absolute amounts  Dollar totals reported in accounts on financial reports that can be misleading because they make no reference to the relative size of the company being analyzed. p. 321
accelerated depreciation methods  Depreciation methods that recognize depreciation expense more rapidly in the early stages of an asset’s life than in the later stages of its life. p. 208
account balance  Difference between total debits and total credits in an account. p. 681
accounting  Service-based profession that provides reliable and relevant financial information useful in making decisions. p. 2
accounting controls  Procedures designed to safeguard assets and to ensure accuracy and reliability of the accounting records and reports.
accounting equation  Expression of the relationship between the assets and the claims on those assets. p. 12
accounting event  Economic occurrence that causes changes in an enterprise’s assets, liabilities, or equity. p. 13
accounting period  Span of time covered by the financial statements, normally one year, but may be a quarter, a month or some other time span. p. 15
account receivable  Expected future cash receipt arising from permitting a customer to buy now and pay later; typically a relatively small balance due within a short time period. p. 46
accounts  Records used for classifying and summarizing transaction data; subclassifications of financial statement elements. p. 11
accounts receivable turnover ratio  Financial ratio that measures how fast accounts receivable are turned into cash; computed by dividing sales by accounts receivable.
accrual  Recognition of events before exchanging cash. p. 45
accrual accounting  Accounting system that recognizes expenses or revenues when they occur regardless of when cash is exchanged. p. 45
accrued expenses  Expenses that are recognized before cash is paid. An example is accrued salaries expense. p. 48
accrued interest  Interest revenue or expense that is recognized before cash has been exchanged. p. 45
accumulated conversion factors  Factors used to convert a series of future cash inflows into their present value equivalent and that are applicable to cash inflows of equal amounts spread over equal interval time periods and that can be determined by computing the sum of the individual single factors used for each period. p. 567
accumulated depreciation  Contra asset account that indicates the sum of all depreciation expense recognized for an asset since the date of acquisition. p. 206
acid-test ratio  (quick ratio) Measure of immediate debt-paying ability; calculated by dividing very liquid assets (cash, receivables, and marketable securities) by current liabilities. p. 326
activities  The actions taken by an organization to accomplish its mission. p. 377
activity base  Factor that causes changes in variable cost; is usually some measure of volume when used to define cost behavior. p. 406
activity-based management (ABM) Management of the activities of an organization to add the greatest value by developing products that satisfy the needs of that organization’s customers. p. 377
adjusting entry  Entry that updates account balances prior to preparing financial statements. p. 48
administrative controls  Procedures designed to evaluate performance and the degree of compliance with a firm’s policies and public laws.
adverse opinion  Opinion issued by a certified public accountant that means one or more departures from GAAP in a company’s financial statements are so very material the auditors believe the financial statements do not fairly represent the company’s status; contrast with unqualified opinion. p. 141
aging of accounts receivable  Classifying each account receivable by the number of days it has been outstanding. The aging schedule is used to develop an estimate of the amount of the allowance for doubtful accounts. p. 165
AICPA (American Institute of Certified Public Accountants) National association that serves the educational and professional interests of members of the public accounting profession; membership is voluntary. p. 137
allocation  Process of dividing a total cost into parts and apportioning the parts among the relevant cost objects. p. 434
allocation base  Cost driver used as the basis for the allocation process. p. 435
allocation rate  Factor used to allocate or assign costs to a cost object; determined by taking the total cost to be allocated and dividing it by the appropriate cost driver. p. 435
allowance for doubtful accounts  Contra asset account that contains an amount equal to the accounts receivable that are expected to be uncollectible. p. 158
allowance method of accounting for uncollectible accounts  Method of accounting for bad debts in which bad debts are estimated and expensed in the same period in which the corresponding sales are recognized. The receivables are reported in the financial statements at net realizable value (the amount expected to be collected in cash). p. 158
amortization  Method of systematically allocating the costs of intangible assets to expense over their useful lives; also term for converting the discount on a note or a bond to interest expense over a designated period. pp. 202, 248
annual report  Document in which an organization provides information to stockholders, usually on an annual basis. p. 25
annuity  Series of equal payments made over a specified number of periods. p. 567
appropriated retained earnings  Retained earnings restricted by the board of directors for a specific purpose (e.g., to repay debt or for future expansion); although a part of total retained earnings, not available for distribution as dividends. p. 301
articles of incorporation  Items on an application filed with a state agency for the formation of a corporation; contains such information as the corporation’s name, its purpose, its location, its expected life, provisions for its capital stock, and a list of the members of its board of directors. p. 288
articulation  Characteristic of financial statements that means they are interrelated. For example, the amount of net income reported on the income statement is added to beginning retained earnings as a component in calculating the ending retained earnings balance reported on the statement of changes in stockholders’ equity. p. 18
asset exchange transaction  A transaction that decreases one asset while increasing another asset so that total assets do not change; for example, the purchase of land with cash. pp. 14, 46
assets  Economic resources used by a business to produce revenue. p. 4
asset source transaction  Transaction that increases an asset and a claim on assets; three types of asset source transactions are acquisitions from owners (equity), borrowings from creditors (liabilities), or earnings from operations (revenues). p. 13
asset turnover ratio  The amount of net income divided by average total assets. p. 332
asset use transaction  Transaction that decreases an asset and a claim on assets; the three types are distributions (transfers to owners), liability payments (to creditors), or expenses (used to operate the business). pp. 25, 47
audits  Detailed examination of some aspect of a company’s accounting records or operating procedures in order to report the results to interested parties. p. 139
authority manual  A document that outlines the chain of command for authority and responsibility. The authority manual provides guidelines for specific positions such as personnel officer as well as general authority such as all vice presidents are authorized to spend up to a designated limit. p. 127
authorized stock  Number of shares that the corporation is approved by the state to issue. p. 293
