code") must be to codify ethics respecting practice as a certified management accountant, to maintain the dignity and honour of the profession, and to protect the public interest. Members must strive for their observance of the Code both individually and collectively. The Code, rules and guidelines are not, however, capable of stating every circumstance a Member may face. Members must therefore consider other ethical and moral considerations, as well as legislation relating to Members and laws of a more general nature, in deciding to pursue a course of action in a given situation.

<sup>2</sup> The Society of Management Accountants of Alberta, *Code of Ethics*. The complete code can be found at: [www.cga-alberta.org](http://www.cga-alberta.org).

All Members should follow both the spirit and the letter of the Code, rules and guidelines.

The willingness and determination of the profession to achieve widespread compliance with the Code, rules and guidelines is a more powerful and basic enforcement mechanism than the imposition of sanctions. A Member must therefore be vigilant respecting his or her own behaviour as well as that of colleagues. However, it is improper to use any provision of the Code, rules and guidelines as an instrument of harassment or as a procedural weapon without a genuine concern respecting the interests of an employer, client, the profession or the public.

## Selection from the ICAO Rules of Professional Conduct<sup>3</sup>

To grasp the breadth of the rules of professional conduct, we will review the table of contents for the Institute of Chartered Accountants of Ontario, which includes the following:

### FIRST BYLAW OF 1973

#### FOREWORD

Application of the rules of professional conduct  
Interpretation of the rules of professional conduct

#### 100 - GENERAL

101 Compliance with bylaws, regulations and rules  
102.1 Conviction of criminal or similar offences  
102.2 Reporting disciplinary suspension, expulsion or restriction of right to practise  
103 False or misleading applications  
104 Requirement to reply in writing

#### 200 - STANDARDS OF CONDUCT AFFECTING THE PUBLIC INTEREST

201.1,  
.2 & .3 Maintenance of reputation of profession  
201.4 Advocacy services  
202 Integrity and due care  
203.1 Professional competence  
203.2 Co-operation with practice inspections and conduct investigations  
204.1 Objectivity: assurance and specified auditing procedures engagements  
204.2 Objectivity: insolvency engagements  
204.3 Objectivity: disclosure of impairment of objectivity  
205 False or misleading documents and oral representations  
206 Member's compliance with professional standards  
207 Unauthorized benefits

<sup>3</sup> ICAO, *Rules of Professional Conduct* (Toronto Institute of Chartered Accountants of Ontario). Other provincial institutes have similar provisions. The complete set of rules can be found at: [www.icao.on.ca](http://www.icao.on.ca).

- 208 Confidentiality of information
  - 210 Conflict of interest
  - 211 Duty to report breach of rules of professional conduct
  - 212.1 Handling of trust funds and other property
  - 212.2 Handling property of others
  - 213 Unlawful activity
  - 214 Fee quotations
  - 215 Contingency fees
  - 216 Payment or receipt of commissions
  - 217.1 Advertising and promotion
  - 217.2 Solicitation
  - 217.3 Endorsements
  - 218 Retention of documentation and working papers
- 300 - RELATIONS WITH OTHER MEMBERS OR FIRMS AND WITH NON-MEMBERS LICENSED TO PRACTISE PUBLIC ACCOUNTING
- 302 Communication with predecessor
  - 303 Co-operation with successor
  - 304 Joint engagements
  - 305 Communication of special engagements to incumbent
  - 306.1 Responsibilities on accepting engagements
  - 306.2 Responsibilities on referred engagements
- 400 - ORGANIZATION AND CONDUCT OF A PROFESSIONAL PRACTICE
- 401 Practice names
  - 404.1 Use of descriptive styles
  - 404.2 Operation of members' offices
  - 404.3 Proprietary interest with non-members
  - 405 Association with firms
  - 406 Member responsible for a non-member in practice of public accounting
  - 407 Related business or practice, and member responsible for non-member in such business or practice
  - 408 Association with non-member in public practice
  - 409 Office by representation
  - 410 Practice of public accounting in corporate form
- 500 - RULES OF PROFESSIONAL CONDUCT APPLICABLE ONLY TO FIRMS
- 501 Firm's maintenance of policies and procedures for compliance with professional standards
  - 502 Firm's maintenance of policies and procedures: competence and conduct of firm members
  - 503 Association with firms

## Summary of Appendix 1A



**Describe the codes of ethics and professional conduct for accountants.** Each of the three professional accounting bodies in Canada has a code of

professional conduct outlining the ethical standards required of accountants. Failure to comply leads to disciplinary action.

The glossary includes terms and phrases explained in the chapter.

