



VICTOR_KOCHETKOV/SHUTTERSTOCK.COM

Chapter 1 Introduction to Accounting

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In addition to a system that links customers with private jet service, Jets.com needs a system to account for its business transactions. Thus, it employs accounting professionals who understand the accounting process and generally accepted accounting principles.

Welcome to the world of accounting. We are delighted that you have decided to join us. A solid foundation in accounting concepts and techniques will serve you well. This is true whether you accept a professional position in accounting, work for or own a business, or simply seek a better understanding of your personal finances.

Oh, and what does it cost to take a private jet to the Super Bowl? Rates run from \$5,500 to \$15,000 per hour on one of the busiest weekends of the year.

LEARNING OBJECTIVES

Careful study of this chapter should enable you to:

- LO1** Describe the purpose of accounting.
- LO2** Describe the accounting process.
- LO3** Define GAAP and describe the process used by FASB to develop these principles.
- LO4** Define three types of business ownership structures.
- LO5** Classify different types of businesses by activities.
- LO6** Identify career opportunities in accounting.

Accounting is the language of business. You must learn this language to understand the impact of economic events on a specific company. Common, everyday terms have very precise meanings when used in accounting. For example, you have probably heard terms like asset, liability, revenue, expense, and net income. Take a moment to jot down how you would define each of these terms. After reading and studying Chapter 2, compare your definitions with those developed in this text. This comparison will show whether you can trust your current understanding of accounting terms. Whether you intend to pursue a career in accounting or simply wish to understand the impact of business transactions, you need a clear understanding of this language.

LO1

The Purpose of Accounting

Describe the purpose of accounting.

The purpose of accounting is to provide financial information about the current operations and financial condition of a business to individuals, agencies, and organizations. As shown in Figure 1-1, owners, managers, creditors, and government agencies all need accounting information. Other users of accounting information include customers, clients, labor unions, stock exchanges, and financial analysts.

FIGURE 1-1 Users of Accounting Information

| USER | INFORMATION NEEDED | DECISIONS MADE BY USERS |
|--|--|--|
| Owners—Present and future | Company's profitability and current financial condition. | If business is good, owners may consider making additional investments for growth. If business is poor, they may want to talk to management to find out why and may consider closing the business. |
| Managers—May or may not own business | Detailed measures of business performance. | Managers need to make operating decisions. How much and what kinds of inventory should be carried? Is business strong enough to support higher wages for employees? |
| Creditors—Present and future | Company's profitability, debt outstanding, and assets that could be used to secure debt. | Should a loan be granted to this business? If so, what amount of debt can the business support, and what interest rate should be charged? |
| Government Agencies—National, state, and local | Company's profitability, cash flows, and overall financial condition. | The IRS enforces U.S. tax laws to determine how much income tax the business must pay. Local governments may be willing to adjust property taxes paid by the business to encourage it to stay in town. |

LO2

The Accounting Process

Describe the accounting process.

Accounting is a system of gathering financial information about a business and reporting this information to users. The six major steps of the accounting process are analyzing, recording, classifying, summarizing, reporting, and interpreting (Figure 1-2). Computers are often used in the recording, classifying, summarizing, and reporting steps. Whether or not computers are used, the accounting concepts and techniques are the same. Information entered into the computer system must reflect a proper application of these concepts. Otherwise, the output will be meaningless.

FIGURE 1-2 The Accounting Process

- **Analyzing** is looking at events that have taken place and thinking about how they affect the business. This first step in the accounting process usually occurs when the business receives some type of information, such as a bill, that needs to be properly entered into the business's records. This first step also involves deciding if the piece of information should result in an accounting entry or not.
- **Recording** is entering financial information about events into the accounting system. Although this can be done with paper and pencil, most businesses use computers to perform routine record-keeping operations.
- **Classifying** is sorting and grouping similar items together rather than merely keeping a simple, diary-like record of numerous events.
- **Summarizing** is the aggregation of many similar events to provide information that is easy to understand. For example, a firm may buy and sell baseballs during the year. Summarizing provides information on the total baseballs bought and sold and the change in the number of baseballs held from the beginning to the end of the period.
- **Reporting** is telling the results. In accounting, it is common to use tables of numbers to report results.
- **Interpreting** is deciding the meaning and importance of the information in various reports. This may include ratio analysis to help explain how pieces of information relate to one another.

LO3**Generally Accepted Accounting Principles (GAAP)**

Define GAAP and describe the process used by FASB to develop these principles.

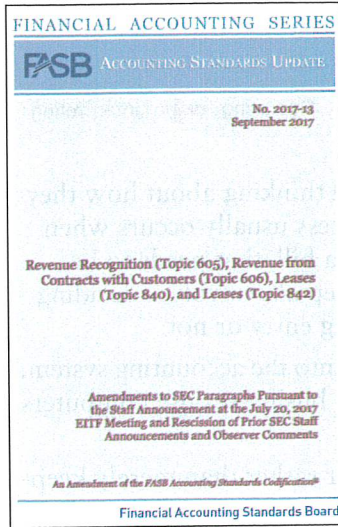
Soon after the stock market crash of 1929, the federal government established the Securities and Exchange Commission (SEC). The purpose of this government agency is to help develop standards for reporting financial information to stockholders. The SEC currently has authority over companies publicly traded on the major stock exchanges (New York and NASDAQ). It has the power to require these firms to follow certain rules when preparing their financial statements. These rules are referred to as **generally accepted accounting principles (GAAP)**.