**average cost** The total cost of making products divided by the total number of products made. p. 363  
**average number of days to collect accounts receivable** Length of the average collection period for accounts receivable; computed by dividing 365 by the accounts receivable turnover ratio. p. 328  
**average number of days to sell inventory** Financial ratio that measures the average number of days that inventory stays in stock before being sold. p. 328  
**avoidable costs** Future costs that can be avoided by taking a specific course of action. To be avoidable in a decision-making context, costs must differ among the alternatives. For example, if the cost of material used to make two different products is the same for both products, that cost could not be avoided by choosing to produce one product over the other. Therefore, the material’s cost would not be an avoidable cost. p. 467  
**balanced scorecard** Analysis tool that includes financial and nonfinancial measures. p. 454  
**balance sheet** Statement that lists the assets of a business and the corresponding claims (liabilities and equity) on those assets. p. 9  
**bank reconciliation** Schedule that identifies and explains differences between the cash balance reported by the bank and the cash balance in the firm’s accounting records. p. 131  
**bank statement** Statement issued by a bank (usually monthly) that denotes all activity in the bank account for that period. p. 131  
**bank statement credit memo** Memorandum that describes an increase in the account balance. p. 131  
**bank statement debit memo** Memorandum that describes a decrease in the account balance. p. 131  
**basket purchase** Acquisition of several assets in a single transaction with no specific cost attributed to each asset. p. 203  
**batch-level costs** The costs associated with producing a batch of products. For example, the cost of setting up machinery to produce 1,000 products is a batch-level cost. The classification of batch-level costs is context sensitive. Postage for one product would be classified as a unit-level cost. In contrast, postage for a large number of products delivered in a single shipment would be classified as a batch-level cost. p. 467  
**benchmarking** Identifying the best practices used by world-class competitors. p. 376  
**best practices** Practices used by world-class companies. p. 376  
**board of directors** Group of individuals elected by the stockholders of a corporation to oversee its operations. p. 290  
**bond certificates** Debentures used to obtain long-term financing in which a company borrows funds from a number of lenders, called bondholders; usually issued in denominations of $1,000. p. 251  
**bond discount** Difference between the selling price and the face amount of a bond sold for less than the face amount. p. 256  
**bond premium** Difference between the selling price and the face amount of a bond that is sold for more than the face amount. p. 260  
**bondholder** The party buying a bond (the lender or creditor). p. 251  
**book of original entry** A journal in which transactions are first recorded. p. 662  
**book value** Historical (original) cost of an asset minus the accumulated depreciation; alternatively, undepreciated amount to date. p. 207  
**book value per share** Value of stock determined by dividing the total stockholders’ equity by the number of shares of stock. pp. 293, 334  
**break-even point** Point where total revenue equals total cost; can be expressed in units or sales dollars. p. 407  
**budgeting** Form of planning that formalizes a company’s goals and objectives in financial terms. p. 498  
**capital budget** Budget that describes the company’s plans regarding investments, new products, or lines of business for the coming year; is used as input to prepare many of the operating budgets and becomes a formal part of the master budget. p. 502  
**capital budgeting** Financial planning activities that cover the intermediate range of time such as whether to buy or lease equipment, whether to purchase a particular investment, or whether to increase operating expenses to stimulate sales. p. 500  
**capital expenditures** Funds spent to improve an asset’s quality or to extend its life. p. 500  
**carrying value** Face amount of a bond liability less any unamortized bond discount or plus any unamortized bond premium. p. 257  
**cash** Coins, currency, checks, balances in checking and certain savings accounts, money orders, bank drafts, certificates of deposit, and other items that are payable on demand. p. 129  
**cash budget** A budget that focuses on cash receipts and payments that are expected to occur in the future. p. 508  
**cash discount** Discount offered on merchandise sold to encourage prompt payment; offered by sellers of merchandise and represent sales discounts to the purchaser when they are used and purchase discounts to the purchaser of the merchandise. p. 94  
**certified check** Check guaranteed by a bank to be drawn on an account having funds sufficient to pay the check. p. 133  
**certified suppliers** Suppliers who have gained the confidence of the buyer by providing quality goods and services at desirable prices in accordance with strict delivery specifications; frequently provide the buyer with preferred customer status in exchange for guaranteed purchase quantities and prompt payment schedules. p. 472  
**chart of accounts** List of all ledger accounts and their corresponding account numbers. p. 662  
**checks** Prenumbered forms, sometimes multi-copy, with the name of the business issuing them preprinted on the face, indicating to whom they are paid, the amount of the payment, and the transaction date. p. 131  
**claims** Owners’ and creditors’ interests in a business’s assets. p. 4  
**claims exchange transaction** Transaction that decreases one claim and increases another so that total claims do not change. For example, the accrual of interest expense is a claims exchange transaction; liabilities increase, and the recognition of the expense causes retained earnings to decrease. p. 48  
**classified balance sheet** Balance sheet that distinguishes between current and noncurrent items. p. 262  
**closely held corporation** Corporation whose stock is exchanged between a limited number of individuals. p. 288  
**closing** See closing the books.  
**closing the books** Process of transferring balances from temporary accounts (Revenue, Expense, and Dividends) to the permanent account (Retained Earnings). p. 22  
**Code of Professional Conduct** A set of guidelines established by the American Institute of Certified Public Accountants (AICPA) to promote high ethical conduct among its membership. p. 137  
**collateral** Assets pledged as security for a loan. pp. 187, 261  
**common costs** Costs that are incurred to support more than one cost object but cannot be traced to any specific object. p. 434  
**common size financial statements** Financial statements in which amounts are converted to percentages to allow a better comparison of period-to-period and company-to-company financial data since all information is placed on a common basis. p. 103  
**common stock** Basic class of corporate stock that carries no preferences as to claims on assets or dividends; certifies that evidence ownership in a company. pp. 12, 294  
**conservatism** A principle that guides accountants in uncertain circumstances to select the alternative that produces the lowest amount of net income. p. 63  
**consistency** The generally accepted accounting principle that a company should, in most circumstances, continually use the same accounting method(s) so that its financial statements are comparable across time. p. 177  
**contingent liability** A potential obligation, the amount of which depends on the outcome of future events. p. 244  
**continuity** Concept that describes the fact that a corporation’s life may extend well beyond the time at which any particular shareholder decides to retire or to sell his or her stock. p. 290  
**continuous improvement** Total quality management (TQM) feature that refers to an ongoing process through which employees learn to eliminate waste, reduce response time, minimize defects, and simplify the design and delivery of products and services to customers. p. 378
cost-plus pricing  Pricing strategy that sets the price at cost plus a markup equal to a percentage of the cost. p. 362

