# Brief Contents

<table>
<thead>
<tr>
<th>Chapter</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chapter 1</td>
<td>An Introduction to Accounting</td>
<td>2</td>
</tr>
<tr>
<td>Chapter 2</td>
<td>Understanding the Accounting Cycle</td>
<td>44</td>
</tr>
<tr>
<td>Chapter 3</td>
<td>Accounting for Merchandising Businesses</td>
<td>86</td>
</tr>
<tr>
<td>Chapter 4</td>
<td>Internal Controls, Accounting for Cash, and Ethics</td>
<td>124</td>
</tr>
<tr>
<td>Chapter 5</td>
<td>Accounting for Receivables and Inventory Cost Flow</td>
<td>156</td>
</tr>
<tr>
<td>Chapter 6</td>
<td>Accounting for Long-Term Operational Assets</td>
<td>200</td>
</tr>
<tr>
<td>Chapter 7</td>
<td>Accounting for Liabilities</td>
<td>240</td>
</tr>
<tr>
<td>Chapter 8</td>
<td>Proprietorships, Partnerships, and Corporations</td>
<td>286</td>
</tr>
<tr>
<td>Chapter 9</td>
<td>Financial Statement Analysis</td>
<td>318</td>
</tr>
<tr>
<td>Chapter 10</td>
<td>An Introduction to Managerial Accounting</td>
<td>358</td>
</tr>
<tr>
<td>Chapter 11</td>
<td>Cost Behavior, Operating Leverage, and Profitability analysis</td>
<td>396</td>
</tr>
<tr>
<td>Chapter 12</td>
<td>Cost Accumulation, Tracing and Allocation</td>
<td>430</td>
</tr>
<tr>
<td>Chapter 13</td>
<td>Relevant Information for Special Decisions</td>
<td>462</td>
</tr>
<tr>
<td>Chapter 14</td>
<td>Planning for Profit and Cost Control</td>
<td>498</td>
</tr>
<tr>
<td>Chapter 15</td>
<td>Performance Evaluation</td>
<td>530</td>
</tr>
<tr>
<td>Chapter 16</td>
<td>Planning for Capital Investments</td>
<td>562</td>
</tr>
<tr>
<td>Appendix A</td>
<td>Accessing the EDGAR Database Through the Internet</td>
<td>595</td>
</tr>
<tr>
<td>Appendix B</td>
<td>Annual Report for Portion of the Form 10-K for Target Corporation</td>
<td>596</td>
</tr>
<tr>
<td>Appendix C</td>
<td>The Double-Entry Accounting System</td>
<td>661</td>
</tr>
<tr>
<td>Glossary</td>
<td></td>
<td>669</td>
</tr>
<tr>
<td>Photo Credits</td>
<td></td>
<td>678</td>
</tr>
<tr>
<td>Index</td>
<td></td>
<td>679</td>
</tr>
</tbody>
</table>
Contents

Chapter 1 An Introduction to Accounting 2

Chapter Opening 2
Role of Accounting in Society 4
Using Free Markets to Set Resource Priorities 4
Accounting Provides Information 4
Types of Accounting Information 6
Non-business Resource Usage 6
Careers in Accounting 7
Measurement Rules 8
Reporting Entities 9

Elements of Financial Statements 10
Using Accounts to Gather Information 11
Accounting Equation 12

Recording Business Events under the Accounting Equation 13
Asset Source Transactions 13
Asset Exchange Transactions 14
Another Asset Source Transaction 15
Asset Use Transactions 15
Summary of Transactions 17
Recap: Types of Transactions 17

Preparing Financial Statements 18
Income Statement and the Matching Concept 18
Statement of Changes in Stockholders' Equity 20
Balance Sheet 20
Statement of Cash Flows 21
The Closing Process 22
The Horizontal Financial Statements Model 23

Real-World Financial Reports 24
Annual Report for Target Corporation 25
Special Terms in Real-World Reports 25

A Look Back 26
A Look Forward 26

Key Terms 28
Questions 28
Multiple-choice Questions 29
Exercises 29
Problems 37

Analyze, Think, Communicate 41

Chapter 2 Understanding the Accounting Cycle 44

Chapter Opening 44
Accrual Accounting 46
Accounting for Accounts Receivable 46
Other Events 47
Accounting for Accrued Salary Expense (Adjusting Entry) 47
Summary of Events and General Ledger 49
Vertical Statements Model 49

The Closing Process 52
Steps in an Accounting Cycle 52
The Matching Concept 53
The Conservatism Principle 53

Second Accounting Cycle 53
Prepaid Items (Cost versus Expense) 54
Accounting for Receipt of Unearned Revenue 55
Chapter 3  Accounting for Merchandising Businesses  86

