

Contents

	PREFACE	xiii
ONE	ACCOUNTING: THE LANGUAGE OF BUSINESS	1
	The purpose and nature of accounting. A system for creating accounting information. Communicating accounting information—who uses accounting reports? Public accounting. Private accounting. Governmental accounting. Development of accounting standards—the FASB. Two primary business objectives. Accounting as the basis for business decisions. Internal control. Forms of business organization. Financial statements: the starting point in the study of accounting. The balance sheet. Assets. Accounting for inflation. Liabilities. Owners' equity. What is capital stock? The accounting equation. Effects of business transactions upon the balance sheet. Effects of business transactions upon the accounting equation. Use of financial statements by outsiders.	
TWO	RECORDING CHANGES IN FINANCIAL POSITION	43
	The use of "accounts" for recording transactions. The ledger. Debit and credit entries. Recording transactions in ledger accounts: illustration. Running balance form of ledger account. The normal balance of an account. Sequence and numbering of ledger accounts. Flow of information through the accounting system. The journal. Posting. The trial balance. Uses and limitations of the trial balance. Locating errors. Accounting records in perspective.	
THREE	MEASURING BUSINESS INCOME	78
	Profits: public image versus economic function. Retained earnings. Net income. Revenue. Expenses. Dividends. Matching revenue and expenses. Relating revenue and expenses to time periods. Rules of debit and credit for revenue and expenses. Ledger accounts for Greenhill Real Estate Company: illustration. Recording depreciation at the end of the period. The adjusted trial balance. Financial statements. The income statement. Statement of retained earnings. The balance sheet. Closing the accounts. After-closing trial balance. Sequence of accounting procedures. Dividends—declaration and payment. Accrual basis of accounting versus cash basis of accounting.	

FOUR

COMPLETION OF THE ACCOUNTING CYCLE

121

Accounting periods and financial statements. Apportioning transactions between accounting periods. Principal types of transactions requiring adjusting entries. Recorded costs apportioned between accounting periods. Recorded revenue apportioned between accounting periods. Unrecorded expenses. Unrecorded revenue. Adjusting entries and the accrual basis of accounting. The work sheet. Preparing the work sheet. Preparing financial statements from the work sheet. Recording adjusting entries in the accounting records. Sequence of accounting procedures when work sheet is used. The accounting cycle. Preparing monthly financial statements without closing the accounts.

FIVE

MERCHANDISING TRANSACTIONS AND INTERNAL CONTROL

162

ACCOUNTING FOR A MERCHANDISING BUSINESS

Income statement for a merchandising business. Analyzing the income statement. Sales of merchandise. The cost of goods sold. The purchases account. Inventory of merchandise and cost of goods sold. The perpetual inventory system. The periodic inventory system. Inflation and the cost of replacing inventories. Illustration of accounting cycle using periodic inventory method. Work sheet for a merchandising business. Summary of merchandising transactions and related accounting entries.

THE SYSTEM OF INTERNAL CONTROL

The meaning of internal control. Administrative controls and accounting controls. Strong internal control now required by law. Guidelines to strong internal control. Organization plan to establish responsibility for every function. Control of transactions. Subdivision of duties strengthens internal control. Internal control in the small business. Internal controls over the purchase and sale of merchandise.

CLASSIFIED FINANCIAL STATEMENTS

The purpose of balance sheet classification. Current assets. Current liabilities. Current ratio. Working capital. Classification in the income statement. Condensed income statement.

SIX

ACCOUNTING SYSTEMS: MANUAL AND EDP

221

MANUAL ACCOUNTING SYSTEMS

Sales journal. Controlling accounts and subsidiary ledgers. Purchases journal. Cash receipts journal. Cash payments

journal. The general journal. Subsidiary ledger accounts. Variations in special journals. Direct posting from invoices.

MECHANICAL ACCOUNTING SYSTEMS

Unit record for each transaction. Simultaneous preparation of documents, journals, and ledgers. Accounting machines. Punched cards and tabulating equipment.

EDP ACCOUNTING SYSTEMS

Elements of an EDP system. Hardware and software. Input devices. Output devices. Processing operations in the computer. Programs. Reliability of EDP systems. Accounting applications of the computer. Computer service centers and time-sharing. Do computers make decisions? Information systems.

SEVEN

FORMS OF BUSINESS ORGANIZATION

268

SINGLE PROPRIETORSHIPS

Accounting for the owner's equity in a single proprietorship. Closing the accounts. Financial statements for a single proprietorship.