cost pool  A collection of costs organized around a common cost driver. The cost pool as opposed to individual costs is allocated to cost objects using the common cost driver thereby promoting efficiency in the allocation process. p. 445

cost tracing  Relating specific costs to the objects that cause their incurrence. p. 433

credit  Entry that increases liability and equity accounts or decreases asset accounts. p. 661

creditors  Individuals or institutions that have loaned goods or services to a business. p. 4

cumulative dividends  Preferred dividends that accumulate from year to year until paid. p. 295

current (short-term) assets  Assets that will be converted to cash or consumed within one year or an operating cycle, whichever is longer. p. 261

current (short-term) liability  Obligation due within one year or an operating cycle, whichever is longer. p. 261

current ratio  Measure of liquidity (short-term debt-paying ability), calculated by dividing current assets by current liabilities. p. 226

date of record  Date that establishes who will receive the dividend payment; shareholders who actually own the stock on the record date will be paid the dividend even if the stock is sold before the dividend is paid. p. 299

debit  Entry that increases asset accounts or decreases liability and equity accounts. p. 661

debt to assets ratio  Financial ratio that measures a company's level of risk. p. 329

debt to equity ratio  Financial ratio that compares creditor financing to owner financing, expressed as the dollar amount of liabilities for each dollar of stockholder's equity. p. 329

decentralization  Practice of delegating authority and responsibility for the operation of business segments. p. 512

declaration date  Date on which the board of directors actually declares a dividend. p. 299

deferral  Recognition of revenue or expense in a period after the cash is exchanged. p. 45

depreciation  Decline in value of long-term tangible assets such as buildings, furniture, or equipment. It is systematically recognized by accountants as depreciation expense over the useful lives of the affected assets. p. 202

depreciation expense  Portion of the original cost of a long-term tangible asset systematically allocated to an expense account in a given period. p. 204

differential revenues  Future-oriented revenues that differ among the alternatives under consideration. p. 467

direct cost  Cost that is easily traceable to a cost object and for which the sacrifice to trace is small in relation to the information benefits attained. p. 433

direct labor  Wages paid to production workers whose efforts can be easily and conveniently traced to products. p. 366

direct raw materials  Costs of raw materials used to make products that can be easily and conveniently traced to those products. p. 365

disclaimer of opinion  Report on financial statements issued when the auditor is unable to obtain enough information to determine if the statements conform to GAAP; is neither positive nor negative. p. 141

discount on bonds payable  Contra liability account used to record the amount of discount on a bond issue. p. 256

dividend  Transfer of wealth from a business to its owners. p. 16

 dividends in arrears  Cumulative dividends on preferred stock that have not been paid; must be paid prior to paying dividends to common stockholders. p. 295

dividend yield  Ratio for comparing stock dividends paid in relation to the market price; calculated as dividends per share divided by market price per share. p. 335

double-declining-balance depreciation  Depreciation method that recognizes larger amounts of depreciation in the early stages of an asset's life and progressively smaller amounts as the asset ages. p. 208

double-entry accounting (bookkeeping)  Method of keeping records that provides a system of checks and balances by recording transactions in a dual format. pp. 14, 661

double taxation  Policy to tax corporate profits distributed to owners twice, once when the income is reported on the corporation's income tax return and again when the dividends are reported on the individual's return. p. 289

downstream costs  Costs, such as delivery costs and sales commissions, incurred after the manufacturing process is complete. p. 371

earnings  The difference between revenues and expenses. Same as net income or profit. p. 4

earnings per share  Measure of the value of a share of common stock in terms of company earnings; calculated as net income available to common stockholders divided by the average number of outstanding common shares. p. 334

effective interest rate  Yield rate of bonds, equal to the market rate of interest on the day the bonds are sold. p. 256
company’s accounting records and the documents that support the information reported in the financial statements; includes testing the reliability of the underlying accounting system used to produce the financial reports. p. 139

financial statements Primary means of communicating the financial information of an organization to the external users. The four general-purpose financial statements are the income statement, statement of changes in equity, balance sheet, and statement of cash flows. p. 10

