

Understanding Financial Accounting

Second Canadian Edition

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The first edition of *Understanding Financial Accounting* was based on
Financial Accounting: A User Perspective, Sixth Canadian Edition

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About the Author



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CHRISTOPHER BURNLEY, FCPA, FCA, is a professor in the Accounting Department at Vancouver Island University's Faculty of Management. Prior to his full-time academic career, Chris worked for 12 years in public practice and also audited federal 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.

At Vancouver Island University (VIU), Chris has developed a number of new courses, has served as departmental chair, and

served two terms as an elected faculty representative on the university's board of governors. He is active internationally, teaching and delivering guest lectures at VIU's partner institutions in Europe, Asia, and the South Pacific. He has been awarded numerous internal and external grants in support of his academic work and has presented at national conferences. Chris has also taught in the Master of Professional Accounting Program at the Edwards School of Business at the University of Saskatchewan, where he was recognized by the university with the Chartered Professional Accountants of Alberta teaching excellence award.

Chris has received a number of awards from the Canadian Academic Accounting Association for his academic work, including awards for case authoring and developing innovative ideas in accounting education.

Chris is active in the accounting profession, serving as a director on the board of the Chartered Professional Accountants of British Columbia, and is a past chair of the board of the Chartered Professional Accountants' Education Foundation of BC. In 2007, Chris was awarded the Ritchie W. McCloy Award for CA Volunteerism. Chris is also a co-author of the textbook *Financial Accounting: Tools for Business Decision-Making*, published by John Wiley & Sons Canada, Ltd.

The aim of *Understanding Financial Accounting* is to introduce students to the core concepts of financial accounting by illustrating the relevance of the material to a wide variety of decision-making contexts. The focus is on providing students with the tools to help them understand the rationale behind the numbers. If students can develop an understanding of the language of accounting, grasp what the accounting information means, and appreciate what managers are saying when they present the financial information, they will have laid a foundation they can build upon in whatever position they hold in the future.

The material is written at a level meant to be understandable for all students who put the time into working through it. It is based on 18 years of teaching the material to thousands of students with a wide variety of backgrounds, the majority of whom have been non-accounting majors, but also to others who have gone on to medal on national professional accounting exams.

Continuing Features

Cohesively Structured Content

The text has been structured around a series of **core questions** that students may ask themselves about the chapter topics and that they need to be able to answer in order to achieve the learning objectives. The material that follows each question then becomes more relevant to the students and provides them with a clear picture of why they need to understand it. The text also walks students through the basic mechanical elements of financial accounting, because it is very difficult for students to understand accounting information if they lack an understanding of the system used to generate it.

The Take 5 Videos

Each chapter includes a number of whiteboard screen capture videos that students can preview before coming to class or use for review after. These videos are a great tool for instructors who like to flip their classroom. In addition, new Take 5 Videos developed for this edition focus on solution walkthroughs of the end-of-chapter review problems that are in the text.

Opportunities for Classroom Discussion

Each chapter of the text includes features that can form the basis for classroom discussions. These include the **Ethics in Accounting** feature that highlights ethical issues that must be dealt with in relation to all kinds of accounting situations, the **For Example** feature that showcases and interprets financial statements of real companies, and the **Conceptual Framework** feature that discusses the theory behind accounting practices.

Unparalleled Review and Practice Opportunities

Concise and to-the-point chapter summaries recap the key points covered by each learning objective. Chapter End Review Problems, with accompanying Take 5 videos, walk the student through the steps required to solve complex problems.

Each chapter includes a variety of assignment material, enabling faculty to choose the level of breadth and depth at which they want to assess the students. This includes Discussion Questions, Application Problems (now expanded and divided into two sets), User Perspective Problems, Reading and Interpreting Financial Statements problems, and small Cases.

Key Enhancements

This second edition of *Understanding Financial Accounting* builds on the strength of the innovative first edition. All content has been carefully reviewed and revised to maximize student understanding. Significant work has gone into enhancing the reading content, the assessment material, and the material available in the *WileyPLUS* course.

Tightened Linkages between the Reading Content and the WileyPLUS Course

WileyPLUS is an innovative, research-based online environment for effective teaching and learning. Among its many features, *WileyPLUS* allows students to study and practise using the digital textbook, quizzes, and algorithmic exercises. The immediate feedback helps students understand where they need to focus their study efforts.