Rather than developing GAAP on its own, the SEC encouraged the creation of a private standard-setting body. It did so because it believed the private sector had better access to the resources and talent necessary to develop these standards. Since 1973, the Financial Accounting Standards Board (FASB) has filled this role. In developing accounting standards, FASB follows a specific process and relies on the advice of many organizations. When an accounting issue is identified, the following steps are followed:

1. The issue is placed on FASB's agenda. This lets everyone know that the Board plans to develop a standard addressing this issue.
2. After researching an issue, FASB issues a **Preliminary Views** document. This document identifies the pros and cons of various accounting treatments for an event and invites others to comment.
3. To gather additional views on the issue, the Board will often hold **public hearings** around the country. Interested parties are invited to express their opinions at these hearings.



SOURCE: FINANCIAL ACCOUNTING
STANDARDS BOARD



4. Following these hearings, the Board issues an **Exposure Draft**. This document explains the rules that FASB believes firms should follow in accounting for this event.
5. After considering feedback on the Exposure Draft, the Board issues a final **Accounting Standards Update** which amends the **Financial Accounting Standards Board Accounting Standards Codification**. This Codification is an electronic database that provides one authoritative source for the standards that must be followed by U.S. companies.

Throughout this process, many parties participate by testifying at public hearings or by sending letters to the Board explaining why they agree or disagree with the proposed standard. These parties include the American Institute of Certified Public Accountants (AICPA), the American Accounting Association (AAA), the Institute of Management Accountants (IMA), Financial Executives International (FEI), corporate executives and accountants, representatives from the investment community, analysts, bankers, industry associations, and the SEC and other government agencies. Clearly, FASB considers the views of a wide range of parties. By doing so, it maximizes the likelihood of developing and gaining acceptance of the most appropriate accounting and disclosure requirements.

The International Accounting Standards Board (IASB) issues accounting standards followed by many firms in countries outside the United States. These are called International Financial Reporting Standards (IFRS). In recent years, the IASB and FASB have worked together to try to minimize the differences in these standards. These standards may eventually converge into one set of standards used around the world.

LO4

Define three types of business ownership structures.

Three Types of Ownership Structures

One or more persons may own a business. Businesses are classified according to who owns them and the specific way they are organized. Three types of ownership structures are (1) sole proprietorship, (2) partnership, and (3) corporation (Figure 1-3). Accountants provide information to owners of all three types of ownership structures.

FIGURE 1-3 Types of Ownership Structures—Advantages and Disadvantages

| TYPES OF OWNERSHIP STRUCTURES | | |
|--|--|--|
| <p>Sole Proprietorship</p> <ul style="list-style-type: none"> • One owner • Owner assumes all risk • Owner makes all decisions | <p>Partnership</p> <ul style="list-style-type: none"> • Two or more partners • Partners share risks • Partners may disagree on how to run business | <p>Corporation</p> <ul style="list-style-type: none"> • Stockholders • Stockholders have limited risk • Stockholders may have little influence on business decisions |

Most businesses in the United States operate as sole proprietorships or partnerships. However, corporations earn the highest amount of revenue.

Sole Proprietorship

A **sole proprietorship** is owned by one person. The owner is usually called a proprietor. The proprietor often manages the business. The owner assumes all risks for the business, and personal assets can be taken to pay creditors. The advantage of a sole proprietorship is that the owner can make all decisions.

Partnership

A **partnership** is owned by more than one person. One or more partners may manage the business. Like proprietors, partners assume the risks for the business, and their assets may be taken to pay creditors. An advantage of a partnership is that owners share risks and decision making. A disadvantage is that partners may disagree about the best way to run the business.

Corporation

A **corporation** is owned by stockholders (or shareholders). Corporations may have many owners, and they usually employ professional managers. The owners' risk is usually limited to their initial investment, and they often have very little influence on the business decisions.

The largest corporations in the United States are known as the "Fortune 500."

LO5 Types of Businesses

Classify different types of businesses by activities.

Businesses are classified according to the type of service or product provided. Some businesses provide a service. Others sell a product. A business that provides a service is called a **service business**. A business that buys a product from another business to sell to customers is called a **merchandising business**. A business that makes a product to sell is called a **manufacturing business**. You will learn about all three types of businesses in this book. Figure 1-4 lists examples of types of businesses organized by activity.

FIGURE 1-4 Types and Examples of Businesses Organized by Activities

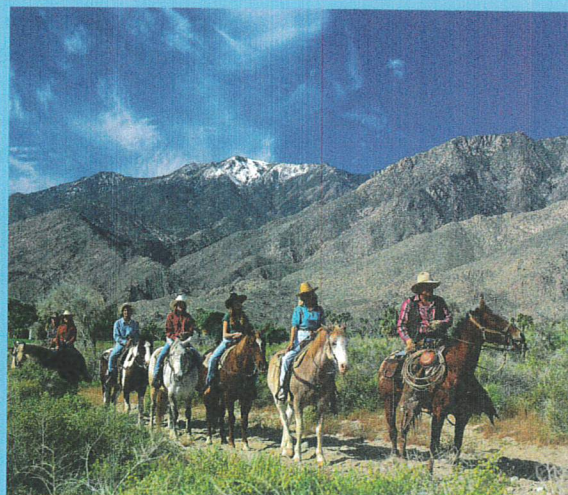
| SERVICE | MERCHANDISING | MANUFACTURING |
|---------------------|------------------|-------------------------|
| Travel Agency | Department Store | Automobile Manufacturer |
| Computer Consultant | Pharmacy | Furniture Maker |
| Physician | Grocery Store | Toy Factory |