financing activities Cash inflows and outflows from transactions with investors and creditors (except interest). These cash flows include cash receipts from the issue of stock, borrowing activities, and cash disbursements associated with dividends. p. 21

finished goods inventory Asset account used to accumulate the product costs (direct materials, direct labor, and overhead) associated with completed products that have not yet been sold. p. 370

first-in, first-out (FIFO) cost flow method Inventory cost flow method that treats the first items purchased as the first items sold for the purpose of computing cost of goods sold. p. 172

fixed cost Cost that in total remains constant when activity volume changes; varies per unit inversely with changes in the volume of activity. p. 398

fixed cost volume variance The difference between the budgeted fixed cost and the applied fixed cost. p. 537

fixed interest rate Interest rate (charge for the use of money) that does not change over the life of the loan. p. 247

flexible budgets Budgets that show expected revenues and costs at a variety of different activity levels. p. 533

flexible budget variances Differences between budgets based on standard amounts at the actual level of activity and actual results; caused by differences in standard and actual unit cost since the volume of activity is the same. p. 538

FOB (free on board) destination Term that designates the seller as the responsible party for freight costs (transportation-in costs). p. 95

FOB (free on board) shipping point Term that designates the buyer as the responsible party for freight costs (transportation-in costs). p. 95

franchise Exclusive right to sell products or perform services in certain geographic areas. p. 217

full disclosure The accounting principle that financial statements should include all information relevant to an entity’s operations and financial condition. Full disclosure frequently requires adding footnotes to the financial statements. p. 177

gains Increases in assets or decreases in liabilities that result from peripheral or incidental transactions. p. 98

general authority Policies and procedures that apply across different levels of a company’s management, such as everyone flies coach class. p. 127

general journal Journal in which all types of accounting transactions can be entered but which is commonly used to record adjusting and closing entries and unusual types of transactions. p. 681

general ledger Complete set of accounts used in accounting systems. pp. 17, 662

generally accepted accounting principles (GAAP) Rules and regulations that accountants agree to follow when preparing financial reports for public distribution. p. 8

general, selling, and administrative costs All costs not associated with obtaining or manufacturing a product; in practice are sometimes referred to as period costs because they are normally expensed in the period in which the economic sacrifice is incurred. p. 367

general uncertainties Uncertainties inherent in operating a business, such as competition and damage from storms. Unlike contingent liabilities, these uncertainties arise from future rather than past events. p. 244

going concern assumption Assumption that a company will continue to operate indefinitely, will pay its obligations and should therefore report those obligations at their full face value in the financial statements. p. 240

goodwill Added value of a successful business that is attributable to factors—reputation, location, and superior products—that enable the business to earn above-average profits; stated differently, the excess paid for an existing business over the appraised value of the net assets. p. 218

gross margin (gross profit) Difference between sales revenue and cost of goods sold; the amount a company makes from selling goods before subtracting operating expenses. p. 89

gross margin percentage Expression of gross margin as a percentage of sales computed by dividing gross margin by net sales; the amount of each dollar of sales that is profit before deducting any operating expenses. p. 107

gross profit See gross margin.

historical cost concept Actual price paid for an asset when it was purchased. pp. 16, 203

horizontal analysis Analysis technique that compares amounts of the same item over several time periods. p. 321

horizontal statements model Arrangement of a set of financial statements horizontally across a sheet of paper. p. 23

income Added value created in transforming resources into more desirable states. p. 4

income statement Statement that measures the difference between the asset increases and the asset decreases associated with running a business. This definition is expanded in subsequent chapters as additional relationships among the elements of the financial statements are introduced. p. 18

incremental revenue Additional cash inflows from operations generated by using an additional capital asset. p. 571

independent auditor Licensed certified public accountant engaged to audit a company’s financial statements; not an employee of the audited company. p. 140