## Glossary

**Accounting** An information system that identifies, measures, records and communicates relevant, reliable, consistent, and comparable information about an organization's economic activities. (p. 4)

**Audit** A check of an organization's accounting systems and records. (p. 17)

**Bookkeeping** The part of accounting that involves recording economic transactions and events, either electronically or manually; also called *recordkeeping*. (p. 6)

**Budgeting** The process of developing formal plans for future activities, which often serve as a basis for evaluating actual performance. (p. 18)

**Business** One or more individuals selling products or services for profit. (p. 6)

**Business entity principle** Every business is accounted for separately from its owner's personal activities. (p. 7)

**CA** Chartered Accountant; an accountant who has met the examination, education, and experience requirements of the Institute of Chartered Accountants for an individual professionally competent in accounting. (p. 18)

**CCRA** Canada Customs and Revenue Agency; the federal government agency responsible for the collection of tax and enforcement of tax laws. (p. 10)

**CGA** Certified General Accountant; an accountant who has met the examination, education, and experience requirements of the Certified General Accountants' Association for an individual professionally competent in accounting. (p. 18)

**CMA** Certified Management Accountant; an accountant who has met the examination, education, and experience requirements of the Society of Management Accountants for an individual professionally competent in accounting. (p. 18)

**Codes of Professional Conduct** Sets of guidelines governing the behaviour of the professional. (p. 22)

**Common shares** The name for a corporation's shares when only one class of share capital is issued. (p. 8)

**Controller** The chief accounting officer of an organization. (p. 18)

**Corporation** A business that is a separate legal entity under provincial or federal laws with owners who are called shareholders. (p. 7)

**Cost accounting** A managerial accounting activity designed to help managers identify, measure, and control operating costs. (p. 18)

**Costs** The expenses incurred to earn revenues (or sales). (p. 18)

**Ethics** Beliefs that differentiate right from wrong. (p. 13)

**External auditors/auditing** Examine and provide assurance that financial statements are prepared according to generally accepted accounting principles (GAAP). (p. 17)

**External users** Persons using accounting information who are not directly involved in the running of the organization; examples include shareholders, customers, regulators, and suppliers. (p. 10)

**Financial accounting** The area of accounting aimed at serving external users. (p. 10)

**Generally Accepted Accounting Principles (GAAP)** The rules that indicate acceptable accounting practice. (p. 7)

**General accounting** The task of recording transactions, processing data, and preparing reports for managers; includes preparing financial statements for disclosure to external users. (p. 18)

**Government accountants** Accountants who work for local, provincial, and federal government agencies. (p. 17)

**Internal auditors/auditing** Employees within organizations who assess whether managers are following established operating procedures and evaluate the efficiency of operating procedures. (p. 18)

**Internal controls** Procedures set up to protect assets, ensure reliable accounting reports, promote efficiency, and encourage adherence to company policies. (p. 12)

**Internal users** Persons using accounting information who are directly involved in managing and operating an organization; examples include managers and officers. (p. 11)

**Limited liability** The owner's liability is limited to the amount of investment in the business. (p. 8)

**Limited liability partnership** Restricts partners' liabilities to their own acts and the acts of individuals under their control. (p. 7)

**Limited partnership** Includes both general partner(s) with unlimited liability and limited partner(s) with liability restricted to the amount invested. (p. 7)

**Management consulting** Activity in which suggestions are offered for improving a company's procedures; the suggestions may concern new accounting and internal control systems, new computer systems, budgeting, and employee benefit plans. (p. 18)

**Managerial accounting** The area of accounting aimed at serving the decision-making needs of internal users. (p. 12)

**Partnership** A business owned by two or more people, which is not organized as a corporation. (p. 7)

**Private accountants** Accountants who work for a single employer other than the government or a public accounting firm. (p. 17)

**Public accountants** Accountants who provide their services to many different clients. (p. 17)

**Recordkeeping** The recording of financial transactions and events, either manually or electronically; also called *book-keeping*. (p. 6)

**Shareholders** The owners of a corporation. (p. 8)

**Shares** Units of ownership in a corporation. (p. 8)

**Single proprietorship** A business owned by one individual, which is not organized as a corporation; also called a *sole proprietorship*. (p. 7)

**Social responsibility** A commitment to considering the impact and being accountable for the effects that actions might have on society. (p. 15)

**Sole proprietorship** A business owned by one person, which is not organized as a corporation; also called a *single proprietorship*. (p. 7)

**Taxation** The field of accounting that includes preparing tax returns and planning future transactions to minimize the amount of tax paid; involves private, public, and government accountants. (p. 18)

**Unlimited liability** When the debts of a sole proprietorship or partnership are greater than its resources, the owner(s) is (are) financially responsible. (p. 7)



For more study tools, quizzes, and problem material, refer to the Online Learning Centre at [www.mcgrawhill.ca/college/larson](http://www.mcgrawhill.ca/college/larson)

Short-answer questions reinforce key chapter concepts in order of learning objectives.

