Al-Mustaqbal university college

ACCOUNTING IN ACTION 2

The Building Blocks of Accounting

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Chapter
1-1

The Building Blocks of Accounting

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.

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.

Generally Accepted Accounting Principles (GAAP)

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

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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) http://www.iasb.org/

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

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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.

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

Assumptions

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.

Forms of Business Ownership

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

Forms of Business Ownership

Proprietorship	Partnership	Corporation
• Generally owned by one person. • Often small service-type businesses • Owner receives any profits, suffers any losses, and is personally liable for all debts.	• Owned by two or more persons. • Often retail and service-type businesses • Generally unlimited personal liability • Partnership agreement	• 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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A business organized as a separate legal entity under state law having ownership divided into shares of stock is a

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b. partnership.

c. corporation.

d. sole proprietorship.

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