indirect cost Cost that cannot be easily traced to a cost object and for which the economic sacrifice to trace is not worth the informational benefits. pp. 368, 433
information overload  Situation in which presentation of too much information confuses the user of the information.  p. 320
installment notes  Obligations that require regular payments of principal and interest over the life of the loan.  p. 248
intangible assets  Assets that may be represented by pieces of paper or contracts that appear intangible; however, the true value of an intangible asset lies in the rights and privileges extended to its owners.  p. 202
interest  Fee paid for the use of borrowed funds; also refers to revenue from debt securities.  pp. 5, 167
internal controls  A company's policies and procedures designed to reduce the opportunity for fraud and to provide reasonable assurance that its objectives will be accomplished.  p. 126
internal rate of return  Rate that will produce a present value of an investment's future cash inflows that equals cash outflows required to acquire the investment; alternatively, the rate that produces in a net present value of zero.  p. 571
inventory cost flow methods  Methods used to allocate the cost of goods available for sale between cost of goods sold and inventory.  p. 174
inventory holding costs  Costs associated with acquiring and retaining inventory including cost of storage space; lost, stolen, or damaged merchandise; insurance; personnel and management costs; and interest.  p. 372
inventory turnover  Ratio of cost of goods sold to inventory that indicates how many times a year the average inventory is sold (turned over).  p. 328
investing activities  One of the three categories of cash inflows and outflows shown on the statement of cash flows; includes cash received and spent by the business on productive assets and investments in the debt and equity of other companies.  p. 21
investment center  Type of responsibility center for which revenue, expense and capital investments can be measured.  p. 532
investors  Company or individual who gives assets or services in exchange for security certificates representing ownership interests.  p. 4
issued stock  Stock sold to the public.  p. 289
issuer  Individual or business that issues a note payable, bonds payable, or stock (the party receiving cash). See also maker.  pp. 242, 251
journals  Books of original entry in which accounting data are entered chronologically before posting to the ledger accounts.  p. 682
just in time (JIT)  Inventory flow system that minimizes the amount of inventory on hand by making inventory available for customer consumption on demand, therefore eliminating the need to store inventory. The system reduces explicit holding costs including financing, warehouse storage, supervision, theft, damage, and obsolescence. It also eliminates hidden opportunity costs such as lost revenue due to the lack of availability of inventory.  p. 372
last-in, first-out (LIFO) cost flow method  Inventory cost flow method that treats the last items purchased as the first items sold for the purpose of computing cost of goods sold.  p. 172
legal capital  Amount of assets that should be maintained as protection for creditors; the number of shares multiplied by the par value.  p. 283
liabilities  Obligations of a business to relinquish assets, provide services, or accept other obligations.  pp. 10, 241, 261
limited liability  Concept that investors in a corporation may not be held personally liable for the actions of the corporation (the creditors cannot lay claim to the owners' personal assets as payment for the corporation's debts).  p. 290
limited liability companies (LLC)  Organizations offering many of the best features of corporations and partnerships and with many legal benefits of corporations (e.g., limited liability and centralized management) but permitted by the Internal Revenue Service to be taxed as a partnership, thereby avoiding double taxation of profits.  p. 289
line of credit  Preapproved credit arrangement with a lending institution in which a business can borrow money by simply writing a check up to the approved limit.  p. 251
liquidation  Process of dividing up the assets and returning them to the resource providers. Creditors normally receive first priority in business liquidations; in other words, assets are distributed to creditors first. After creditor claims have been satisfied, the remaining assets are distributed to the owners (investors) of the business.  p. 4
liquidity  Ability to convert assets to cash quickly and meet short-term obligations.  pp. 20, 169
liquidity ratios  Measures of short-term debt-paying ability.  p. 325
long-term liabilities  Liabilities with maturity dates beyond one year or the company's operating cycle, whichever is longer; noncurrent liabilities.  p. 247
long-term operational assets  Assets used by a business to generate revenue; condition of being used distinguishes them from assets that are sold (inventory) and assets that are held (investments).  p. 200
losses  Decreases in assets or increases in liabilities that result from peripheral or incidental transactions.  p. 98
low-ball pricing  Pricing a product below competitors’ price to lure customers away and then raising the price once customers depend on the supplier for the product.  p. 472
maker  The party issuing a note (the borrower).  p. 167
making the numbers  Expression that indicates marketing managers attained the planned master budget sales volume.  p. 536
management by exception  The philosophy of focusing management attention and resources only on those operations where performance deviates significantly from expectations.  p. 540
managerial accounting  Branch of accounting that provides information useful to internal decision makers and managers in operating an organization.  p. 6
manufacturing business  Companies that make the goods they sell to customers.  p. 24
manufacturing overhead  Production costs that cannot be traced directly to products.  p. 388
margin  Component in the determination of the return on investment. Computed by dividing operating income by sales.  p. 542
margin of safety  Difference between break-even sales and budgeted sales expressed in units, dollars, or as a percentage; the amount by which actual sales can fall below budgeted sales before a loss is incurred.  p. 410
market rate of interest  Interest rate currently available on a wide range of alternative investments with similar levels of risk.  p. 280
market value  The price at which securities sell in the secondary market; also called fair value.  p. 293
master budget  Composition of the numerous separate but interdependent departmental budgets that cover a wide range of operating and financial factors such as sales, production, manufacturing expenses, and administrative expenses.  p. 502
matching concept  Process of matching expenses with the revenues they produce; three ways to match expenses with revenues include matching expenses directly to revenues, matching expenses to the period in which they are incurred, and matching expenses systematically with revenues.  pp. 53, 168
materiality  Concept that recognizes practical limits in financial reporting by allowing flexible handling of matters not considered material; information is considered material if the decisions of a reasonable person would be influenced by its omission or misstatement; can be measured in absolute, percentage, quantitative, or qualitative terms.  p. 321
maturity date  The date a liability is due to be settled (the date the borrower is expected to repay a debt).  p. 167
merchandise business  Companies that buy and resell merchandise inventory.  p. 86
merchandise inventory  Supply of finished goods held for resale to customers.  p. 86
minimum rate of return  Minimum amount of profitability required to persuade a company to accept an investment opportunity; also known as desired rate of return, required rate of return, hurdle rate, cutoff rate, and discount rate.  p. 585
mixed costs (semivariable costs)  Costs composed of a mixture of fixed and variable components.  p. 405
multistep income statement  Income statement format that matches particular revenue items with related expense items and distinguishes between recurring operating activities and nonoperating items such as gains and losses.  p. 98
natural resources  Mineral deposits, oil and gas reserves, and reserves of timber, mines, and quarries are examples; sometimes called wasting assets because their value wastes away as the resources are removed.  p. 202