## Questions

1. In the chapter's opening article, what does Wynne Powell identify as the key to success in business?
2. Identify three businesses that offer services and three businesses that offer products.
3. Describe three forms of business organizations and their characteristics.
4. Identify the two organizations for which accounting information is available in Appendix I at the end of the book.
5. Identify three types of organizations that can be formed as either profit-oriented businesses, government units, or not-for-profit establishments.
6. What type of accounting information might be useful to those who carry out the marketing activities of a business?
7. Identify four external and internal users and their uses of accounting information.
8. Describe the internal role of accounting for organizations.
9. What is the purpose of accounting in society?
10. What ethical issues might accounting professionals face in dealing with confidential information?
11. Technology is increasingly used to process accounting data. Why, then, should we study accounting?
12. What is the relation between accounting and technology?
13. Identify four managerial accounting tasks performed by both private and government accountants.
14. Identify two management-consulting services offered by public accounting professionals.
15. What work do tax accounting professionals perform in addition to preparing tax returns?
16. Identify the auditing firm that audited the financial statements of Leon's in Appendix I.



Appendix I at the end of the text includes two sets of real-life financial statements to provide you with a frame of reference.

Quick Study items are single-topic exercises that give the reader a brief test of each key element in the chapter.



## Quick Study

**QS 1-1**

Identifying ethical matters

Identify two possible uses of accounting information.

LO<sup>3</sup>

← Each Quick Study, Exercise, and Problem is referenced to the Learning Objective in the chapter.

**QS 1-2**

Explaining internal control

Accounting professionals must sometimes choose between two or more acceptable methods of accounting for certain transactions. Explain why these situations can involve difficult matters of ethical concern.

LO<sup>4</sup>**QS 1-3**

Uses of accounting information

Explain why accountants need to enhance their knowledge of information technology.

LO<sup>5</sup>**QS 1-4**

Impact of technology on accounting

An important responsibility of many accounting professionals is to design and implement internal control procedures for organizations. Explain the purpose of internal control procedures.

LO<sup>6</sup>**QS 1-5**

Accounting and accounting-related opportunities

Identify at least three main areas of accounting for accounting professionals. For each accounting area, identify at least three accounting-related opportunities in practice.

LO<sup>6</sup>

← An asterisk (\*) identifies material related to a chapter appendix.

**\*QS 1-6**

Experience technology

Read the article about the Rotary 4-Way Test by going to the McGraw-Hill Online Learning Centre ([www.mcgrawhill.ca/college/larson](http://www.mcgrawhill.ca/college/larson)), choose the 11th Edition and click on the "Extend Your Knowledge" link. Explain how the article relates to the codes of ethics and professional conduct for accountants.LO<sup>7</sup>

\_\_\_\_\_ An asterisk (\*) identifies assignment material based on Appendix 1A.

Exercises provide you with an additional opportunity to reinforce basic chapter concepts.



## Exercises

Presented below are descriptions of several different business organizations. Determine whether the situation described refers to a sole proprietorship, partnership, or corporation.

- Ownership of Cola Company is divided into 1,000 shares.
- Text Tech is owned by Kimberly Fisher, who is personally liable for the debts of the business.
- Jerry Forrentes and Susan Montgomery own Financial Services, a financial and personal services provider. Neither Forrentes nor Montgomery has personal responsibility for the debts of Financial Services.
- Nancy Kerr and Frank Levens own Runners, a courier service. Both Kerr and Levens are personally liable for the debts of the business.
- MRS Consulting Services does not have a separate legal existence apart from the one person who owns it.
- Biotech Company has one owner and does not pay taxes.
- Torby Technologies has two owners and pays its own taxes.

### Exercise 1-1

Distinguishing business organizations

LO<sup>2</sup>

Identify the users of TLC Daycare's accounting information as internal (I) or external (E).

<i>I or E</i>		<i>I or E</i>	
Bank manager		Parent	
Owner		Canada Customs and Revenue Agency	
Toy supplier		Cleaner contracted by TLC Daycare	

### Exercise 1-2

Users of accounting information

LO<sup>3</sup>

Identify at least three external users of accounting information and indicate some questions that they might seek to answer through their use of accounting information.

### Exercise 1-3

Identifying accounting users and uses

LO<sup>3</sup>

Assume the following role and describe a situation where ethical considerations play an important part in guiding your action:

- You are a student in an accounting principles course.
- You are a manager with responsibility for several employees.
- You are an accounting professional preparing tax returns for clients.
- You are an auditing professional with audit clients that are competitors in business.

### Exercise 1-4

Identifying ethical decisions

LO<sup>4</sup>

Go to each of the following Internet sites and briefly describe what information the site provides.