PARTNERSHIPS

Significant features of a partnership. Partnership accounting. Partnership profits and income taxes. Alternative methods of dividing partnership income.

CORPORATIONS

Advantages and disadvantages of the corporate form of organization. Formation of a corporation. Functions of the board of directors. Functions of corporate officers. Authorization and issuance of capital stock. Par value. No-par value stock. Preferred and common stock. Characteristics of preferred stock. The underwriting of stock issues. Market price of common stock. Stock issued for assets other than cash. Subscriptions to capital stock. Retained earnings or deficit. Special records of corporations. Income taxes in corporate financial statements. Balance sheet for a corporation illustrated.

EIGHT

CORPORATIONS: EARNINGS PER SHARE, RETAINED EARNINGS, AND DIVIDENDS

312

Developing predictive information. Discontinued operations of a segment of a business. Extraordinary items. Other nonoperating gains and losses. Earnings per share (EPS). Primary and fully diluted earnings per share. Income statement for a corporation illustrated. Cash dividends. Dividend dates. Property and liquidating dividends. Stock dividends. Stock splits. Retained earnings. Prior period adjustments to the Retained Earnings

account. Appropriations and restrictions of retained earnings. Statement of retained earnings. Treasury stock. Book value per share of common stock. Illustration of stockholders' equity section.

NINE

CASH AND MARKETABLE SECURITIES

351

CASH

Balance sheet presentation. Management responsibilities relating to cash. Basic requirements for internal control over cash. Cash receipts. Cash disbursements. The voucher system. Petty cash. Bank checking accounts. The bank statement. Reconciling the bank account. Electronic funds transfer system (EFTS).

INVESTMENTS IN MARKETABLE SECURITIES

Reasons for investing in marketable securities. Securities exchanges. Determining the cost of investments in stocks and bonds. Gains and losses from sale of investments in securities. Balance sheet valuation of marketable securities. Lower of cost or market. The argument for valuation at market value. Presentation of marketable securities in financial statements. Investments for purposes of control. The equity method.

TEN

RECEIVABLES AND PAYABLES

392

Accounts receivable. Uncollectible accounts. Reflecting uncollectible accounts in the financial statements. The allowance for doubtful accounts. Estimating uncollectible accounts expense. Writing off an uncollectible account receivable. Recovery of an account previously written off. Direct charge-off method of recognizing uncollectible accounts expense. Credit card sales. Analysis of accounts receivable. Notes receivable. Nature of interest. Accounting for notes receivable. Discounting notes receivable. Classification of receivables in the balance sheet. Current liabilities. Notes payable. Notes payable with interest included in the face amount. Discounts on notes payable. Comparison of the two forms of notes payable. The concept of present value applied to long-term notes. Installment receivables. Income tax aspects of installment sales.

ELEVEN

INVENTORIES

435

Some basic questions relating to inventory. Inventory defined. Inventory valuation and the measurement of income. Importance of an accurate valuation of inventory. Taking a physical inventory. Pricing the inventory. Cost basis of inventory valuation. Inventory valuation methods. Consistency in the valuation

of inventory. The environment of inflation. Inventory profits. The SEC rules on replacement cost. The lower-of-cost-or-market rule. Gross profit method of estimating inventories. The retail method of inventory valuation. Perpetual inventory system. Inventories for a manufacturing business.

TWELVE

PLANT AND EQUIPMENT, DEPRECIATION, NATURAL RESOURCES, AND INTANGIBLE ASSETS

475

PLANT AND EQUIPMENT

Plant and equipment represent bundles of services to be received. Major categories of plant and equipment. Accounting problems relating to plant and equipment. Determining the cost of plant and equipment. Leased property. Capital expenditures and revenue expenditures. Extraordinary repairs.

DEPRECIATION

Allocating the cost of plant and equipment over the years of use. Accumulated depreciation does not consist of cash. Causes of depreciation. Methods of computing depreciation. Revision of depreciation rates. Depreciation and income taxes. Inflation and depreciation. Depreciation not a process of valuation. Historical cost versus replacement cost. The SEC requirement for disclosure of replacement cost. Disposal of plant and equipment. Trading in used assets on new.

NATURAL RESOURCES

Accounting for natural resources. Depletion.

INTANGIBLE ASSETS

Characteristics. Operating expenses versus intangible assets. Amortization. Goodwill. Patents. Franchises. Trademarks. Other intangibles and deferred charges.

