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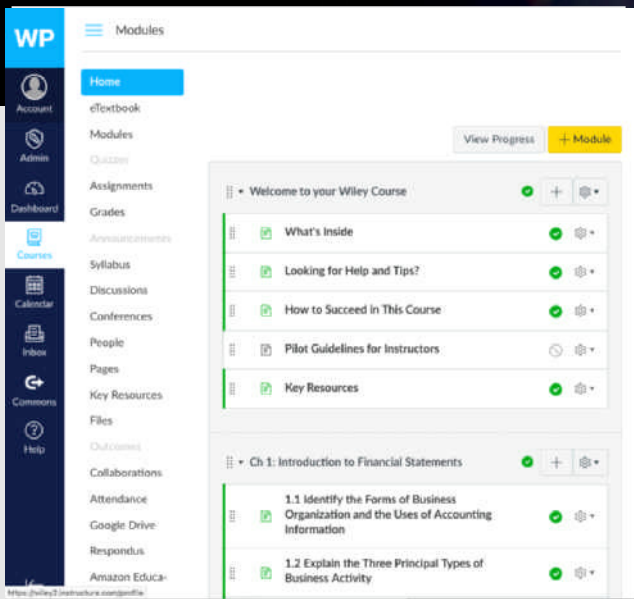
FINANCIAL ACCOUNTING

Tools for Business Decision-Making

Eighth Canadian Edition

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BARBARA TRENHOLM, FCPA, FCA, ICD.D, is a professor emerita at the University of New Brunswick, for which she continues to teach on a part-time basis. Her teaching and educational leadership has been widely recognized with numerous local, national, and international teaching awards. She also served a three-year term as a Teaching Scholar at the University of New Brunswick.

Barbara is a member of the boards of Plaza REIT, NB Power, and the International Development Research Centre. She is a past board member of Atomic Energy of Canada Limited, the Canadian Institute of Chartered Accountants (now known as CPA Canada), and the Atlantic School of Chartered Accountancy (now known as CPA Atlantic School of Business), and past president of the New Brunswick Institute of Chartered Accountants (now known as CPA New Brunswick). She has extensive service as chair and a member of a wide range of committees at the provincial, national, and international levels of the accounting profession. In addition to her involvement with her profession, she has also served in leadership roles at the university and in the community.

She has presented at many conferences and published widely in the field of accounting education and standard setting in journals, including *Accounting Horizons*, *Journal of the Academy of Business Education*, *CAMagazine*, *CGA Magazine*, and *CMA Magazine*. She is also part of the Canadian author team of Weygandt, Kieso, Kimmel, Trenholm, Warren, and Novak, *Accounting Principles*, published by John Wiley & Sons Canada, Ltd.



WAYNE IRVINE, FCPA, FCA, CFA, teaches accounting at the Haskayne School of Business, University of Calgary for undergraduates and students enrolled in executive MBA and executive education programs. Prior to his full-time academic career, Wayne worked for 12 years at Price Waterhouse in the audit group and as a senior audit manager and coordinated the Calgary office's continuing education program.

Wayne has over 28 years of teaching experience with several professional accounting programs, most recently as a session leader for CPA Western School of Business in its Professional Education Program.

Wayne has, in addition to other publishing projects, authored several case exams for CPA legacy programs and published a case in *Accounting Perspectives*.

Wayne is a four-time recipient of the University of Calgary's Students' Union Teaching Excellence Award. He has also received over a dozen other teaching and service awards from other student organizations and from the CPA profession.



CHRIS BURNLEY, FCPA, FCA, is a professor in the accounting department at Vancouver Island University. Prior to his full-time academic career, Chris worked for 12 years in public practice and also audited government departments and United Nations agencies with the Office of the Auditor General of Canada. Chris also teaches in the CPA Professional Education Program for the CPA Western School of Business.

Chris also teaches in the Master of Professional Accounting Program at the University of Saskatchewan, where he is a two-time recipient of the Chartered Professional Accountants of Alberta teaching excellence award. He is active internationally, teaching and delivering guest lectures at Vancouver Island University's partner institutions in Europe, Asia, and the South Pacific. Chris has been awarded numerous internal and external grants in support of his academic work and has presented at national conferences. Chris has been awarded a number of prizes by the Canadian Academic Accounting Association as a result of his academic work, including awards for case authoring and developing innovative ideas in accounting education.

Chris is active in the accounting profession, serving on the boards of the Canadian Academic Accounting Association and the Chartered Professional Accountants of British Columbia (CPABC). He is past chair of CPABC's Education Foundation. He received the Ritchie W. McCloy Award for CA Volunteerism. Chris is also the author of the textbook *Understanding Financial Accounting*, published by John Wiley & Sons Canada, Ltd.



PAUL D. KIMMEL, PH.D., CPA, received his bachelor's degree from the University of Minnesota and his doctorate in accounting from the University of Wisconsin. He taught at U.W.—Milwaukee for over 25 years and now teaches at U.W.—Madison. He has public accounting experience with Deloitte & Touche (Minneapolis). He was the recipient of the UWM School of Business Advisory Council Teaching Award, the Reggie Taite Excellence in Teaching Award, and a three-time winner of the Outstanding Teaching Assistant Award at the University of Wisconsin. He is also a recipient of the Elijah Watts Sells Award for Honorary Distinction for his results on the CPA exam. He is a member of the American Accounting Association and the Institute of Management Accountants and has published articles in *Accounting Review*, *Accounting Horizons*, *Advances in Management Accounting*, *Managerial Finance*, *Issues in Accounting Education*, and *Journal of Accounting Education*, as well as other journals. His research interests include accounting for financial instruments and innovation in accounting education. He has published papers and given numerous talks on incorporating critical thinking into accounting education and he has helped prepare a catalogue of critical thinking resources for the Federated Schools of Accountancy.