Chapter Opening  86
Product Costs Versus Selling and Administrative Costs  88
Allocating Inventory Cost between Asset and Expense Accounts  89
Perpetual Inventory System  89
  Effects of 2012 Events on Financial Statements  90
  Financial Statements for 2012  91
  Transportation Cost, Purchase Returns and Allowances, and Cash Discounts Related to Inventory Purchases  92
  Effects of 2013 Events on Financial Statements  92
  Accounting for Purchase Returns and Allowances  93
  Purchase Discounts  94
  The Cost of Financing Inventory  94
  Accounting for Transportation Costs  95
  Recognizing Gains and Losses  98

Multistep Income Statement  98
Lost, Damaged, or Stolen Inventory  100
  Adjustment for Lost, Damaged, or Stolen Inventory  101
Events Affecting Sales  101
  Accounting for Sales Returns and Allowances  102
  Accounting for Sales Discounts  102
Common Size Financial Statements  103
A Look Back  105
A Look Forward  106
Appendix  106
Self-Study Review Problem  107
Key Terms  109
Questions  109
Multiple-choice Questions  110
Exercises  110
Problems  117
Analyze, Think, Communicate  121
Chapter 4  Internal Controls, Accounting for Cash, and Ethics  124

Chapter Opening  124

Key Features of Internal Control Systems  126
- Separation of Duties  126
- Quality of Employees  127
- Bonded Employees  127
- Required Absences  127
- Procedures Manual  127
- Authority and Responsibility  127
- Prenumbered Documents  128
- Physical Control  128
- Performance Evaluations  128
- Limitations  128

Accounting for Cash  129
- Controlling Cash  129
- Checking Account Documents  130
- Reconciling the Bank Account  131
- Determining True Cash Balance  131
- Illustrating a Bank Reconciliation  134

Importance of Ethics  137
- Common Features of Criminal and Ethical Misconduct  137

Role of the Independent Auditor  139
- The Financial Statement Audit  140
- Materiality and Financial Audits  140
- Types of Audit Opinions  141
- Confidentiality  141

A Look Back  142
A Look Forward  143
Self-Study Review Problem  143

Key Terms  144
Questions  144
Multiple-choice Questions  145
Exercises  145
Problems  149
Analyze, Think, Communicate  153

Chapter 5  Accounting for Receivables and Inventory Cost Flow  156

Chapter Opening  156

Allowance Method of Accounting for Uncollectible Accounts  158
- Accounting Events Affecting the 2012 Period  158
- Accounting Events Affecting the 2013 Period  161

Estimating Uncollectible Accounts Expense Using the Percent of Revenue (Sales) Method  163
- Analysis of Financial Statements  163

Estimating Uncollectible Accounts Expense Using the Percent of Receivables Method  164
- Matching Revenues and Expenses versus Asset Measurement  166

Accounting for Notes Receivable (Promissory Notes)  166
- How Accounting for Notes Receivable Affects Financial Statements  167

Accounting for Credit Card Sales  170

Inventory Cost Flow Methods  171
- Specific Identification  172
- First-In, First-Out (FIFO)  172
- Last-In, First-Out (LIFO)  172
- Weighted Average  172
- Physical Flow  172
Effect of Cost Flow on Financial Statements 172
  Effect on Income Statement 172
  Effect on Balance Sheet 173
Inventory Cost Flow under a Perpetual System 174
  Multiple Layers with Multiple Quantities 174
  Allocating Cost of Goods Available for Sale 174
  Effect of Cost Flow on Financial Statements 174
A Look Back 179
A Look Forward 179
Self-Study Review Problem 1 180
Self-Study Review Problem 2 180
Key Terms 182
Questions 182
Multiple-choice Questions 183
Exercises 183
Problems 191
Analyze, Think, Communicate 197

Chapter 6 Accounting for Long-Term Operational Assets 200

Chapter Opening 200
Tangible versus Intangible Assets 202
  Tangible Long-Term Assets 202
  Intangible Assets 202
Determining the Cost of Long-Term Assets 203
  Basket Purchase Allocation 203
Methods of Recognizing Depreciation Expense 204
  Dryden Enterprises Illustration 205
  Straight-Line Depreciation 205
  Financial Statements 207
  Double-Declining-Balance Depreciation 208
  Units-of-Production Depreciation 211
  Comparing the Depreciation Methods 212
Revision of Estimates 213
  Revision of Life 213
  Revision of Salvage 213
Continuing Expenditures for Plant Assets 214
  Costs That Are Expensed 214
  Costs That Are Capitalized 214
Natural Resources 216
Intangible Assets 216
  Trademarks 216
  Patents 217
  Copyrights 217
  Franchises 217
  Goodwill 218
Expense Recognition for Intangible Assets 219
  Expensing Intangible Assets with Identifiable Useful Lives 219
  Impairment Losses for Intangible Assets with Indefinite Useful Lives 219
Balance Sheet Presentation 220
Effect of Judgment and Estimation 220
Effect of Industry Characteristics 221
A Look Back 222
A Look Forward 223
Self-Study Review Problem 223
Key Terms 224
Questions 224
Multiple-choice Questions 225
Exercises 225
Problems 231
Analyze, Think, Communicate 237
Chapter 7  Accounting for Liabilities    240