Based on cognitive science, *WileyPLUS* with ORION is a personalized adaptive learning experience that gives students the practice they need to build proficiency on topics while using their study time more effectively. The adaptive engine is powered by hundreds of unique questions per chapter, giving students endless opportunities for practice throughout the course. Orion is available with all chapters of this text.

This edition makes a clear link between the reading content and the wealth of pedagogical material available in the *WileyPLUS* course. The new **Assess Your Understanding** box at the end of many chapter sections directs students to the relevant Demonstration Problems in the *WileyPLUS* course. Additional Demonstration Problems are in *WileyPLUS* and there is now a companion Demonstration Problem for every Chapter End Review Problem, doubling the opportunities for students to practise working through problems.

Augmented End-of-Chapter Material

Revisions based on faculty and student usage data. The all-important end-of-chapter material has been

significantly revised. These revisions were data-driven. Data from *WileyPLUS* was used to determine the questions most frequently assigned by faculty and the questions most often attempted by students. The number of popular end-of-chapter questions has been significantly increased, while infrequently assigned questions were removed. For example, the number of Application Problems has doubled, to more than 350.

Mirror problem set ‘B’ introduced for Application Problems. The Application Problems have been grouped into two sets, A and B, whose topics mirror each other, so they can be assigned separately or together for extra practice. The Application Problems are now organized by learning objective to better test students’ understanding of each objective and to make it easier for faculty to quickly identify relevant problem material.

Unique, new Work In Progress problems. A new type of problem, Work In Progress, was added, which enhances students’ critical thinking and communication skills by requiring them to correct or improve a statement about key concepts in the chapter.

Other additions and changes. The number of Discussion Questions and User Perspective Problems has been increased by roughly 20%. Finally, all Reading and Interpreting Published Financial Statements problems have been revised to reflect the most recent publicly available financial statements.

Current Accounting Standards

This edition has been revised to reflect new financial reporting standards, such as IFRS 15 (Revenue from contracts with customers) and IFRS 16 (Leases). The text covers in depth the five-step revenue recognition model and the impact of the new IFRS 15 on sales discounts, warranties, sales returns, gift cards, and loyalty programs. Chapter 4 was completely rewritten to reflect IFRS 15, and now provides the most comprehensive revenue recognition coverage of any introductory financial accounting text.

Enhanced Coverage in Several Areas

This edition has enhanced the discussion in several areas. For example, material has been added to Chapter 6 related to the responsibility for and limitations of internal controls, while content has been added to Chapter 11 on the types of preferred shares and why they are considered to be hybrid securities. As well, the number of For Example feature boxes has increased by more than 50%, to provide students with even more real-life examples to illustrate concepts.

Enhanced Self-Assessment Opportunities

This edition has strengthened the opportunities for students to assess their mastery of the content. At the end of many sections is a new feature, Assess Your Understanding, which directs students to the Chapter End Review Problems and *WileyPLUS* Demonstration Problems relevant to that topic and learning objective. This makes it much easier for students to know what material they should attempt to ensure that they understand the related content. The number of Chapter End Review Problems

has more than doubled. Fully annotated solutions are provided for all of the Chapter End Review Problems, and additional Take 5 videos have been created to support students by walking them through the most difficult of these.

Specific Chapter Enhancements

The following are the notable revisions, additions, and improvements to the chapters in this second edition.

Chapter 1. Overview of Corporate Financial Reporting

- The discussion of financial accounting’s focus on external users was expanded.

Chapter 2. Analyzing Transactions and Their Effects on Financial Statements

- Content was added on dual-listed companies, Ontario Securities Commission reporting deadlines, and the requirement for external audit.
- The revenue recognition criteria were replaced with the five-step model for revenue recognition, in accordance with IFRS 15.
- The definition of what it means when an expense is incurred was enhanced.
- The graphical presentation of the qualitative characteristics from the conceptual framework was revised.

Chapter 3. Double-Entry Accounting and the Accounting Cycle

- The chapter was revised to more clearly distinguish adjusting entries from regular journal entries.
- Sample adjusting journal entries were added, together with examples from public companies.

Chapter 4. Revenue Recognition and the Statement of Income

- The chapter was completely rewritten to reflect IFRS 15.
- Information was added on the contract-based approach.
- The five-step model for revenue recognition was added, using a question-based approach to move through the model. Examples presented included the sale of goods, the provision of services, and a sale with multiple performance obligations.
- Details were added to focus on four contractual arrangements that affect the recognition of revenue: sales with right of return, warranties, consignment arrangements, and third-party sale arrangements.
- Accounts were changed to be consistent with IFRS 15 (for example, the Sales Discounts and Sales Returns and Allowances accounts were removed).