JERRY J. WEYGANDT, PH.D., CPA, is the Arthur Andersen Alumni Emeritus Professor of Accounting at the University of Wisconsin—Madison. He holds a Ph.D. in accounting from the University of Illinois. Articles by Professor Weygandt have appeared in *Accounting Review*, *Journal of Accounting Research*, *Accounting Horizons*, *Journal of Accountancy*, and other academic and professional journals. Professor Weygandt is 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 served on numerous committees of the American Accounting Association and as a member of the editorial board of *Accounting Review*; he has also served as President and Secretary-Treasurer of the American Accounting Association.

In addition, he has been actively involved with the American Institute of Certified Public Accountants and has been a member of the Accounting Standards Executive Committee of that organization. He served on the FASB task force that examined the reporting issues related to accounting for income taxes and as a trustee of the Financial Accounting Foundation. Professor Weygandt has received the Chancellor's Award for Excellence in Teaching and the Beta Gamma Sigma Dean's Teaching Award. He is on the board of directors of M&I Bank of Southern Wisconsin. 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.



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 chairman of the Department of Accountancy and is currently the KPMG Emeritus Professor of Accounting at Northern Illinois University (NIU). He has public accounting experience with Price Waterhouse & Co. and Arthur Andersen & Co. and research experience with the Research Division of the American Institute of Certified Public Accountants. He is a recipient of NIU's Teaching Excellence Award and four Golden Apple Teaching Awards. Professor Kieso is a member of the American Accounting Association, the American Institute of Certified Public Accountants, and the Illinois CPA Society. He has served as a member of the Board of Directors of the Illinois CPA Society, the AACSB's Accounting Accreditation Committees, and the State of Illinois Comptroller's Commission; as Secretary-Treasurer of the Federation of Schools of Accountancy; and as Secretary-Treasurer of the American Accounting Association. Professor Kieso is currently serving on the Board of Trustees and Executive Committee of Aurora University, and he is a member of various other boards. From 1989 to 1993, he served as a charter member of the national Accounting Education Change Commission. He is the recipient of the Outstanding Accounting Educator Award from the Illinois CPA Society, the FSA's Joseph A. Silvos Award of Merit, the NIU Foundation's Humanitarian Award for Service to Higher Education, the Distinguished Service Award from the Illinois CPA Society, and an honorary doctorate from Aurora University in 2003.

What's New?

Helping Students Learn Accounting Concepts

We have carefully scrutinized all chapter material to find new ways to engage students and help them learn accounting concepts. An additional 11 DO IT! exercises have been developed, meaning that there are now 99 in-chapter opportunities for students to test their understanding before moving on to the next topic. Some of the new DO IT! exercises help students confirm their understanding of the five-step model of revenue recognition. Other new DO IT! exercises have been created for

blended loan payments, bond pricing, and market measures, in addition to other topics. We highlighted accounting concepts that are useful for management decision-making throughout the text. We included a summary of Decision Tools in each chapter as well as a practice exercise and solution, Using the Decision Tools. As well, we added and/or revised a significant number of explanations, examples and illustrations throughout the text to better facilitate student learning.

Real-World Context

One of the goals of the financial accounting course is to orient students to the application of accounting principles and techniques in practice. Accordingly, we have expanded our practice of using current examples from real companies throughout the textbook by adding even more high-interest companies such as Uber, Live Nation, Aritzia, True Büch Kombucha, and Apple. We hope that these will increase student engagement. This edition includes more than 300 references to real-world companies of interest to students. Half of the chapter-opening feature stories were replaced with new stories, while the remainder were updated. **Accounting Matters** insight boxes that feature real companies were also updated. The feature companies for this edition are The North West Company and Sobey's, two well-known companies in the grocery industry. References to these

companies have been included throughout the textbook in a variety of ways—in simplified financial statements in the chapter material, ratio analyses, Using the Decision Toolkit, end-of-chapter cases, and financial statements in Appendices A and B at the end of the textbook. Other features that were updated include **Keeping an Eye on Cash**, which explains the significance of cash, and the **Missing in Action** features, which show how a missing control can result in errors and misstatements. In addition, our author team is active in delivering the CPA Professional Education Program and incorporated this real-world perspective when writing each chapter, including the end-of-chapter material. International Financial Reporting Standards (IFRS) and Accounting Standards for Private Enterprises (ASPE) were also revised to reflect current and pending changes to standards.

New IFRS Content

Chapters 4, 5, and 8 now include significantly expanded IFRS 15 content related to the five-step model of revenue recognition. The material has been presented in a graduated manner, exposing students to situations involving only a single performance obligation, before moving on to multiple performance obliga-

tions. Content on variable consideration and refund liabilities has also been added. These discussions are well supported with related DO IT! exercises. Chapter 8 has also been updated to reflect the expected credit loss model from IFRS 9, while lease content in Chapter 9 has been updated to reflect IFRS 16.