Chapter Opening    240

Accounting for Current Liabilities    242
  Accounting for Notes Payable    242
  Accounting for Sales Tax    243
  Contingent Liabilities    244
  Warranty Obligations    245
  Financial Statements    246

Accounting for Long-Term Debt    247
  Installment Notes Payable    248
  Line of Credit    251
  Bond Liabilities    251
  Bonds Issued at Face Value    252

Amortization Using the Straight-Line Method    256
  Bonds Issued at a Discount    256
  Bonds Issued at a Premium    260

Security for Loan Agreements    261
  Current versus Noncurrent    261

A Look Back    263

A Look Forward    264

Self-Study Review Problem    268

Key Terms    269

Questions    269

Multiple-choice Questions    270

Exercises    270

Problems    277

Analyze, Think, Communicate    283

Chapter 8  Proprietorships, Partnerships, and Corporations    286

Chapter Opening    286

Forms of Business Organizations    288

Advantages and Disadvantages of Different Forms of Business Organization    288
  Regulation    288
  Double Taxation    289
  Limited Liability    289
  Continuity    290
  Transferability of Ownership    290
  Management Structure    290
  Ability to Raise Capital    291

Appearance of Capital Structure in Financial Statements    291
  Presentation of Equity in Proprietorships    291
  Presentation of Equity in Partnerships    292
  Presentation of Equity in Corporations    293

Characteristics of Capital Stock    293
  Par Value    293
  Stated Value    293
  Other Valuation Terminology    293
  Stock: Authorized, Issued, and Outstanding    293
  Classes of Stock    294

Accounting for Stock Transactions on the Day of Issue    296
  Issuing Par Value Stock    296
  Stock Classification    296
  Stock Issued at Stated Value    296
  Stock Issued with No Par Value    297
  Financial Statement Presentation    297

Stockholders’ Equity Transactions after the Day of Issue    298
  Treasury Stock    298
  Cash Dividend    299
Chapter 9  Financial Statement Analysis  318

Chapter Opening  318
Factors in Communicating Useful Information  320
   The Users  320
   The Types of Decisions  320
   Information Analysis  320
Methods of Analysis  320
   Horizontal Analysis  321
   Vertical Analysis  324
   Ratio Analysis  324
Measures of Debt-Paying Ability  325
   Liquidity Ratios  325
   Solvency Ratios  329
Measures of Profitability  331
   Measures of Managerial Effectiveness  331
   Stock Market Ratios  333

Presentation of Analytical Relationships  336
Limitations of Financial Statement Analysis  337
   Different Industries  338
   Changing Economic Environment  338
   Accounting Principles  339
A Look Back  339
A Look Forward  339
Self-Study Review Problem  340
Key Terms  342
Questions  342
Multiple-choice Questions  342
Exercises  342
Problems  348
Analyze, Think, Communicate  354

Chapter 10  An Introduction to Managerial Accounting  358

Chapter Opening  358
Differences between Managerial and Financial Accounting  360
   Users and Types of Information  360
   Level of Aggregation  360
   Regulation  361
   Information Characteristics  362

Time Horizon and Reporting Frequency  362
Product Costing in Manufacturing Companies  362
   Tabor Manufacturing Company  362
   Average Cost per Unit  362
   Costs Can Be Assets or Expenses  363
Chapter 12  Cost Accumulation, Tracing, and Allocation    430

Chapter Opening    430
Determine the Cost of Cost Objects    432
    Estimated versus Actual Cost    432
Assignment of Costs to Objects in a Retail Business    432
Identifying Direct and Indirect Costs    433
    Cost Classifications—Independent and Context Sensitive    434
Allocating Indirect Costs to Objects    434
Selecting a Cost Driver    436
    Behavioral Implications    439
Effects of Cost Behavior on Selecting the Most Appropriate Cost Driver    440
    Using Volume Measures to Allocate Variable Overhead Costs    440
    Allocating Fixed Overhead Costs    443
Allocating Costs to Solve Timing Problems    444
Aggregating and Disaggregating Individual Costs into Cost Pools    445
Cost Allocation: The Human Factor    445
    Using Cost Allocations in a Budgeting Decision    445
    Using Cost Drivers to Make Allocations    446
    Choosing the Best Cost Driver    447
    Controlling Emotions    447
A Look Back    448
A Look Forward    448
Self-Study Review Problem    448
Key Terms    450
Questions    450
Multiple-choice Questions    451
Exercises    451
Problems    455
Analyze, Think, Communicate    458