Chapter 5. The Statement of Cash Flows

- The coverage was enhanced of options for classifying cash flows related to interest and dividends paid and received.
- The section on non-cash investing and financing activities was expanded.

- An exhibit was added outlining how changes in current asset and liability accounts impact cash flows.
- A For Example box was added providing more details on how changes in working capital items affect cash flows from operating activities.
- A For Example box was added linking the components of the statement of financial position to the statement of cash flows classification.

Chapter 6. Cash and Accounts Receivable

- Coverage of the responsibility for and limitations of internal controls was added.
- An exhibit was added to reflect the effect of journal entries flowing from the bank reconciliation.

Chapter 7. Inventory

- A section was added on the types of inventory errors and the impact they have on the financial statements.
- A learning objective was added on cost formulas under periodic inventory systems.
- The discussion of the gross margin inventory estimation method was expanded.
- Examples were added of public companies using each inventory cost formula.

Chapter 8. Long-Term Assets

- Examples were added of public companies using each depreciation method.
- Content was added regarding fully depreciated property, plant, and equipment (PP&E), idle PP&E, and PP&E held for sale.
- An exhibit was added to show how to determine the carrying amount if impairment charges are recognized.

- Examples of intangible assets of public companies were expanded.

Chapter 9. Current Liabilities

- The chapter was revised to reflect the impact of the new IFRS 15 regarding revenue recognition on gift cards, customer loyalty programs, and warranties.
- The core question on gift cards and loyalty programs was split into two questions.
- The terminology used in the unearned revenues discussion was updated to reflect the terminology in the new standard.
- The core question on accounting for warranties was completely rewritten to reflect the new accounting standards.

Chapter 10. Long-Term Liabilities

- The chapter was revised to reflect the new IFRS 16, Leases.

Chapter 11. Shareholders' Equity

- Content was added on types of preferred shares and on preferred shares as hybrid securities.
- Several new For Example boxes were added to provide more context for multiple types and classes of shares, share buybacks, initial public offerings and underwriting costs, non-voting shares, redeemable preferred shares, convertible preferred shares, and stock splits.

Chapter 12. Financial Statement Analysis

- The chapter was updated to reflect the new IFRS auditor reporting standard.
- A new learning objective was added, covering commonly used non-IFRS financial measures and other industry metrics.

Acknowledgements

The text's cover photo, taken not far from my home on eastern Vancouver Island, features an arbutus tree stretching out from the shoreline of the Salish Sea in search of the sun. Arbutus trees, which are Canada's only native broadleaved evergreen tree, are found along the coast in southern British Columbia. The arbutus tree is honoured by the Coast Salish peoples as their tree of knowledge because it knows how to find the sun. The Coast Salish also recognize it for its strength, which comes from its deep roots and strong inner core. The arbutus tree provides a wonderful metaphor for this text in a number of ways.

This edition draws strength from the roots put down by the first edition of the text. I would like to thank the students and faculty who provided feedback to improve this edition. This text's core is also strengthened as a result of the problem material that has been drawn from *Financial Accounting: A User Perspective*. I am indebted to Maureen Fizzell, Donald Cherry, and Robert Hoskin for authoring

such rich, diverse material. The Hoskin text was one of the books I used when I began teaching financial accounting and it helped inform and shape the way I continue to present this material. These teachings continue to be reflected in this text.

Arbutus trees require very specific environmental conditions and are only found within about 8 km of the Pacific Ocean. Any new growth also requires the right environmental conditions. I have been fortunate to work with a group of colleagues at Vancouver Island University who have supported my teaching and writing over the past 18 years. I have learned from each of them and would like to thank them, especially Gordon Holyer, Tracy Gillis, Colin Haime, Sameer Mustafa, Erin Egeland, Jeremy Clegg, Vanessa Oltmann, and Steve Purse. I have also been fortunate to work with four deans of the Faculty of Management: Ian Ross, Mike Mann, David Twynam, and Suzanne Flannigan. Each created opportunities for me to grow and provided the space in which growth could occur.