A BROADER VIEW

All Kinds of Businesses Need Accounting Systems

Even small businesses like those that provide guided horseback tours of the Rocky Mountains need good accounting systems. Proper records must be maintained for the cost of the horses, feed, food served, tour guides' salaries, and office expenses. Without this information, the company would not know how much to charge and whether a profit is made on these trips.

JACK HOLLINGSWORTH/CORBIS



LO6

Career Opportunities in Accounting

Identify career opportunities in accounting.

Accounting offers many career opportunities. The positions described below require varying amounts of education, experience, and technological skill.

Accounting Clerks

Businesses with large quantities of accounting tasks to perform daily often employ **accounting clerks** to record, sort, and file accounting information. Often, accounting clerks will specialize in cash, payroll, accounts receivable, accounts payable, inventory, or purchases. As a result, they are involved with only a small portion of the total accounting responsibilities for the firm. Accounting clerks usually have at least one year of accounting education.

Bookkeepers and Para-Accountants

Bookkeepers generally supervise the work of accounting clerks, help with daily accounting work, and summarize accounting information. In small-to-medium-sized businesses, the bookkeeper may also help managers and owners interpret the accounting information. Bookkeepers usually have one to two years of accounting education and experience as an accounting clerk.

Para-accountants provide many accounting, auditing, or tax services under the direct supervision of an accountant. A typical para-accountant has a two-year degree or significant accounting and bookkeeping experience.

Accountants

The difference between accountants and bookkeepers is not always clear, particularly in smaller companies where bookkeepers also help interpret the accounting information. In large companies, the distinction is clearer. Bookkeepers focus on the processing of accounting data. **Accountants** design the accounting information system and focus on analyzing and interpreting information. They also look for important trends in the data and study the impact of alternative decisions.

Most accountants enter the field with a college degree in accounting. In fact, since many states require 150 credit hours to sit for the CPA exam, many students are also earning a master's degree in accounting before entering the profession. Accountants are employed in public accounting, private (managerial) accounting, and governmental and not-for-profit accounting (Figure 1-5).

FIGURE 1-5 Accounting Careers

| ACCOUNTING CAREERS | | |
|--|--|--|
| <p>Public Accounting</p> <ul style="list-style-type: none"> • Auditing • Taxation • Management Advisory Services | <p>Private Accounting</p> <ul style="list-style-type: none"> • Accounting Information Systems • Financial Accounting • Cost Accounting • Budgeting • Tax Accounting • Internal Auditing | <p>Governmental and Not-for-Profit Accounting</p> |

Public Accounting

Public accountants offer services in much the same way as doctors and lawyers. The public accountant can achieve professional recognition as a **Certified Public Accountant (CPA)**. This is done by meeting certain educational and experience requirements as determined by each state and passing a uniform examination prepared by the American Institute of Certified Public Accountants.

Many CPAs work alone, while others work for local, regional, national, or international accounting firms that vary in scope and size. The largest public accounting firms in the United States are known as the “Big Four.” They are Deloitte, Ernst & Young, KPMG, and PricewaterhouseCoopers.

Services offered by public accountants are listed below.

- **Auditing.** Auditing involves the application of standard review and testing procedures to be certain that proper accounting policies and practices have been followed. The purpose of the audit is to provide an independent opinion that the financial information about a business is fairly presented in a manner consistent with generally accepted accounting principles.
- **Taxation.** Tax specialists advise on tax planning, prepare tax returns, and represent clients before governmental agencies such as the Internal Revenue Service.
- **Management Advisory Services.** Given the financial training and business experience of public accountants, many businesses seek their advice on a wide variety of managerial issues. Often, accounting firms are involved in designing computerized accounting systems.
- **Forensic Accounting.** Forensic accounting is a rapidly growing segment of accounting practice. It includes fraud detection, fraud prevention, litigation support, business valuations, expert witness services, and other investigative activities. Public accounting firms offer forensic accounting services, but forensic accountants also work for insurance companies, banks, law enforcement agencies, and other organizations. By meeting certain requirements, and passing the Certified Fraud Examiner exam, a forensic accountant may earn a **Certified Fraud Examiner (CFE)** designation.

In 2002, the **Sarbanes-Oxley Act (SOX)** was passed by Congress to help improve reporting practices of public companies. The act was in response to accounting scandals at firms like Enron, WorldCom, Cendant, Xerox, and others. Key provisions of SOX are listed below.

- The Public Company Accounting Oversight Board (PCAOB) was created to enforce SOX rules and regulations. The PCAOB also has authority to set auditing standards for public company audits and to perform inspections of auditing firms.
- For the largest companies, external auditors are required to report on the effectiveness of a public company’s accounting procedures.
- Auditing firms are prohibited from offering many nonaudit services to their public audit clients.
- Auditing firms must rotate lead audit partners off audit engagements every five years.
- The CEO and CFO must personally certify that the financial statements are accurate.