Chapter 13  Relevant Information for Special Decisions    462

Chapter Opening    462
Relevant Information    464
    Sunk Cost    464
    Opportunity Costs    464
    Relevance Is an Independent Concept    465
    Relevance Is Context-Sensitive    466
    Relationship Between Relevance and Accuracy    466
    Quantitative versus Qualitative Characteristics of Decision Making    466
    Differential Revenue and Avoidable Cost    467
Relationship of Cost Avoidance to a Cost Hierarchy    467
Relevant Information and Special Decisions    468
Special Order Decisions    468
Outsourcing Decisions    471
Segment Elimination Decisions    473
Summary of Relationships Between Avoidable Costs and the Hierarchy of Business Activity    476
Equipment Replacement Decisions    477
A Look Back    478
A Look Forward    479
Self-Study Review Problem    479
Key Terms    482
Questions    482
Multiple-choice Questions    483
Exercises    483
Problems    489
Analyze, Think, Communicate    493
Chapter 14  Planning for Profit and Cost Control  498

Chapter Opening  498
The Planning Process  500
Three Levels of Planning for Business Activity  500
Advantages of Budgeting  501
Planning  501
Coordination  501
Performance Measurement  501
Corrective Action  501
Budgeting and Human Behavior  501
The Master Budget  502
Hampton Hams Budgeting Illustration  503
Sales Budget  503
Inventory Purchases Budget  505
Selling and Administrative Expense Budget  507
Cash Budget  508
Pro Forma Income Statement  511
Pro Forma Balance Sheet  512
Pro Forma Statement of Cash Flows  512
A Look Back  513
A Look Forward  514
Self-Study Review Problem  514
Key Terms  516
Questions  516
Multiple-choice Questions  517
Exercises  517
Problems  522
Analyze, Think, Communicate  526

Chapter 15  Performance Evaluation  530

Chapter Opening  530
Decentralization Concept  532
Responsibility Centers  532
Controllability Concept  532
Preparing Flexible Budgets  533
Determining Variances for Performance Evaluation  535
Sales and Variable Cost Volume Variances  535
Interpreting the Sales and Variable Cost Volume Variances  535
Fixed Cost Considerations  536
Flexible Budget Variances  537
Calculating the Sales Price Variance  538
The Human Element Associated with Flexible Budget Variances  539
Need for Standards  540
Managerial Performance Measurement  540
Return on Investment  540
Qualitative Considerations  541
Factors Affecting Return on Investment  542
Residual Income  543
Calculating Multiple ROIs and/or RIs for the Same Company  545
Responsibility Accounting and the Balanced Scorecard  545
A Look Back  546
A Look Forward  546
Self-Study Review Problem 1  546
Self-Study Review Problem 2  548
Key Terms  549
Questions  550
Multiple-choice Questions  550
Exercises  550
Problems  555
Analyze, Think, Communicate  558
Chapter 16  Planning for Capital Investments  562

Chapter Opening  562
Capital Investment Decisions  564
   Time Value of Money  564
   Determining the Minimum Rate of Return  564
Converting Future Cash Inflows to Their Equivalent Present Values  565
   Present Value Table for Single-Amount Cash Inflows  566
   Present Value Table for Annuities  566
   Software Programs That Calculate Present Values  567
   Ordinary Annuity Assumption  568
   Reinvestment Assumption  568
Techniques for Analyzing Capital Investment Proposals  569
   Net Present Value  569
   Internal Rate of Return  570
Techniques for Measuring Investment Cash Flows  571
   Cash Inflows  571
   Cash Outflows  572
Techniques for Comparing Alternative Capital Investment Opportunities  572
   Net Present Value  572
   Internal Rate of Return  574
   Relevance and the Time Value of Money  576
   Tax Considerations  576
Techniques That Ignore the Time Value of Money  578
   Payback Method  578
   Unadjusted Rate of Return  579
   Real-World Reporting Practices  581
Postaudits  581
A Look Back  582
Appendix  582
Self-Study Review Problem  583
Key Terms  584
Questions  584
Multiple-choice Questions  585
Exercises  585
Problems  589
Analyze, Think, Communicate  592

Appendix A  Accessing the EDGAR Database Through the Internet  595
Appendix B  Annual Report for Portion of the Form 10-K for Target Corporation  596
Appendix C  The Double-Entry Accounting System  661
Glossary  669
Photo Credits  678
Index  679