

ACCOUNTING IN ACTION 2

The Building Blocks of Accounting

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Ethics In Financial Reporting

Standards of conduct by which one's actions are judged as right or wrong, honest or dishonest, fair or not fair, are **Ethics**.

- Recent financial scandals include: Enron, WorldCom, HealthSouth, AIG, and others.
- Congress passedSarbanes-Oxley Act of 2002.
- Effective financial reporting depends on sound ethical behavior.

Chapter 1-2

LO 3 Understand why ethics is a fundamental business concept.

Ethics

Review Question

Ethics are the standards of conduct by which one's actions are judged as:

- a. right or wrong.
- b. honest or dishonest.
- c. fair or not fair.
- d. all of these options.

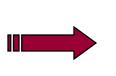
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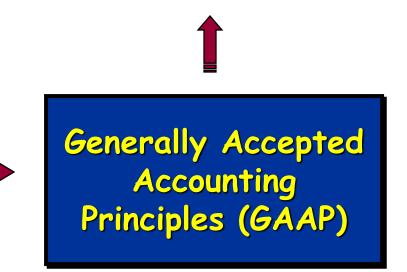
Various users need financial information



Financial Statements

- Balance Sheet
- Income Statement
- Statement of Owner's Equity
- Statement of Cash Flows
- Note Disclosure

The accounting profession has attempted to develop a set of standards that are generally accepted and universally practiced.



Chapter

1-5 LO 4 Explain generally accepted accounting principles and the cost principle.

Organizations Involved in Standard Setting:



Securities and Exchange Commission (SEC)

http://www.sec.gov/



Financial Accounting Standards Board (FASB)

http://www.fasb.org/



International Accounting Standards Board (IASB) <u>http://www.iasb.org/</u>

Chapter

1-6 LO 4 Explain generally accepted accounting principles and the cost principle.

Cost Principle (Historical) - dictates that companies record assets at their cost.

Issues:

- Reported at cost when purchased and also over the time the asset is held.
- Cost easily verified, whereas market value is often subjective.
- Fair value information may be more useful.

^{Chapter} 1-7 LO 4 Explain generally accepted accounting principles and the cost principle. **Monetary Unit Assumption** – include in the accounting records only transaction data that can be expressed in terms of money.

Economic Entity Assumption - requires that activities of the entity be kept separate and distinct from the activities of its owner and all other economic entities.

- Proprietorship.
- Partnership.
- Corporation.



LO 5 Explain the monetary unit assumption and the economic entity assumption.

Forms of Business Ownership

Proprietorship

- Generally owned by one person.
- Often small service-type businesses
- Owner receives any profits, suffers any losses, and is personally liable for all debts.

Partnership

- Owned by two or more persons.
- Often retail and service-type businesses
- Generally unlimited personal liability
- Partnership agreement

Corporation

- Ownership divided into shares of stock
- Separate legal entity organized under state corporation law
- Limited liability

LO 5 Explain the monetary unit assumption and the economic entity assumption.

Review Question

Combining the activities of Kellogg and General Mills would violate the

a. cost principle.

- b. economic entity assumption.
- c. monetary unit assumption.
- d. ethics principle.

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Forms of Business Ownership

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A business organized as a separate legal entity under state law having ownership divided into shares of stock is a

- a. proprietorship.
- b. partnership.
- c. corporation.
- d. sole proprietorship.

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