It is difficult to guarantee that information provided in financial statements is always complete and accurate. These measures are a step in the right direction. If our economy and financial markets are to function properly, information provided in financial statements must be reliable.

Private (Managerial) Accounting

Many accountants are employees of private business firms. The **controller** oversees the entire accounting process and is the principal accounting officer of the company. Private or managerial accountants perform a wide variety of services for the business. These services are listed below.

- **Accounting Information Systems.** Accountants in this area design and implement manual and computerized accounting systems.
- **Financial Accounting.** Based on the accounting data prepared by the bookkeepers and accounting clerks, accountants prepare various reports and financial statements and help in analyzing operating, investing, and financing decisions.
- **Cost Accounting.** The cost of producing specific products or providing services must be measured. Further analysis is also done to determine whether the products are produced and services are provided in the most cost-effective manner.
- **Budgeting.** In the budgeting process, accountants help managers develop a financial plan.
- **Tax Accounting.** Instead of hiring a public accountant, a company may have its own accountants. They focus on tax planning, preparation of tax returns, and dealing with the Internal Revenue Service and other governmental agencies.
- **Internal Auditing.** Internal auditors review the operating and accounting control procedures adopted by management to make sure the controls are adequate and are being followed. They also monitor the accuracy and timeliness of the reports provided to management and to external parties.

A managerial accountant can achieve professional status as a **Certified Management Accountant (CMA)**. This is done by passing a uniform examination offered by the Institute of Management Accountants. An internal auditor can achieve professional recognition as a **Certified Internal Auditor (CIA)** by passing the uniform examination offered by the Institute of Internal Auditors.

Governmental and Not-for-Profit Accounting

Thousands of governmental and not-for-profit organizations (states, cities, schools, churches, and hospitals) gather and report financial information. These organizations employ a large number of accountants. Since these entities are not profit oriented, the rules are somewhat different for governmental and not-for-profit organizations. However, many accounting procedures are similar to those found in profit-seeking enterprises.

Job Opportunities

Job growth in some areas will be much greater than in others. Employment advertisements often indicate that accountants and accounting clerks are expected to have computer skills. Computer skills definitely increase the opportunities available to you in your career. Almost every business needs accountants, accounting clerks, and bookkeepers. Figure 1-6 shows the expected growth for different industry sectors. Notice that growth will be greatest in health care services. Chapters 2 through 9 introduce accounting skills that you will need to work in a service business, like health care. Chapter 10 begins the discussion of merchandising businesses. Accounting for manufacturing businesses is addressed in the last chapters of the book.

Figure 1-7 shows an overall increase in projected demand for accounting skills. Demand for billing and posting clerks, accountants and auditors, and budget analysts is expected to increase by 14.1%, 10.0%, and 6.5% respectively from 2016 to 2026. Demand for bookkeepers, accounting, and auditing clerks is projected to dip by 1.5%.

Figure 1-8 provides various job descriptions in the accounting profession along with the range of salaries paid.

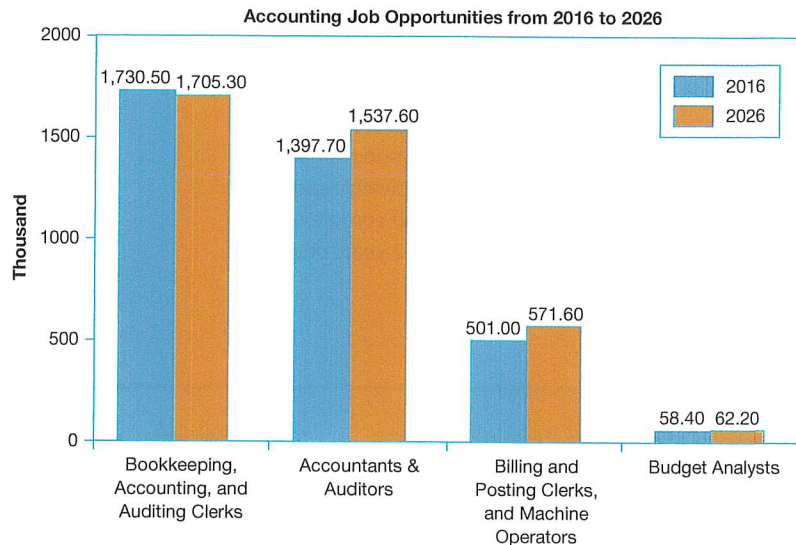
FIGURE 1-6 Expected Job Growth by Industry 2016–2026 (in thousands)



The growth in the number of new jobs from 2016 to 2026 will vary according to industry. As shown above, health care industries are expected to account for a large portion of the new jobs projected through 2026. Other industries are shown for comparison purposes. Note that professional and business services also appear to provide good opportunities. Total employment for all industry sectors is projected to grow by 7.4% over the decade, resulting in 11.5 million new jobs.