I am indebted to a number of accounting academics without whom I would never have considered authoring a text. The efforts of Sandy Hilton, especially at the Canadian Academic Accounting Association, to create venues to support teaching and learning for faculty made a significant difference to me. Sandy has also supported my case authoring efforts for years and provided excellent advice at the outset of this project. Peter Norwood has created numerous opportunities for me to broaden my participation in the academic community and also willingly shared wisdom garnered from his years as a successful author. Scott Sinclair's feedback throughout in the development of the first edition resulted in a much improved text. I am also thankful for the advice and encouragement of Irene Gordon, Gary Spraakman, and Eldon Gardner in my earliest efforts as an author.

As a tree grows, new rings are added to its trunk. Many people have contributed growth rings to this text. Vito Di Turi, with whom I began my accounting journey some 30 years ago, made a significant contribution to this edition by developing much of the new problem material. Cecile Laurin and Maria Belanger also made noteworthy contributions to text and the end-of-chapter material. Julia Scott and Peggy Wallace both contributed to a number of chapters in the first edition of this text. Laurel Hyatt's research work has made for interesting opening vignettes, while her talents as an editor greatly improved the readability of the text. The editorial contributions of Tania Cheffins and Belle Wong are greatly appreciated. The project management expertise of Denise Showers and the typesetting team at Aptara is also greatly valued. I consider myself so fortunate to be part of the Wiley family. Their dedicated team provided outstanding support each step of the way. I am indebted to Zoë Craig for helping frame the initial vision and for her continuous encouragement throughout the process. The editorial talents of Dela Hirjikaka added much to the text and her efforts kept the project on track, bringing the numerous parts together in a seamless fashion. I am also thankful for the support of Meaghan MacDonald, Deanna Durnford, Karen Staudinger, Anita Osborne, and Joanna Vieira.

A number of faculty have also worked hard to develop the supplements that accompany this text:

Maria Belanger, Algonquin College
 Jeremy Clegg, Vancouver Island University
 Rosalie Harms, University of Winnipeg
 Amy Hoggard, Camosun College
 Sandy Kizan, Athabasca University
 Cecile Laurin, Algonquin College
 Debbie Musil, Kwantlen Polytechnic University
 Joel Shapiro, Ryerson University
 Laura Simeoni, York University
 Marie Sinnott, College of New Caledonia
 Vito Di Turi, University of Ottawa (Sessional)

Many other faculty reviewed the text at various stages of development, providing advice and constructive criticism that resulted in a better offering. I would like to thank them for their insights.

Manuscript development stage (first edition)

Ibrahim Aly, Concordia University
 George Boland, Queen's University
 Else Grech, Ryerson University

Sohyung Kim, Brock University
 Jennifer Li, Brock University
 Anne Macdonald, Simon Fraser University
 Robert Madden, St. Francis Xavier University
 Julie McDonald, Ryerson University
 Jaime Morales, Trent University
 Peter Norwood, Langara College
 Sandy Qu, York University
 Scott Sinclair, University of British Columbia
 Sara Wick, University of Guelph

First edition

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 Concordia University
 Brenda Collings, University of New Brunswick Saint John
 Erin Egeland, Vancouver Island University
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 Steve Gibson, Simon Fraser University (Burnaby Campus)
 Len Hostin, McMaster University
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 Robert Madden, St Francis Xavier University

Just as trees use the magic of photosynthesis to transform light energy into chemical energy, a magical process takes place in classrooms at campuses the world over. Much of what is best about this product has resulted from such classroom interactions. The echoes of the hundreds of introductory accounting classes and seminars I have taught over the past 18 years can be heard throughout the pages of this text. So much of what I have learned about presenting this material is thanks to the thousands of students from these classes. I am so thankful for the shared learning experience.

The strength of a tree is provided by its heartwood, so it is no surprise that, for this text, strength came from the people closest to my own heart. I am grateful for a wonderful collection of family and friends. Two key supports were my mother, Bernette, and my sister, Faith. My children, Jacob and Erin, have been a constant source of inspiration and have patiently dealt with me disappearing into my office for long hours of writing and have tolerated the working edition of the text as a constant presence wherever we are. I am most indebted to my partner and best friend, Caroline. She has always encouraged me to take on new challenges, providing constant and unwavering support. Caroline has inspired so much of what is wonderful in my life and this book is just another example of that.

I hope that the text will help you to develop your own strong understanding of financial accounting. Feedback and suggestions for improving future editions are welcome. Please email them to BurnleyAuthor@gmail.com.

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January 2018

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APPENDIX A Specimen Financial Statements: Dollarama Inc. A-1