Data Analytics

New features on data analytics, called **Analytics Mindset**, have been authored for this edition and are included in eight of the chapters. These features are focused on helping students develop the ability to ask the right questions and identify the internal and external data that could be captured to help answer these questions. Related end-of-chapter material, in the form of questions and critical thinking problems, has also been created for faculty wanting to expand the discussion of this material.

A new **accounting-specific data analytics module** with interactive lessons, case studies, and videos is part of the *WileyPLUS* course. The module has been prepared using industry-validated content to help you develop the professional competencies needed for the Common Final Examination (CFE) and the changing workforce.

Review and Practice

The review and practice section at the end of each chapter has been refined. This area includes, in one place, an overview of the learning objectives, key terms, differences (if any) between IFRS and ASPE, and decision tools, in addition to practice opportunities using the Decision Toolkit and a comprehensive DO IT!. The review and practice section also includes objective-format questions that allow students to self-assess their understanding of the topics in each chapter. These questions

are comprehensive in their coverage, with detailed feedback provided at the end of the chapter to help students analyze their results. Additional practice objective-format questions are available in the test bank for instructor use. These questions are similar to ones that CPA Canada is introducing to the Professional Education Program, providing students with an early opportunity to learn how to approach and develop a level of comfort with this style of question.

End-of-Chapter Material

The end-of-chapter material underwent a comprehensive updating to ensure that it continues to be relevant and fresh. One third of the questions, brief exercises, exercises, problems, and cases in the end-of-chapter material are either new or significantly updated. A new type of critical thinking problem has been added in every chapter that requires students to think through the high-level financial statement impacts of a variety

of transactions. The serial case, which has been an important continuing feature in each chapter in past editions, has been revised to follow the evolution of a hypothetical computer consulting company from a small private firm to a large publicly traded company. The serial case includes the application of the five-step revenue recognition model.

Key Features of Each Chapter

Chapter 1: The Purpose and Use of Financial Statements

- Feature story is about The North West Company and how accounting aids decision-making
- Identifies the users and uses of financial accounting information and forms of business organization—proprietorship, partnership, private corporation, and public corporation
- Describes the business activities—financing, investing, and operating activities—that affect companies
- Explains the content, purpose, and interrelationships of each of the financial statements—income statement, statement of changes in equity, statement of financial position, and statement of cash flows
- Uses financial statements of a hypothetical company (to keep it simple), followed by those for a real company, The North West Company (to make it relevant)
- **Key changes:** Added context on the nature of public companies and role of shareholders. Added an illustration highlighting the differences between forms of business. Included context on share repurchases. Added discussion on the alternative cash flow treatments of interest and dividend payments under IFRS. Added content related to the auditors' report and notes to the financial statements.

Chapter 2: A Further Look at Financial Statements

- Feature story is about Aritzia, its users, and use of accounting standards
- Presents the classified statement of financial position and the items typically found in each section
- Explains how ratio analysis is used to analyze a company's liquidity, solvency, and profitability
- Applies ratio analysis to two years for retailers including Aritzia, Reitmans, and their industry (working capital, debt to total assets, basic earnings per share, and price-earnings ratios)
- Describes the conceptual framework of accounting
- **Key changes:** New feature company Aritzia. Updated terminology to focus on fair value rather than current value, as this is more applicable to introductory accounting coverage. Updated definitions due to changes in the conceptual framework. Expanded references to more companies, including Exco Technologies Ltd., Cogeco Communications Inc., and CGI Group Inc. Revised Practice Using the Decision Tools to focus on Roots Corporation. Introduced the concept of data analytics and big data concepts and discussed data collection techniques in our new Analytics Mindset feature.

Chapter 3: The Accounting Information System

- Feature story is about True Büch Kombucha's experiences with an accounting information system
- Covers transaction analysis, explaining how accounts, debits, and credits are used to record transactions
- Explains the first four steps in the accounting cycle, including analyzing, journalizing, and posting transactions and preparing the trial balance
- **Key changes:** New feature company True Büch Kombucha. Revised all accounting equation analysis features using an expanded format that includes statement of income account names. This means that students are required to think about account names as soon as they start analyzing transactions, making the leap to journal entries easier when the time comes. Transactions revised to make it easier for students to understand the implications of key financing transactions. Added a new illustration to clarify how normal balances are determined and expanded the normal balance discussion.

Chapter 4: Accrual Accounting Concepts

- Feature story is about Western University's application of accrual accounting
- Explains revenue recognition, including the five-step model as it applies to both single and multiple performance obligations
- Explains expense recognition
- Emphasizes the difference between cash and accrual accounting
- Completes the accounting cycle, from adjusting entries to the closing process
- **Key changes:** Significantly expanded discussions of the revenue recognition process. This includes new content related to the five-step model, which walks students through both single and multiple performance obligations related to service contracts. Developed new DO IT! exercises to help students assess their understanding of this new material. Expanded the discussion of adjusting prepaid expenses and depreciation. Included additional material in relation to closing entries, including an expanded discussion of the purpose of the income summary account. Added end-of-chapter material at all levels (brief exercises, exercises, problems, and cases) about the new five-step revenue recognition model content.