Source: Bureau of Labor Statistics News Release, January 30, 2018: Employment Projections—2016–2026. (<https://www.bls.gov/news.release/pdf/ecopro.pdf>)

FIGURE 1-7 Expected Demand



The highest number of jobs available is expected to be for bookkeepers, accounting and auditing clerks, though a 1.5 percent dip in these jobs over the decade is projected. As shown below, jobs for accountants and auditors are expected to increase by 10 percent. The projected growth, or decline, for each area from 2016 to 2026 is shown below.

| | Thousands | Percentage |
|---|-----------|------------|
| Accountants and auditors | 139.9 | 10.0% |
| Budget analysts | 3.8 | 6.5% |
| Bookkeeping, accounting, and auditing clerks | -25.2 | -1.5% |
| Billing and posting clerks, and machine operators | 70.6 | 14.1% |

Source: Bureau of Labor Statistics, National Employment Matrix as of January 30, 2018. (https://www.bls.gov/emp/ep_table_102.htm)

FIGURE 1-8 Accounting Positions according to Salary.com, 2018

Accounting Clerk I

Performs routine accounting activities such as maintenance of the general ledger, preparation of various accounting statements and financial reports. Posts journal entries and verifies billings, invoices and checks. Assists in completing moderately complex calculations. Reconciles accounts and bank statements. Has a basic understanding of bookkeeping and accounting principles. Is proficient with spreadsheets and other software tools. Typically requires a high school diploma. Typically reports to a supervisor or manager. Possesses a moderate understanding of general aspects of the job. Works under the close direction of senior personnel in the functional area. May require 0-1 year of general work experience.

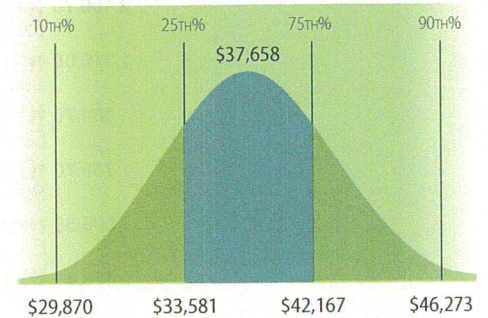
Bookkeeper

Maintains and records a complete and systematic set of business transactions. Balances ledgers, reconciles accounts, and prepares reports to show receipts, expenditures, accounts receivable, and payable. Follows bookkeeping procedures established by the organization. May require an associate's degree or its equivalent. Typically reports to a supervisor or a manager. Gaining or has attained full proficiency in a specific area of discipline. Works under moderate supervision. Typically requires 1-3 years of related experience.

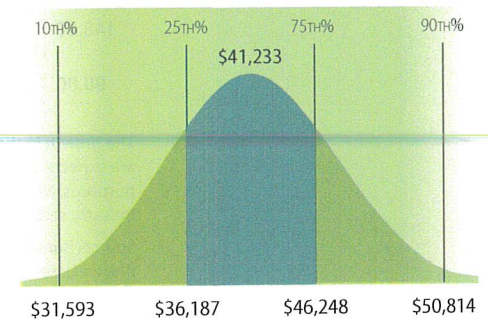
Budget Analyst I

Analyzes an organization's accounting records to determine financial resources required. Plans, analyzes, and prepares the organization's budget activities according to previous budget figures and estimated revenue. Makes recommendations for budget allocations to ensure conformance to budgetary limits. Keeps track of expenses, inventories, and budget balances. Prepares financial reports. Requires a bachelor's degree. Typically reports to a supervisor or manager. Works on projects/matters of limited complexity in a support role. Work is closely managed. Typically requires 0-2 years of related experience.

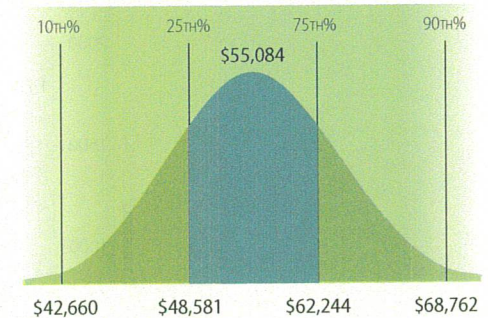
Accounting Clerk I – U.S. National Averages



Bookkeeper – U.S. National Averages



Budget Analyst I – U.S. National Averages



YOUR PERSPECTIVE

Industrial Engineering Technician

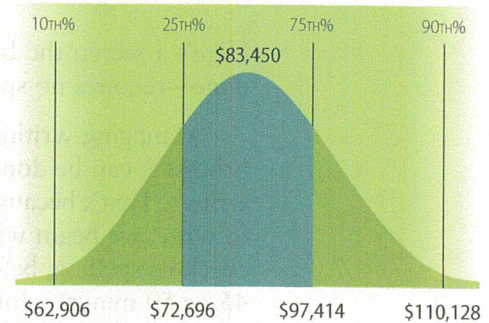
Accounting is the language of business and the eyes and ears of management. No matter the job, it likely provides accounting information that management uses to make important operating decisions. Even a technology-oriented

job, such as *industrial engineering technician*, involves accounting. These technicians assist engineers in devising systems that make products or provide services. They also perform duties that provide accounting information such as analyzing production costs and managing supply chain costs to control inventory.

Accounts Payable Manager

Manages all activities in the accounts payable function. Ensures timely payments of vendor invoices and expense vouchers and maintains accurate records and control reports. Reviews applicable accounting reports and accounts payable register to ensure accuracy. Typically requires a bachelor's degree. Typically reports to a head of a unit/department. Manages subordinate staff in the day-to-day performance of their jobs. True first level manager. Ensures that project/department milestones/goals are met and adhering to approved budgets. Has full authority for personnel actions. Extensive knowledge of department processes. Typically requires 5 years experience in the related area as an individual contributor. 1 to 3 years supervisory experience may be required.