net income  Increase in net assets resulting from operating the business.  p. 18
net loss  Decrease in net assets resulting from operating the business. p. 18
net margin  Profitability measurement that indicates the percentage of each sales dollar resulting in profit; calculated as net income divided by net sales. p. 331
net present value  Evaluation technique that uses a desired rate of return to discount future cash flows back to their present value equivalents and then subtracts the cost of the investment from the present value equivalents to determine the net present value. A zero or positive net present value (present value of cash inflows equals or exceeds the present value of cash outflows) implies that the investment opportunity provides an acceptable rate of return. p. 589
net realizable value  Face amount of receivables less an allowance for accounts whose collection is doubtful (amount actually expected to be collected). p. 158
net sales  Sales less returns from customers and allowances or cash discounts given to customers. p. 102
non-sufficient-funds (NSF) check  Customer’s check deposited but returned by the bank on which it was drawn because the customer did not have enough funds in its account to pay the check. p. 133
non-value-added activities  Tasks undertaken that do not contribute to a product’s ability to satisfy customer needs. p. 377
note payable  A liability that results from executing a legal document called a promissory note which describes the interest rate, maturity date, collateral, and so on. p. 242
notes receivable  Notes that evidence rights to receive cash in the future from the maker of a promissory note; usually specify the maturity date, interest rate, and other credit terms. p. 158
operating activities  Cash inflows and outflows associated with operating the business. These cash flows normally result from revenue and expense transactions including interest. p. 21
operating budgets  Budgets prepared by different departments within a company that will become a part of the company’s master budget; typically include a sales budget, an inventory purchases budget, a selling and administrative budget, and a cash budget. p. 592
operating cycle  Time required to turn cash into inventory, inventory into receivables, and receivables back to cash. p. 261
operating income (or loss)  Income statement subtotal representing the difference between operating revenues and operating expenses, but before recognizing gains and losses from peripheral activities which are added to or subtracted from operating income to determine net income or loss. p. 59
operating leverage  Operating condition in which a percentage change in revenue produces a proportionately larger percentage change in net income; measured by dividing the contribution margin by net income. The higher the proportion of fixed cost to total costs, the greater the operating leverage. p. 398
operations budgeting  Short-range planning activities such as the development and implementation of the master budget. p. 502
opportunity  An element of the fraud triangle that recognizes weaknesses in internal controls that enable the occurrence of fraudulent or unethical behavior. p. 138
opportunity cost  Cost of lost opportunities such as the failure to make sales due to an insufficient supply of inventory or the wage a working student forgoes to attend class. pp. 373, 464
ordinary annuity  Annuity whose cash inflows occur at the end of each accounting period. p. 568
outsourcing  The practice of buying goods and services from another company rather than producing them internally. p. 471
outstanding checks  Checks deducted from the depositor’s cash account balance but not yet presented to the bank for payment. p. 133
outstanding stock  Stock owned by outside parties; normally the amount of stock issued less the amount of treasury stock. p. 293
overhead  Costs associated with producing products that cannot be cost effectively traced to products including indirect costs such as indirect materials, indirect labor, utilities, rent, and depreciation. p. 362
overhead costs  Indirect costs of doing business that cannot be directly traced to a product, department, or process, such as depreciation. p. 433
paid-in capital in excess of par (or stated) value  Any amount received above the par or stated value of stock when stock is issued. p. 296
participative budgeting  Budget technique that allows subordinates to participate with upper-level managers in setting budget objectives, thereby encouraging cooperation and support in the attainment of the company’s goals. p. 502
partnership agreement  Legal document that describes the division of income and losses. p. 288
partnerships  Business entities owned by at least two people who share talents, capital, and the risks of the business. p. 288
par value  Arbitrary value assigned to stock by the board of directors. p. 293
patent  Legal right granted by the U.S. Patent Office ensuring a company or an individual the exclusive right to a product or process. p. 217
payback method  Technique that evaluates investment opportunities by determining the length of time necessary to recover the initial net investment through incremental revenue or cost savings; the shorter the period, the better the investment opportunity. p. 578
payee  The party collecting cash. p. 167
payment date  Date on which a dividend is actually paid. p. 300
percentage analysis  Analysis of relationships between two different items to draw conclusions or make decisions. p. 322
percent of receivables method  Estimating the amount of the allowance for doubtful accounts as a percentage of the outstanding receivables balance. The percentage is typically based on a combination of factors such as historical experience, economic conditions, and the company’s credit policies. p. 164
percent of revenue method  Estimating the amount of uncollectible accounts expense as a percentage of the revenue earned on account during the accounting period. The percentage is typically based on a combination of factors such as historical experience, economic conditions, and the company’s credit policies. p. 163
period costs  General, selling, and administrative costs that are expensed in the period in which the economic sacrifice is made. pp. 53, 89
periodic inventory system  Method of accounting for changes in the Inventory account only at the end of the accounting period. p. 106
permanent accounts  Accounts that contain information transferred from one accounting period to the next. p. 22
perpetual (continuous) budgeting  Continuous budgeting activity normally covering a 12-month time span by replacing the current month’s budget at the end of each month with a new budget; keeps management constantly involved in the budget process so that changing conditions are incorporated on a timely basis. p. 500
perpetual inventory system  Method of accounting for inventories that increases the Inventory account each time merchandise is purchased and decreases it each time merchandise is sold. p. 106
physical flow of goods  Physical movement of goods through the business; normally a FIFO flow so that the first goods purchased are the first goods delivered to customers, thereby reducing the likelihood of obsolete inventory. p. 172
plant assets  Long-term liabilities  Financial ratio that suggests how well a company manages its long-term debt. p. 321
postaudit  Repeat calculation using the techniques originally employed to analyze an investment project; accomplished with the use of actual data available at the completion of the investment project so that the actual results can be compared with expected results based on estimated data at the beginning of the project. Its purpose is to provide feedback as to whether the expected results were actually accomplished in improving the accuracy of future analysis. p. 581
posting  Process of copying information from journals to ledgers. p. 662
predetermined overhead rate  Allocation rate calculated before actual costs or activity are known; determined by dividing the estimated overhead costs for the coming period by some measure of estimated total production activity for the period, such as the number of labor-hours or machine-hours. The base should relate rationally to overhead use. The rate is used throughout the accounting period to allocate overhead costs to work in process inventory based on actual production activity. p. 445
preferred stock  Stock that receives some form of preferential treatment (usually as to dividends) over common stock; normally has no voting rights. p. 294