Chapter 5: Merchandising Operations

- Feature story is about Loblaw Companies Limited's initiatives to improve its process of getting products from its suppliers to its shelves
- Identifies the key differences between service and merchandising companies

- Introduces inventory systems using the perpetual inventory system (the periodic inventory system is presented in an appendix)
- Explains how to record purchases of merchandise
- Explains revenue recognition, including the five-step model as it applies to both single and multiple performance obligations related to the sale of merchandise
- Presents single-step and multiple-step income statements
- Applies ratio analysis to Loblaw, Metro, and their industry (gross profit margin and profit margin)
- **Key changes:** Significantly expanded discussions of the revenue recognition process. This includes new content on the five-step model, which walks students through both single and multiple performance obligations related to the sale of merchandise. Developed new DO IT! exercises to help students assess their understanding of this new material. Also added new illustration for the operating cycle of a merchandising company. Added new content related to adjusting inventory for shortages at year end when using perpetual inventory systems. Removed content related to recording sales returns allowance and sales discounts in order to keep the discussion of variable consideration at an introductory level. Added discussion of other comprehensive income, comprehensive income, and the statement of comprehensive income. Revised the illustration featuring the difference between perpetual and periodic inventory systems. Added an appendix on accounting for sales returns and sales discounts under ASPE.

Chapter 6: Reporting and Analyzing Inventory

- Feature story is about lululemon athletica inc.'s inventory management
- Explains how inventory quantities and ownership are determined
- Covers cost formulas and their financial statement effects using the perpetual inventory system (the periodic inventory system is presented in an appendix)
- Discusses effects of two major types of inventory errors on financial statements
- Outlines how to value and record inventory at the lower of cost and net realizable value
- Applies ratio analysis to lululemon, Limited Brands, and their industry (inventory turnover and days in inventory)
- **Key changes:** Expanded coverage on how inventory errors reverse. Added two Analytics Mindset features to introduce the use of data when managing inventory. Introduced more coverage of internal controls consistent with control procedures covered in the *CPA Handbook*. Added new illustrations on cost flow formula differences and introduced new illustrations in appendix explaining the flow of costs from opening inventory through purchases and goods available for sale into ending inventory and cost of goods sold.

Chapter 7: Internal Control and Cash

- Feature story is about cash control at DAVIDsTEA Inc.
- Explains the components of an internal control system, including its control activities and limitations
- Identifies the key control activities over cash receipts and payments
- Discusses bank reconciliations in detail as a control feature
- Explains how cash is reported and managed
- **Key changes:** New feature story on DAVIDsTea. Expanded discussion of fraud, including the main factors contributing to fraudulent activity. Added feature discussing how businesses make payments, to provide students with additional context regarding the importance of bank reconciliations. Added an Analytics Mindset feature on intelligent cash drawers.

Chapter 8: Reporting and Analyzing Receivables

- Feature story is about NFI Group's receivables
- Presents the basic types of receivables and how to record accounts receivable transactions, including the use of subsidiary ledgers
- Explains how to account for bad debt expense, write offs, and recovery of uncollectible accounts using the allowance method
- Outlines how to account for notes receivable, interest income, and derecognizing notes
- Explains statement presentation of receivables
- Identifies the principles of accounts receivable management
- Applies ratio analysis to NFI, Grande West Transportation, and their industry (receivables turnover and average collection period)
- **Key changes:** New feature story on NFI Group. Revised text to reflect the language of IFRS 15 (such as transaction price and variable consideration). Addressed refund liabilities and estimated inventory returns. Deleted sections on sales discounts and accruing interest on overdue accounts receivable. Updated narrative to reflect the expected credit loss model from IFRS 9. Added Analytics Mindset feature related to credit granting.

Chapter 9: Reporting and Analyzing Long-Lived Assets

- Feature story is about WestJet's property and equipment
- Covers the acquisition and derecognition of property, plant, and equipment
- Reviews buy or lease decisions
- Explains the calculation and implications of using different depreciation methods
- Discusses, at the appropriate level for an introductory accounting course, the treatment of significant components, capital cost allowance, impairments, the revalua-

tion model, depreciation revisions, and natural resources and depletion

- Discusses the accounting for intangible assets and goodwill
- Reviews the reporting of long-lived assets
- Applies ratio analysis to WestJet, Air Canada, and their industry (return on assets, asset turnover, and profit margin)
- **Key changes:** Expanded coverage of natural resources and depletion. Added a DO IT! exercise on depletion and impairment. Introduced a new Decision Tool dealing with the impact of profit margin on return on assets. Added numerical example for goodwill calculations. Explained impact of IFRS 16 leasing standards change. Expanded discussion of the use of big data when managing long-lived assets and added an Analytics Mindset feature to the chapter.

Chapter 10: Reporting and Analyzing Liabilities

- Feature story is about Interfor's liabilities
- Covers current liabilities, including operating lines of credit, sales taxes, property taxes, payroll, provisions, and contingencies
- Covers interest-bearing liabilities, both current and non-current, and how to record loan payments and interest accruals
- Reviews reporting and analysis of liabilities
- Applies ratio analysis to Interfor, Canfor, and their industry (debt to total assets and times interest earned)
- Appendix covers accounting for bond liability transactions, future and present value concepts, and how to calculate bond prices
- **Key changes:** New feature story on Interfor. Updated examples related to payroll to incorporate recent changes to deduction limits. Moved coverage of all interest-bearing liabilities into one learning objective. Expanded coverage of provisions and added a DO IT! exercise on this topic. Introduced coverage of how companies use data analytics to estimate provisions. Deleted coverage of loan payments consisting of fixed principal plus interest payments because these are becoming less prevalent in practice. Added more discussion on the advantages and disadvantages of using debt financing. Added more information in the appendix on future values to foster greater understanding of present values and how they relate to bond prices and added another DO IT! exercise for this topic. Added a new Practice Using the Decision Tools, which uses West Fraser Timber Co. Ltd.