- |  |  |
|--|--|
| a. <a href="http://globeandmail.ca">http://globeandmail.ca</a>         | e. <a href="http://www.canadianbusiness.com">http://www.canadianbusiness.com</a> |
| b. <a href="http://www.PROFITguide.com">http://www.PROFITguide.com</a> | f. <a href="http://finance.yahoo.com">http://finance.yahoo.com</a>               |
| c. <a href="http://www.sedar.com">http://www.sedar.com</a>             | g. <a href="http://www.strategis.ic.gc.ca">http://www.strategis.ic.gc.ca</a>     |
| d. <a href="http://canada.gc.ca">http://canada.gc.ca</a>               | h. <a href="http://www.canadiancareers.com">http://www.canadiancareers.com</a>   |

### Exercise 1-5

Using technology as an accounting research tool

LO<sup>5</sup>

**Exercise 1-6**

Learning the language of business

LO 1, 2, 3, 4, 6

Indicate which description best depicts each of the following important terms:

- |   |                         |
|---|-------------------------|
| <b>a.</b> Government accountants            | <b>e.</b> Recordkeeping |
| <b>b.</b> Internal auditing                 | <b>f.</b> CGA           |
| <b>c.</b> Canada Customs and Revenue Agency | <b>g.</b> GAAP          |
| <b>d.</b> Accounting                        | <b>h.</b> Shareholders  |

- \_\_\_\_\_ 1. Responsibility of an organization's employees involving examining the organization's recordkeeping processes, assessing whether managers are following established operating procedures, and appraising the efficiency of operating procedures.
- \_\_\_\_\_ 2. Federal department responsible for collecting federal taxes and enforcing tax law.
- \_\_\_\_\_ 3. Accounting professionals who provide services to many different clients.
- \_\_\_\_\_ 4. Accounting professionals employed by federal, provincial, or local branches of government.
- \_\_\_\_\_ 5. Accounting rules.

**Exercise 1-7**

Learning the language of business

LO 1, 3, 4, 6

Indicate which description best depicts each of the following important terms:

- |                           |                              |
|---------------------------|------------------------------|
| <b>a.</b> Audit           | <b>e.</b> Ethics             |
| <b>b.</b> Recordkeeping   | <b>f.</b> General accounting |
| <b>c.</b> Cost accounting | <b>g.</b> Budgeting          |
| <b>d.</b> GAAP            | <b>h.</b> Taxation           |

- \_\_\_\_\_ 1. An accounting area that includes planning future transactions to minimize taxes paid.
- \_\_\_\_\_ 2. A managerial accounting process designed to help managers identify, measure, and control operating costs.
- \_\_\_\_\_ 3. Principles that determine whether an action is right or wrong.
- \_\_\_\_\_ 4. An examination of an organization's accounting system and records that adds credibility to financial statements.
- \_\_\_\_\_ 5. The task of recording transactions, processing recorded data, and preparing reports and financial statements.

**Exercise 1-8**

Describing accounting responsibilities

LO 6

Many accounting professionals work in one of the following three areas:

- a.** Financial accounting
- b.** Managerial accounting
- c.** Taxation accounting

For each of the following responsibilities, identify the area of accounting that most likely involves that responsibility:

- \_\_\_\_\_ 1. Auditing financial statements.
- \_\_\_\_\_ 2. Planning transactions to minimize taxes paid.
- \_\_\_\_\_ 3. Cost accounting.
- \_\_\_\_\_ 4. Preparing financial statements.
- \_\_\_\_\_ 5. Reviewing financial reports for compliance with provincial securities commissions requirements.
- \_\_\_\_\_ 6. Budgeting.
- \_\_\_\_\_ 7. Internal auditing.
- \_\_\_\_\_ 8. Investigating violations of tax laws.

Problems typically incorporate two or more concepts. There are two groups of problems: A problems and Alternate or B problems. B problems mirror the A problems to help you improve your understanding through repetition.

## Problems

Complete the chart below by placing a checkmark in the appropriate column.

Characteristic	Type of Business Organization		
	Sole Proprietorship	Partnership	Corporation
Limited liability			
Unlimited liability			
Owners are shareholders			
Owners are partners			
Taxed as a separate legal entity			

**Problem 1-1A**  
Identifying type of business organization

LO<sup>2</sup>

## Alternate Problems

- Refer to Appendix I at the end of the book. Determine if WestJet Airlines is a sole proprietorship, partnership, or corporation.
- Refer to Appendix I at the end of the book. Determine if Leon's Furniture is a sole proprietorship, partnership, or corporation.



**Problem 1-1B**  
Identifying type of business organization

LO<sup>2</sup>

## Ethics Challenge

Dennis Willaby recently completed his professional accounting program and was hired to work in the accounting office of a large hardware store. A tremendous ice storm struck and caused countless people to be without electricity for extended periods. Dennis's boss instructed him to raise the selling price of the gas-powered generators that people were buying to generate their own electricity until the power could be restored. You have a concern about the ethics and social responsibility issue related to the practice of raising prices during a time of crisis. Comment.

**EC 1-1**