premium on bonds payable Difference between the selling price and the face amount of a bond that is sold for more than the face amount. p. 260
prepaid items Deferred expenses. An example is prepaid insurance. p. 54
present value index Present value of cash inflows divided by the present value of cash outflows. Higher index numbers indicate higher rates of return. p. 574
present value table Table that consists of a list of factors to use in converting future values into their present value equivalents; composed of columns that represent different return rates and rows that depict different periods of time. p. 566
pressure An element of the fraud triangle that recognizes conditions that motivate fraudulent or unethical behavior. p. 139
price-earnings (P/E) ratio Measurement used to compare the values of different stocks in terms of earnings; calculated as market price per share divided by earnings per share. p. 334
principal Amount of cash actually borrowed. p. 187
procedures manual Manual that sets forth the accounting procedures to be followed. p. 127
product costing Classification and accumulation of individual inputs (materials, labor, and overhead) for determining the cost of making a good or providing a service. p. 382
product costs All costs related to obtaining or manufacturing a product intended for sale to customers; are accumulated in inventory accounts and expensed as cost of goods sold at the point of sale. For a manufacturing company, product costs include direct materials, direct labor, and manufacturing overhead. pp. 89, 362
productive assets Assets used to operate the business; frequently called long-term assets. p. 21
product-level costs Costs incurred to support different kinds of products or services; can be avoided by the elimination of a product line or a type of service. p. 468
profitability ratios Measurements of a firm’s ability to generate earnings. p. 355
profit center Type of responsibility center for which both revenues and costs can be identified. p. 532
pro forma financial statements Budgeted financial statements prepared from the information in the master budget. p. 502
promissory note A legal document representing a credit agreement between a lender and a borrower. The note specifies technical details such as the maker, payee, interest rate, maturity date, payment terms, and any collateral. p. 186
property, plant, and equipment Category of assets, sometimes called plant assets, used to produce products or to carry on the administrative and selling functions of a business; includes machinery and equipment, buildings, and land. p. 202
purchase discount Reduction in the gross price of merchandise extended under the condition that the purchaser pay cash for the merchandise within a stated time (usually within 10 days of the date of the sale). p. 94
purchase returns and allowances A reduction in the cost of purchases resulting from dissatisfaction with merchandise purchased. p. 83
qualified opinion Opinion issued by a certified public accountant that means the company’s financial statements are, for the most part, in compliance with GAAP, but there is some circumstance (explained in the auditor’s report) about which the auditor has reservations; contrast with unqualified opinion. p. 141
qualitative characteristics Nonquantifiable features such as company reputation, welfare of employees, and customer satisfaction that can be affected by certain decisions. p. 466
quantitative characteristics Numbers in decision making subject to mathematical manipulation, such as the dollar amounts of revenues and expenses. p. 466
quick ratio See acid-test ratio. p. 326
ratio analysis See percentage analysis. p. 324
rationalization An element of the fraud triangle that recognizes a human tendency to justify fraudulent or unethical behavior. p. 139
raw materials Physical commodities (e.g., wood, metal, paint) used in the manufacturing process. p. 365
raw materials inventory Asset account used to accumulate the costs of materials (such as lumber, metals, paints, chemicals) that will be used to make a company’s products. p. 370
realization A term that usually refers to actually collecting cash. p. 44
recognition Reporting an accounting event in the financial statements. p. 44
recovery of investment Recovery of the funds used to acquire the original investment. p. 580
reengineering Business practices designed by companies to make production and delivery systems more competitive in world markets by eliminating or minimizing waste, errors, and costs. p. 376
reinvest Record an account receivable previously written off back into the accounting records, generally when cash is collected long after the original due date. p. 162
relative fair market value method Method of assigning value to individual assets acquired in a basket purchase in which each asset is assigned a percentage of the total price paid for all assets. The percentage assigned equals the market value of a particular asset divided by the total of the market values of all assets acquired in the basket purchase. p. 203
relevant costs Future-oriented costs that differ between business alternatives; also known as avoidable costs. p. 485
relevant information Decision-making information about costs, costs savings, or revenues that have these features: (1) future-oriented information and (2) the information differs between the alternatives; decision-specific (information that is relevant in one decision may not be relevant in another decision). p. 464
relevant range Range of activity over which the definitions of fixed and variable costs are valid. p. 405
reliability concept Information is reliable if it can be independently verified. Reliable information is factual rather than subjective. p. 17
reporting entities Particular businesses or other organizations for which financial statements are prepared. p. 9
residual income Approach that evaluates managers on their ability to maximize the dollar value of earnings above some target level of earnings. p. 543
responsibility accounting Performance measure that evaluates managers based on how well they maximize the dollar value of earnings above some target level of earnings. p. 530
responsibility center Point in an organization where the control over revenue or expense items is located. p. 532
restrictive covenants Special provisions specified in the loan contract that are designed to prohibit management from taking certain actions that place creditors at risk. p. 261
retail companies Companies that sell goods to consumers. p. 86
retained earnings Portion of stockholders’ equity that includes all earnings retained in the business since inception (revenues minus expenses and distributions for all accounting periods). p. 12
return on equity Measure of the profitability of a firm based on earnings generated in relation to stockholders’ equity; calculated as net income divided by stockholders’ equity. p. 333
return on investment Measure of profitability based on the asset base of the firm. It is calculated as net income divided by average total assets. ROI is a product of net margin and asset turnover. pp. 332, 540
return on sales Percent of net income generated by each $1 of sales; computed by dividing net income by net sales. p. 103
revenue The economic benefit (increase in assets or decrease in liabilities) gained by providing goods or services to customers. p. 10
revenue expenditures Costs incurred for repair or maintenance of long-term operational assets; recorded as expenses and subtracted from revenue in the accounting period in which incurred. p. 214
salaries payable Amounts of future cash payments owed to employees for services that have already been performed. p. 46
sales discount Cash discount extended by the seller of goods to encourage prompt payment. When the buyer of the goods takes advantage of the discount to pay less than the original selling price, the difference between the selling price and the cash collected is the sales discount. p. 101
sales price variance Difference between actual sales and expected sales based on the standard sales price per unit times the actual level of activity. p. 538
sales return and allowances A reduction in sales revenue resulting from dissatisfaction with merchandise sold. p. 103
Glossary 675
transferability  Concept referring to the practice of dividing the ownership of corporations into small units that are represented by shares of stock, which permits the easy exchange of ownership interests. p. 290