Chapter 11: Reporting and Analyzing Shareholders' Equity

- Feature story is about Leon's Furniture Limited
- Discusses corporate form of organization and its advantages and disadvantages

- Covers issues related to common and preferred shares, including reasons why companies repurchase their own shares
- Explains cash dividends, stock dividends, stock splits, and implications for analysis
- Describes the presentation of equity items in the statement of financial position and statement of changes in equity (IFRS) or statement of retained earnings (ASPE)
- Applies ratio analysis to Leon's Furniture, BMTC, and their industry (payout ratio, dividend yield, earnings per share, and return on common shareholders' equity)
- **Key changes:** Added examples of cross-listed companies and the impact on their decision to report using IFRS or U.S. GAAP. Expanded discussion of share repurchases and how they are accounted for to better reflect the extent of this type of activity by Canadian public companies. Deleted references to contributed capital, retaining references to contributed surplus. Added context to the discussion of preferred shares, including new content on rate reset and floating-rate preferred shares. Added feature on share consolidations.

Chapter 12: Reporting and Analyzing Investments

- Feature story is about Scotiabank's management of investments
- Explains why companies purchase debt and equity securities as strategic or non-strategic investments
- Describes the various valuation models for non-strategic investments: fair value through profit or loss, fair value through other comprehensive income, amortized cost, and cost
- Describes the accounting for strategic investments, including the use of the equity and cost valuation models
- Discusses other comprehensive income, including the statement of comprehensive income, and accumulated other comprehensive income
- Explains how investments are reported on the financial statements under each of the valuation models used for non-strategic and strategic investments, including the different reporting requirements under IFRS and ASPE
- Introduces consolidation accounting for financial reporting purposes at a conceptual level
- Discusses the accounting for investments in bonds and compares it with bonds payable in a chapter appendix
- **Key changes:** Introduced coverage of how equity investors use data to assess investment decisions. Expanded

discussion of fair value through other comprehensive income without adding coverage of detailed entries for this model.

Chapter 13: Statement of Cash Flows

- Feature story is about Cineplex's cash flows
- Explains the purpose and content of the statement of cash flows
- Describes the preparation of the operating, investing, and financing activities of the statement of cash flows
- Shows the use of the indirect method within the chapter and the direct method in the appendix to provide greater flexibility when determining which of these topics will be covered
- Applies ratio analysis to Cineplex, AMC, and their industry (free cash flow)
- **Key changes:** New feature story on Cineplex. Increased coverage of corporate life cycle with real company examples. Added Analytics Mindset boxes covering ways to use data to improve free cash flow. Incorporated changes in new IFRS 15 account movements when determining operating cash flows. Featured Gildan in the Practice Using Decision Tools.

Chapter 14: Performance Measurement

- Feature story is about Sobeys' business strategy, including its acquisitions and divestitures
- Demonstrates horizontal analysis, vertical analysis, and ratio analysis
- Applies ratio analysis to Sobeys, North West, and their industry (comprehensive analysis of all ratios)
- Discusses factors that can limit the usefulness of financial analysis, including the diversification of the company's operations, the use of alternative accounting policies, the use of estimates, and the impact of other comprehensive income items, discontinued operations, and nonrecurring items
- Discusses the use of non-GAAP measures
- **Key changes:** New feature story on Sobeys. Focused the chapter on integrated coverage of Sobeys and North West financial statement analysis. Added more Decision Toolkit items to focus on more specific ratios and introduced the use of data dealing with non-financial statement analysis in the Analytics Mindset feature. Covered analysis of key Netflix ratios and how they relate to pricing strategies and share price movements.

Digital Resources for Students and Instructors

Financial Accounting: Tools for Business Decision-Making, Eighth Canadian Edition, is completely integrated with *WileyPLUS*, featuring a suite of teaching and learning resources. *WileyPLUS* allows students to create a personalized study plan, assess their progress along the way, and access the content and resources needed to master the material. *WileyPLUS* provides immediate insight into students' strengths and problem areas with visual reports that highlight what's most important for both the instructor and the student. Many dynamic resources are integrated into the course to help students build knowledge and understanding, stay motivated, and prepare for decision-making in a real-world context. *WileyPLUS* also includes integrated adaptive practice that helps students build proficiency and use study time most effectively. Additional features of the *WileyPLUS* course include resources for students and instructors.

For Instructors

We offer several useful supplements and resources on the book's companion website (www.wiley.com/go/kimmelcanada) and in *WileyPLUS*. On these sites, instructors will find the Solutions Manual, PowerPoint presentations, Test Bank, Instructor's Manual, Computerized Test Bank, and other valuable teaching resources.

The supplements are prepared by subject matter experts and contributors who are often users of the text. Supplements are meticulously reviewed to ensure consistency with the textbook. Supplements like the Test Bank and the Solutions Manual are also rigorously checked to ensure accuracy.

For Students

Students will find selected support materials on the book's companion website (www.wiley.com/go/kimmelcanada) and an expanded list of resources in *WileyPLUS* that will help them develop their conceptual understanding of class material and increase their ability to solve problems. In addition to other resources, students will find:

- Multimedia tutorials
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- Account classification and presentation
- Checklist of key figures
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The Purpose and Use of Financial Statements

Simon Potter/Getty Images, Inc.