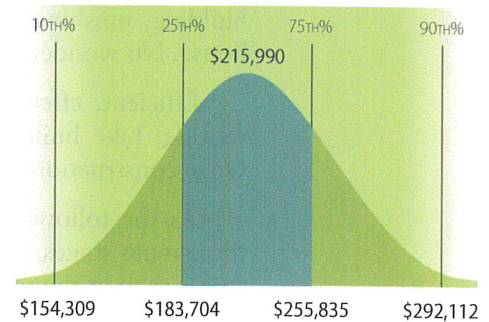
Accounts Payable manager – U.S. National Averages



Top Audit Executive

Oversees all aspects of an organization's auditing function. Plans and directs all accounting and financial data. Designs internal auditing procedures and ensures they are followed. Monitors procedures for effectiveness and provides recommendations for improvement. Requires a bachelor's degree. Typically reports to top management. Manages a business unit, division, or corporate function with major organizational impact. Establishes overall direction and strategic initiatives for the given major function or line of business. Has acquired the business acumen and leadership experience to become a top function or division head.

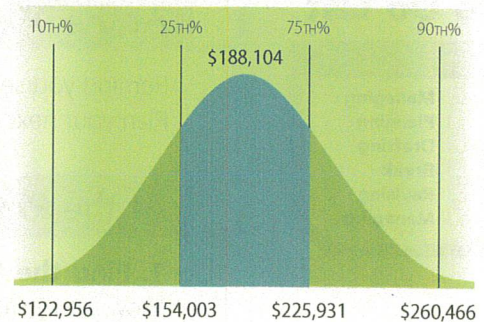
Top Audit Executive – U.S. National Averages



Controller

Leads and directs an organization's accounting functions. Establishes and maintains the organization's overall accounting systems, procedures, and policies. Directs all analysis and reporting of financial information including budgets, planning, and required filings and reports. Presents findings and recommendations to management. Requires a bachelor's degree of accounting or finance. Typically reports to Chief Financial Officer (CFO). Typically requires CPA. Manages a departmental function within a broader corporate function. Develops major goals to support broad functional objectives. Approves policies developed within various sub-functions and departments. Comprehensive knowledge of the overall departmental function. Typically requires 8+ years of managerial experience.

Controller – U.S. National Averages



Source: Salary.com, March 2018.

Managing Your Writing

Regardless of the type of career you desire, writing skills are important in business and your personal life. Becoming a good writer requires practice and a strategy for the process used to prepare memos, letters, and other documents. On pages 14 and 15, Ken Davis, *Professor Emeritus of English at Indiana University*, offers an excellent approach to managing your writing. Take a moment to read Ken's tips. Then, practice his approach by completing the writing assignments as you finish each chapter.

From: Ken Davis
 Subject: Managing Your Writing
 To: Accounting Students

Here's a secret: the business writing that you and I do—the writing that gets the world's work done—requires no special gift. It can be managed, like any other business process.

Managing writing is largely a matter of managing time. Writing is a process, and like any process it can be done efficiently or inefficiently. Unfortunately, most of us are pretty inefficient writers. That's because we try to get each word, each sentence, right the first time. Given a letter to write, we begin with the first sentence. We think about that sentence, write it, revise it, even check its spelling, before going on to the second sentence. In an hour of writing, we might spend 45 or 50 minutes doing this kind of detailed drafting. We spend only a few minutes on overall planning at the beginning and only a few minutes on overall revising at the end.

That approach to writing is like building a house by starting with the front door: planning, building, finishing—even washing the windows—before doing anything with the rest of the house. No wonder most of us have so much trouble writing.

Efficient, effective writers take better charge of their writing time. They *manage* their writing. Like building contractors, they spend time planning before they start construction. Once construction has started, they don't try to do all of the finishing touches as they go.

As the following illustration shows, many good writers break their writing process into three main stages: planning, drafting, and revising. They spend more time at the first and third stages than at the second. They also build in some “management” time at the beginning and the end, and some break time in the middle. To manage *your* writing time, try the following steps.

To Do List

CHECK LIST

- Managing
- Planning
- Drafting
- Break
- Revising
- Managing

At the **Managing Stage** *(perhaps two or three minutes for a one-hour writing job):*

Remind yourself that writing *can* be managed and that it's largely a matter of managing time. Plan your next hour.

At the **Planning Stage** *(perhaps 20 minutes out of the hour):*

- 1. Find the “we.”** Define the community to which you and your reader belong. Then ask, “How are my reader and I alike and different?”—in knowledge, attitudes, and circumstances.
- 2. Define your purpose.** Remember the advice a consultant once gave Stanley Tool executives: “You're not in the business of making drills: you're in the business of making holes.” Too many of us lose sight of the difference between making drills and making holes when we write letters and memos. We focus on the piece of writing—the tool itself—not its purpose. The result: our writing often misses the chance to be as effective as it could be. When you're still at the planning stage, focus on the outcome you want, not on the means you will use to achieve it.
- 3. Get your stuff together.** Learn from those times when you've turned a one-hour home-improvement project into a three- or four-hour job by having to make repeated trips to the hardware store for tools or parts. Before you start the drafting stage of writing, collect the information you need.
- 4. Get your ducks in a row.** Decide on the main points you want to make. Then, make a list or rough outline placing your points in the most logical order.