transportation-in (freight-in)  Cost of freight on goods purchased under terms FOB shipping point that is usually added to the cost of inventory and is a product cost. p. 95

transportation-out (freight-out)  Freight cost for goods delivered to customers under terms FOB destination; a period cost expensed when it is incurred. p. 95

treasury stock  Stock first issued to the public and then bought back by the corporation. p. 293

trend analysis  Study of the performance of a business over a period of time. p. 321

trial balance  List of ledger accounts and their balances that provides a check on the mathematical accuracy of the recording process. p. 664

due to balance  Actual balance of cash owned by a company at the close of business on the date of the bank statement. p. 131

turnover  Component in the determination of the return on investment. Computed by dividing sales by operating assets. p. 542

2/10, n/30  Expression meaning the seller will allow the purchaser a 2 percent discount off the gross invoice price if the purchaser pays cash for the merchandise within 10 days from the date of purchase. p. 94

unadjusted bank balance  Ending cash balance reported by the bank as of the date of the bank statement. p. 131

unadjusted book balance  Balance of the Cash account as of the date of the reconciliation before making any adjustments. p. 131

unadjusted rate of return  Measure of profitability computed by dividing the average incremental increase in annual net income by the average cost of the original investment (original cost − 2). p. 579

uncollectible accounts expense  Expense associated with uncollectible accounts receivable; the amount recognized may be estimated using the percent of revenue or the percent of receivables method, or actual losses may be recorded using the direct write-off method. p. 159

unearned revenue  Revenue for which cash has been collected but the service has not yet been performed. p. 55

unfavorable variance  Variance that occurs when actual costs exceed standard costs or when actual sales are less than standard sales. p. 535

unit-level costs  Costs incurred each time a company makes a single product or performs a single service and that can be avoided by eliminating a unit of product or service. Likewise, unit-level costs increase with each additional product produced or service provided. p. 467

units-of-production depreciation  Depreciation method based on a measure of production rather than a measure of time; for example, an automobile may be depreciated based on the expected miles to be driven rather than on a specific number of years. p. 211

unqualified opinion  Opinion issued by a certified public accountant that means the company’s financial statements are, in all material respects, in compliance with GAAP; the auditor has no reservations. Contrast with qualified opinion. p. 141

upstream costs  Costs incurred before the manufacturing process begins, for example, research and development costs. p. 321

value-added activity  Any unit of work that contributes to a product’s ability to satisfy customer needs. p. 377

value-added principle  The benefits attained (value added) from the process should exceed the cost of the process. p. 381

value chain  Linked sequence of activities that create value for the customer. p. 377

variable cost  Cost that in total changes in direct proportion to changes in volume of activity; remains constant per unit when volume of activity changes. p. 387

variable cost volume variance  The difference between a variable cost calculated at the planned volume of activity and the same variable cost calculated at the actual volume of activity. p. 535

variable interest rate  Interest rate that fluctuates (may change) from period to period over the life of the loan. p. 247

variances  Differences between standard and actual amounts. p. 535

vertical analysis  Analysis technique that compares items on financial statements to significant totals. p. 324

vertical integration  Attainment of control over the entire spectrum of business activity from production to sales; as an example a grocery store that owns farms. p. 472

vertical statements model  Arrangement of a full set of financial statements on a single page with account titles arranged from the top to the bottom of the page. p. 82

warranties  Promises to correct deficiencies or dissatisfactions in quality, quantity, or performance of products or services sold. p. 245

weighted-average cost flow method  Inventory cost flow method in which the cost allocated between inventory and cost of goods sold is based on the average cost per unit, which is determined by dividing total costs of goods available for sale during the accounting period by total units available for sale during the period. If the average is recomputed each time a purchase is made, the result is called a moving average. p. 172

wholesale companies  Companies that sell goods to other businesses. p. 86

withdrawals  Distributions to the owners of proprietorships and partnerships. p. 291

work in process inventory  Asset account used to accumulate the product costs (direct materials, direct labor, and overhead) associated with incomplete products that have been started but are not yet completed. p. 370

working capital  Current assets minus current liabilities. p. 579

working capital ratio  Another term for the current ratio; calculated by dividing current assets by current liabilities. p. 326