The **Feature Story** helps you picture how the chapter relates to the real world of accounting and business. You will find references to the story throughout the chapter.

Feature Story

Trading on a Long Tradition

The North West Company Inc. is one of the world's longest-running retail enterprises. It was established in Montreal in 1779 by European fur traders who helped map Canada's North. It was merged with the rival Hudson's Bay Company in 1821 and became the Northern Stores Division. A group of investors purchased the division in 1987 and, in 1992, the company began trading on the Toronto Stock Exchange as The North West Company, Inc.

The North West Company is still a fixture in Canada's North. It is the largest private employer of Indigenous peoples in Canada and serves communities ranging from 300 to 9,000 people—many of them former trading posts. Its stores carry food, clothing, housewares, appliances, and outdoor gear. Many of the stores also provide services such as fuel, a post office, pharmacy, and income tax return preparation. The challenges and costs of operating in the far North are significant, including the fact that about 40% of the company's stores cannot be accessed by all-weather roads. For example, in November 2018, a fire destroyed its warehouse in Iqaluit, after the last shipments by boat had arrived before winter. North West co-operated with a competitor to ensure that the Nunavut community had enough supplies to last the winter.

In 1992, North West began operating internationally when it acquired stores in Alaska. This was followed by a 2007

acquisition of stores in the South Pacific and Caribbean. At January 31, 2019, North West operated 193 stores in Canada, 32 in Alaska, and 20 in the South Pacific and Caribbean. These stores are operated under a number of banners, including Northern, NorthMart, Quickstop, Giant Tiger, AC Value Centers, and Cost-U-Less. The Giant Tiger stores are franchises, as is the one Tim Hortons restaurant that the company operates. Staying true to its roots, North West still has operations that purchase furs from trappers. For the fiscal year ending January 31, 2019, North West had sales of more than \$2.0 billion and profits of about \$90 million. The company's international operations generated 38% of its total revenues.

How does a company like the North West Company decide whether to expand into a new market, change its product categories, or operate as a franchisee? How are decisions made regarding what types and quantities of inventory should be carried at each store? How are pricing decisions made given the significance of transportation costs and changing foreign currency values? How does the company track consumer demands in the disparate markets it serves? Management relies on accounting as its key decision-making tool. And it's not just the company that needs financial information for making decisions. External audiences, such as banks, potential shareholders, and suppliers, also need to see the company's financial information before deciding whether to lend to, invest in, or sell to the retailer. The way the North West Company and other businesses communicate their financial information is through financial statements.¹

Chapter Preview

To be successful in business, countless decisions have to be made—and many decisions require accounting information. The purpose of this chapter is to show you accounting's role in providing useful financial information for decision-making. The material in this chapter will help you answer a number of questions, including: Who uses accounting information and how do they use it? How are businesses formed? What are the main types of business activities and how are they reported in a business's financial statements? How can you begin to interpret the information in the financial statements and use it to make decisions?

The **Chapter Preview** describes the purpose of the chapter and highlights major topics.

Chapter Outline

The **Chapter Outline** presents the chapter's learning objectives, topics, and practice opportunities to give you a framework for learning the specific concepts covered in the chapter.

LEARNING OBJECTIVES

READ

PRACTICE

| | | |
|---|---|--|
| <p>1 Identify the uses and users of accounting information.</p> | <p>Uses and Users of Accounting Information</p> <ul style="list-style-type: none"> • Internal users • External users | <p>DO IT! 1.1 Users of accounting information</p> |
| <p>2 Describe the primary forms of business organization.</p> | <p>Forms of Business Organization</p> <ul style="list-style-type: none"> • Proprietorships • Partnerships • Corporations • Generally accepted accounting principles for business organizations | <p>DO IT! 1.2 Business organizations</p> |
| <p>3 Explain the three main types of business activity.</p> | <p>Types of Business Activity</p> <ul style="list-style-type: none"> • Financing activities • Investing activities • Operating activities • Summary of business activities | <p>DO IT! 1.3 Business activities</p> |
| <p>4 Describe the purpose and content of each of the financial statements.</p> | <p>Financial Statements</p> <ul style="list-style-type: none"> • The financial statements • North West's financial statements • Elements of an annual report | <p>DO IT! 1.4a Accounting equation</p> <p>DO IT! 1.4b Financial statement relationships</p> <p>DO IT! 1.4c Preparing financial statements</p> |

Go to the *Review and Practice* section at the end of the chapter for a targeted summary and practice questions with solutions. Visit **WileyPLUS** for more practice opportunities.

Uses and Users of Accounting Information

Key terms are printed in blue when they first appear. They are listed at the end of each chapter and defined again in the glossary at the end of the book. There are many new terms in the first few chapters of the book to help you learn common business terminology.

The names of real companies are shown in **red** when first referenced in the chapter and end-of-chapter material.

LEARNING OBJECTIVE 1

Identify the uses and users of accounting information.

Accounting is the information system that identifies and records the economic events of an organization, and then communicates them to a wide variety of interested users. Why does accounting matter to these users? The world's economic systems depend on highly transparent, reliable, and accurate financial reporting. Because of this, accounting has long been labelled "the language of business."