At the **Drafting Stage** (perhaps 5 minutes out of the hour):

5. Do it wrong the first time. Do a “quick and dirty” draft, without editing. Think of your draft as a “prototype,” written not for the end user but for your own testing and improvement. Stopping to edit while you draft breaks your train of thought and keeps you from being a good writer. (*Hint:* If you are writing at a computer, try turning off the monitor during the drafting stage.)

At the **Break Stage** (perhaps 5 minutes):

6. Take a break and change hats. Get away from your draft, even if for only a few minutes. Come back with a fresh perspective—the reader’s perspective.

At the **Revising Stage** (perhaps 25 minutes):

7. Signal your turns. Just as if you were driving a car, you’re leading your reader through new territory. Use “turn signals”—*and, in addition, but, however, or, therefore, because, for example*—to guide your reader from sentence to sentence.

8. Say what you mean. Put the point of your sentences in the subjects and verbs. For example, revise “There are drawbacks to using this accounting method” to “This accounting method has some drawbacks.” You’ll be saying what you mean, and you’ll be a more effective communicator.

9. Pay by the word. Reading your memo requires work. If your sentences are wordy and you are slow to get to the point, the reader may decide that it is not worth the effort. Pretend you are paying the reader by the word to read your memo. Then, revise your memo to make it as short and to the point as possible.

10. Translate into English. Keep your words simple. (Lee Iacocca put both these tips in one “commandment of good management”: “Say it in English and keep it short.”) Remember that you write to express, not impress.

11. Finish the job. Check your spelling, punctuation, and mechanics.

Finally, at the **Managing Stage** (2 to 3 minutes):

12. Evaluate your writing process. Figure out how to improve it next time.

By following these 12 steps, you can take charge of your writing time. Begin today to *manage your writing*. As a United Technologies Corporation advertisement in *The Wall Street Journal* admonished, “If you want to manage somebody, manage yourself. Do that well and you’ll be ready to stop managing and start leading.”

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SELF-STUDY

LEARNING OBJECTIVES

Key Points to Remember

| | |
|---|--|
| LO1 Describe the purpose of accounting. | The purpose of accounting is to provide financial information about a business to individuals and organizations. |
| LO2 Describe the accounting process. | The six major steps of the accounting process are analyzing, recording, classifying, summarizing, reporting, and interpreting. |
| LO3 Define GAAP and describe the process used by FASB to develop these principles. | Generally accepted accounting principles (GAAP) are the rules that businesses must follow when preparing financial statements. FASB takes the following steps to develop an accounting standard: <ol style="list-style-type: none">1. The issue is placed on the Board's agenda.2. After researching the issue, a Preliminary Views document is issued.3. Public hearings are held.4. An Exposure Draft is issued.5. The Board issues an Accounting Standards Update which amends the FASB Accounting Standards Codification. |
| LO4 Define three types of business ownership structures. | Three types of business ownership structures are the sole proprietorship, the partnership, and the corporation. |
| LO5 Classify different types of businesses by activities. | Different types of businesses classified by activities are a service business, a merchandising business, and a manufacturing business. |
| LO6 Identify career opportunities in accounting. | Career opportunities in accounting include work in public accounting, private accounting, and governmental and not-for-profit accounting. |

KEY TERMS

- accountant** (8) Designs the accounting information system and focuses on analyzing and interpreting information.
- accounting** (4) A system of gathering financial information about a business and reporting this information to users.
- accounting clerk** (8) Records, sorts, and files accounting information.
- accounting information systems** (10) Accountants in this area design and implement manual and computerized accounting systems.
- Accounting Standards Update** (6) A standard issued by the Financial Accounting Standards Board. These standards must be followed when preparing financial statements. The updates are included in the FASB Accounting Standards Codification.
- analyzing** (5) Looking at events that have taken place and thinking about how they affect the business.
- auditing** (9) Reviewing and testing to be certain that proper accounting policies and practices have been followed.