THIRTEEN

BONDS PAYABLE, LEASES, AND OTHER LIABILITIES

516

BONDS PAYABLE

Characteristics of a bond. Effect of bond financing on holders of capital stock. Accounting entries for a bond issue. The concept of present value. The present value concept and bond prices. Bonds sold at a discount. Amortization of bond discount. Bonds sold at a premium. Year-end adjustments for bond interest expense. Straight-line amortization: a theoretical shortcoming. Effective interest method of amortization. Amortization of bond discount or premium from the investor's viewpoint. Retirement of bonds payable. Conversion of bonds payable into common stock. Bond sinking fund.

LEASES

Operating lease. Capital lease. Distinguishing between capital leases and operating leases. New standards reduce off-balance-sheet financing.

OTHER LIABILITIES

Mortgages payable. Pension plans. Payroll accounting. Deductions from earnings of employees. Payroll records and procedures. Payroll taxes on the employer. Other current liabilities. Loss contingencies.

FOURTEEN

ACCOUNTING PRINCIPLES AND CONCEPTS: CURRENT-VALUE ACCOUNTING

559

Generally accepted accounting principles. The conceptual framework project. Authoritative support for accounting principles. The accounting environment. The accounting entity concept. The going-concern assumption. The time period principle. The objectivity principle. Asset valuation: the cost principle. The monetary principle. Measuring revenue: the realization principle. Measuring expenses: the matching principle. Recognition of gains and losses. The consistency principle. The disclosure principle. Materiality. Conservatism as a guide in resolving uncertainties. Opinion rendered by independent CPAs on client's financial statements. The search for better financial reporting. Inflation—the greatest challenge to accounting. Profits—fact or illusion. Two approaches to "inflation accounting." Financial statements adjusted for changes in the general price level. Illustration of common dollar financial statements. Gains and losses in purchasing power. Interpreting the common dollar income statement. Current-value accounting distinguished from general price level accounting. Current-value accounting—objectives and problems. What direction will inflation accounting take?

FIFTEEN

STATEMENT OF CHANGES IN FINANCIAL POSITION: CASH FLOWS

603

STATEMENT OF CHANGES IN FINANCIAL POSITION

"Funds" defined as working capital. Sources and uses of working capital. Simple illustration. Effect of transactions on working capital. Working capital provided by operations. Preparation of more complex statement of changes in financial position.

CASH FLOW ANALYSIS

Cash flow from operations. Conversion of an income statement to cash basis. Cash flow statement.

SIXTEEN

**ANALYSIS AND INTERPRETATION OF
FINANCIAL STATEMENTS**

639

What is your opinion of the level of corporate profits? Sources of financial information. Tools of analysis. Dollar and percentage changes. Component percentages. Comparative income statement. Ratios. Standards of comparison. Past performance of the company. Industry standards. Objectives of financial analysis. Quality of earnings. Quality of assets and the relative amount of debt. Impact of inflation. Illustrative analysis for Seacliff Company. Analysis by common stockholders. Return on investment (ROI). Leverage. Analysis by long-term creditors. Analysis by preferred stockholders. Analysis by short-term creditors. Summary of analytical measurements.

SEVENTEEN

INCOME TAXES AND BUSINESS DECISIONS

680

The critical importance of income taxes. The federal income tax: history and objectives. The effect of income taxes on business decisions. Classes of taxpayers. Cash basis of accounting for individual tax returns. Tax rates. Tax rate schedules. The steeply progressive nature of income taxes. Marginal tax rates compared with average tax rates. Maximum tax on personal service income (earned income). Income taxes and inflation. Income tax formula for individuals. Total income and gross income. Deductions to arrive at adjusted gross income. Deductions from adjusted gross income (itemized deductions). Zero bracket amount. Excess itemized deductions. Personal exemptions. Taxable income. Capital gains and losses. Tax tables. Tax credits. Quarterly payments of estimated tax. Tax returns, tax refunds, and payment of the tax. Withholding makes the system work. Computation of individual income tax illustrated. Partnerships. Taxation of corporations. Corporation tax rates. Illustrative tax computation for corporation. Accumulated earnings tax. Personal holding company tax. Accounting income versus taxable income. Cash basis versus accrual basis of accounting. Alternative accounting methods offering possible tax advantages. Interperiod income tax allocation. Tax planning. Tax avoidance and tax evasion. Form of business organization. Planning business transactions to minimize income taxes. Tax planning in the choice of financial structure. Tax shelters.

APPENDIX:

**FINANCIAL STATEMENTS OF A PUBLICLY OWNED
COMPANY**

727

INDEX

739