That's one of the reasons why many Canadians, even those who do not plan on becoming accountants, study accounting. For example, Mike Cassidy, president of **Maritime Bus**; Sabrina Geremia, managing director of **Google Canada**; Monique Leroux, chair of the board of **Investissement Québec**; Craig Reynolds, CEO of the **Saskatchewan Roughriders**; Elizabeth Marshall, a senator; George Melville, chairman and owner of **Boston Pizza International**; and Joe Resnick, NHL hockey player agent, have all studied accounting in depth.

Whether you plan to become an accountant or not, a working knowledge of accounting will be relevant and useful in whatever role you assume as a user of accounting information—as an owner of your own business, working for someone else in their business, investing in a business, or simply understanding your own personal finances.

Users of accounting information can be divided broadly into two types: internal users and external users. We will discuss each of these in the sections that follow.

Internal Users

Internal users of accounting information manage companies, whether for-profit or not-for-profit, or government organizations. They work for and manage these organizations. By virtue of their position in management, **internal users** have access to internal accounting information to help them make the decisions required to run the company. These include company officers (senior management), as well as managers and directors in finance, marketing, human resources, production, and other functional areas within a company. In other words, anyone who works for a company and has access to accounting information to assist them in managing and operating the company is considered to be an internal user.

In running a business, internal users must answer many important questions, as shown in **Illustration 1.1**.





| | |
|---|---|
|  <p>Finance</p> <p>Is there enough cash to pay the bills? Do we need to borrow more money?</p> |  <p>Marketing</p> <p>What price should we sell tablets for to maximize profits? Did our advertising campaign increase sales?</p> |
|  <p>Human Resources</p> <p>How many employees can we afford to hire this year? Can we afford to negotiate salary increases?</p> |  <p>Production</p> <p>Which product line is the most profitable? Should we contract out some of our production or distribution operations?</p> |

ILLUSTRATION 1.1

Questions asked by internal users

To answer these and other questions, users need detailed accounting information on a timely basis; that is, it must be available when it is required. For internal users, accounting provides a variety of internal reports, such as financial comparisons of operating alternatives, projections of income from new sales campaigns, analyses of sales costs, and forecasts of cash needs. In addition, companies present summarized financial information in the form of financial statements for both internal and external use.

External Users

External users are not involved in managing a company and do not have access to accounting information other than that which is available to the general public. There are several types of external users of accounting information. **Investors** (owners) use accounting information to make decisions to buy, hold, or sell their ownership interest (see **Alternative Terminology**). **Creditors**, such as bankers (which are also known as **lenders**) and suppliers, use accounting

Alternative Terminology notes give synonyms for key terms that you may hear or see in the real world, as well as in this text.

ALTERNATIVE TERMINOLOGY

Investors are also known as **shareholders**. **Creditors** are also known as **lenders**.

information to evaluate the risks of lending money or of selling on credit. **Investors and creditors** are considered to be the primary users of financial accounting information.

Some questions that external users, such as investors and creditors, may ask about a company are shown in **Illustration 1.2**.

ILLUSTRATION 1.2

Questions asked by external users



Investors

- Should I purchase shares of this company?
- What is the return from my investment?



Creditors

- Will the company be able to pay its debts as they come due?
- How does the amount of funds invested by shareholders compare with the amount borrowed from creditors?

In addition to investors and creditors, there are many other external users with a variety of information needs and questions. For example, potential employees use both financial and non-financial information to learn about the company and evaluate job prospects. Current employees who are not directly involved in managing the company, as well as any labour union that may represent them, use financial information to bargain for better salaries and benefits. And taxing authorities, such as the Canada Revenue Agency, use information from a company's financial statements in assessing a company's income tax return.

Accounting systems collect vast amounts of data about the economic events experienced by a company and about the users with whom the company engages, such as suppliers and customers. Business decision makers take advantage of this wealth of data by using data analytics to make more informed business decisions. Data analytics involves analyzing data, often employing both software and statistics, to draw inferences. As both data access and analytical software improve, the use of data analytics to support decisions is becoming increasingly common at virtually all types of companies.

In order for financial information to have value to its users, whether internal or external, it must be prepared by individuals with high standards of ethical behaviour. Ethical decision-making is critical in the preparation of accounting information and to the decision makers who rely on this information.

Fortunately, most individuals in business are ethical. Their actions are both legal and responsible. They consider the organization's interests when they make decisions. Accountants and other professionals have extensive rules of professional conduct to guide their behaviour with each other and the public. In addition, most companies have codes of conduct that outline their commitment to ethical behaviour in their internal and external relationships.

DO IT! exercises prompt you to stop and practise the key points you have just studied. The Action Plan offers you tips on how to approach the exercise.

DO IT! 1.1 | Users of Accounting Information

The following is a list of questions that may be asked by different users of accounting information:

1. Will I be able to obtain enough cash to finance this month's cash shortfall?
2. Will the company be able to repay the money we lend them when the loan comes due?
3. What was the labour cost for the production of 1,000 board feet of lumber?
4. Will the company stay in business long enough to service the products I buy from it?
5. Will the company's share price go up or down in the near future?
6. In which geographical areas and age demographics are our sales increasing?
 - a. Identify the type of user who would most likely ask each of the above questions from the following list of possible users: chief financial officer, customers, investors, creditors, production manager, or marketing manager.
 - b. Indicate whether the user you chose is an internal or external user.

ACTION PLAN

- Understand the difference between internal and external users: Internal users work for the company at a management level and require access to internal accounting information to help manage and operate the company. External users are not involved in running the company and do not have access to accounting information other than that which is available to the general public.
- Understand the types of information internal and external users require to make decisions.