- bookkeeper** (8) Generally supervises the work of accounting clerks, helps with daily accounting work, and summarizes accounting information.
- budgeting** (10) The process in which accountants help managers develop a financial plan.
- Certified Fraud Examiner (CFE)** (9) A forensic accountant who has passed the exam offered by the Association of Certified Fraud Examiners.
- Certified Internal Auditor (CIA)** (10) An internal auditor who has achieved professional recognition by passing the uniform examination offered by the Institute of Internal Auditors.
- Certified Management Accountant (CMA)** (10) An accountant who has passed an examination offered by the Institute of Management Accountants.
- Certified Public Accountant (CPA)** (9) A public accountant who has met certain educational and experience requirements and has passed an examination prepared by the American Institute of Certified Public Accountants.
- classifying** (5) Sorting and grouping similar items together rather than merely keeping a simple, diary-like record of numerous events.
- Controller** (10) The accountant who oversees the entire accounting process and is the principal accounting officer of a company.
- corporation** (7) A type of ownership structure in which stockholders own the business. The owners' risk is usually limited to their initial investment, and they usually have very little influence on the business decisions.
- cost accounting** (10) Determining the cost of producing specific products or providing services and analyzing for cost effectiveness.
- Exposure Draft** (6) This document explains the rules that FASB believes firms should follow in accounting for a particular event. Based on the responses to the Exposure Draft, the Board will decide if any changes are necessary before issuing a final standard.
- financial accounting** (10) Includes preparing various reports and financial statements and analyzing operating, investing, and financing decisions.
- Financial Accounting Standards Board Accounting Standards Codification** (6) This Codification is an electronic database that provides one authoritative source for the standards which must be followed by U.S. companies.
- forensic accounting** (9) A specialized field that combines fraud detection, fraud prevention, litigation support, expert witnessing, business valuations, and other investigative activities.
- generally accepted accounting principles (GAAP)** (5) Procedures and guidelines developed by the Financial Accounting Standards Board to be followed in the accounting and reporting process.
- internal auditing** (10) Reviewing the operating and accounting control procedures adopted by management to make sure the controls are adequate and being followed; assuring that accurate and timely information is provided.
- interpreting** (5) Deciding the meaning and importance of the information in various reports.
- management advisory services** (9) Providing advice to businesses on a wide variety of managerial issues.
- manufacturing business** (7) A business that makes a product to sell.
- merchandising business** (7) A business that buys products to sell.
- para-accountant** (8) A paraprofessional who provides many accounting, auditing, or tax services under the direct supervision of an accountant.

- partnership** (7) A type of ownership structure in which more than one person owns the business.
- Preliminary Views** (5) The first document issued by FASB when developing an accounting standard. This document identifies the pros and cons of various accounting treatments for an event and invites others to comment.
- public hearing** (5) Following the issuance of a discussion memorandum, public meetings are often held by FASB to gather opinions on the accounting issue.
- recording** (5) Entering financial information about events affecting the company into the accounting system.
- reporting** (5) Telling the results of the financial information.
- Sarbanes-Oxley Act (SOX)** (9) An act passed by Congress to help improve reporting practices of public companies.
- service business** (7) A business that provides a service.
- sole proprietorship** (6) A type of ownership structure in which one person owns the business.
- summarizing** (5) Bringing the various items of information together to determine a result.
- tax accounting** (10) Services focused on tax planning, preparing tax returns, and dealing with the Internal Revenue Service and other governmental agencies.
- taxation** (9) See tax accounting.

APPLYING YOUR KNOWLEDGE

CengageNowv2 provides "Show Me How" videos for selected exercises and problems. Additional resources, such as Excel templates for completing selected exercises and problems, are available for download from the companion website at Cengage.com.

REVIEW QUESTIONS

- LO1** 1. What is the purpose of accounting?
- LO1** 2. Identify four user groups normally interested in financial information about a business.
- LO2** 3. Identify the six major steps of the accounting process and explain each step.
- LO3** 4. What are generally accepted accounting principles (GAAP)?
- LO3** 5. Describe the steps followed by the Financial Accounting Standards Board when developing an accounting standard.
- LO3** 6. What is the name of the organization that issues accounting standards followed by many firms in countries outside the United States?
- LO4** 7. Identify the three types of ownership structures and discuss the advantages and disadvantages of each.
- LO5** 8. Identify three types of businesses according to activities.
- LO6** 9. What are the main functions of an accounting clerk?
- LO6** 10. Name and describe four areas of specialization for a public accountant.
- LO6** 11. What is the purpose of the Sarbanes-Oxley Act?
- LO6** 12. Name and describe six areas of specialization for a managerial accountant.

SERIES A EXERCISES

E 1-1A (LO1)

PURPOSE OF ACCOUNTING Match the following users with the information needed.

- | | |
|------------------------|--|
| 1. Owners | a. Whether the firm can pay its bills on time |
| 2. Managers | b. Detailed, up-to-date information to measure business performance (and plan for future operations) |
| 3. Creditors | c. To determine taxes to be paid and whether other regulations are met |
| 4. Government agencies | d. The firm's current financial condition |

E 1-2A (LO2)

ACCOUNTING PROCESS List the six major steps of the accounting process in order (1–6) and define each.

- | | |
|-------|--------------|
| _____ | Recording |
| _____ | Summarizing |
| _____ | Reporting |
| _____ | Analyzing |
| _____ | Interpreting |
| _____ | Classifying |

SERIES B EXERCISES

E 1-1B (LO1)

PURPOSE OF ACCOUNTING Describe the kind of information needed by the users listed.

Owners (present and future)

Managers

Creditors (present and future)

Government agencies

E 1-2B (LO2)

ACCOUNTING PROCESS Match the following steps of the accounting process with their definitions.

- | | |
|--------------|--|
| Analyzing | a. Telling the results |
| Recording | b. Looking at events that have taken place and thinking about how they affect the business |
| Classifying | c. Deciding the importance of the various reports |
| Summarizing | d. Aggregating many similar events to provide information that is easy to understand |
| Reporting | e. Sorting and grouping like items together |
| Interpreting | f. Entering financial information into the accounting system |

CHECK LIST

- Managing
- Planning
- Drafting
- Break
- Revising
- Managing

MANAGING YOUR WRITING

Take a moment to think about what it would be like to run your own business. If you started a business, what would it be? Prepare a one-page memo that describes the type of business you would enjoy the most. Would it be a service, merchandising, or manufacturing business? Explain what form of ownership you would prefer and why.