Solution

Try this DO IT! exercise on your own and then check your answer at the end of the chapter.

Forms of Business Organization

LEARNING OBJECTIVE 2

Describe the primary forms of business organization.

Businesses can be organized in different ways and the accounting standards they use can vary depending on the type of organization. There are three common forms of business organization: proprietorships, partnerships, and corporations.

Proprietorships

When you graduate, you might decide to start your own business. If you do, you may choose to set up a proprietorship. A **proprietorship** is a business owned by one person, known as a proprietor. It is often called a “sole” proprietorship because there is a single owner.

The proprietorship form of business organization is simple to set up and gives the owner control over the business. In most cases, only a relatively small amount of money (capital) is needed to start in business as a proprietorship. The owner receives any income, suffers any losses, and is personally liable (responsible) for all debts of the business. This is known as unlimited liability.

There is no legal distinction between the business as an economic unit and the owner. Accordingly, the life of the proprietorship is limited to the life of the owner. The business income is reported as self-employment income and taxed on the owner’s personal income tax return. However, for accounting purposes, the business records of the proprietorship must be kept separate from those related to the owner’s personal activities.

The separation of business and personal records is known in its simplest form as the reporting entity concept. The **reporting entity concept** requires that the economic activity that can be identified with a particular business be kept separate and distinct from the personal or non-business activities of the owner and of all other economic entities. The objective of the reporting entity concept is to ensure that the entity’s financial statements faithfully represent only its economic activities. This concept applies not only to proprietorships, but also to partnerships and corporations, which are discussed in the next sections.

Small service businesses such as hair salons, plumbers, and mechanics are often proprietorships, as are many small-scale farms and small retail stores.

Partnerships

Another possibility after graduating would be for you to join forces with other individuals to form a partnership. A **partnership** is a business owned by more than one person. In most respects, a partnership is similar to a proprietorship except that there is more than one owner.

Partnerships are often formed because one person does not have enough economic resources to start or expand the business, or because partners bring unique skills or other resources to the partnership.

Partnerships are normally formalized in a written partnership agreement that outlines the formation of the partnership, partners' contributions, how net income and losses are shared, provisions for withdrawals of assets and/or partners, dispute resolution, and partnership liquidation. The need to develop a partnership agreement makes establishing a partnership more complex and costly than establishing a proprietorship. Although there are advantages to working with others, there are also disadvantages. Each partner generally has unlimited liability for all debts of the partnership, even if one of the other partners created the debt. However, there are certain situations where partnerships can be formed with limited liability for selected partners.

Similar to a proprietorship, the income of the partnership is reported as self-employment income and taxed on each partner's personal income tax return. In addition, the reporting entity concept requires that partnership records be kept separate from each partner's personal activities.

Partnerships are typically used to organize professional service businesses, such as the practices of lawyers, doctors, architects, engineers, and accountants.

Corporations

As a third alternative after graduating, you might choose to form a business as a corporation. A **corporation** is a business organized as a separate legal entity owned by shareholders and is the most complex and costly form of business to establish. The **North West Company** in our opening feature story is a corporation. As an investor in a corporation such as The North West Company, you receive shares to indicate your ownership claim (see **Alternative Terminology**). It is often possible for individuals to become owners of shares (shareholders) by investing relatively small amounts of money.

Suppose that you are one of North West's shareholders. The amount of cash that you have in your personal bank account and the balance you owe on your personal car loan are not reported in North West's financial statements. Similar to proprietorships and partnerships, you and the company are separate reporting entities under the reporting entity concept.

Since a corporation is a separate legal entity, its life is indefinite. That means it continues on regardless of who owns its shares. It is not affected by the withdrawal, death, or incapacity of an owner, as is the case in a proprietorship or partnership. In fact, North America's oldest corporation, the **Hudson's Bay Company**, was formed in 1670.

There are other factors that need to be considered when deciding which organizational form of business to choose. As we discussed earlier, if you choose to organize as a proprietorship or partnership, you are personally liable for all debts of the business. Shareholders are not responsible for corporate debts unless they have provided a personal guarantee to the lender for them. Most shareholders enjoy limited liability since their risk of loss is limited to the amount they have invested in the company's shares. This limited liability is a significant advantage for the corporate form of organization.

All of these advantages taken together—indefinite life, ease of transferring ownership when selling shares, and limited liability—can make it easier for corporations, especially large corporations, to raise capital (cash) compared with proprietorships and partnerships. Another potential advantage is that corporations may receive a more favourable income tax treatment than other forms of business organization such as proprietorships and partnerships. Because of the wide variety of income tax issues that apply to different companies in different jurisdictions, you would be wise to seek professional advice on taxation matters before choosing any form of business organization.

Although the combined number of proprietorships and partnerships in Canada is more than the number of corporations, the revenue produced by corporations is far greater. Most of the largest businesses in Canada—for example, **Alimentation Couche-Tard**, **Royal Bank of Canada**, **Power Corporation of Canada**, **Loblaw Companies**, **Great-West Life**, **Suncor**, **Imperial Oil**, and **Empire Company**—are corporations. Recently, the top 15 of Canada's largest corporations each reported annual revenues ranging from \$34.7 billion to \$78.8 billion.²

ALTERNATIVE TERMINOLOGY

Shares are also known as stock.