WARREN, FESS, REEVE 18TH ED.

ACCOUNTING

18E

ACCOUNTING

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Accounting, 18e

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IN ITS SEVENTH DECADE OF PUTTING STUDENTS *FIRST.*

Accounting, 18e...

THE STUDENT-APPROVED PACKAGE FOR LEARNING ACCOUNTING

65th

IN ITS SEVENTH DECADE OF PUTTING STUDENTS *FIRST.*

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Accounting, 18e, is the time-tested leader for teaching accounting in an interesting and understandable way. This renowned learning system continues to be the preferred teaching tool on campuses coast to coast. Through generations of users, *Accounting* has focused on the most current and relevant topics and applications ... providing you with the accounting you need to know as you enter the business world.

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2. **Work the problems** assigned by your instructor.
3. **Complete the Continuing Problem** in Chs. 1 - 4 so you'll understand an accounting basic — the accounting cycle.
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5. **Attend class!** Note-taking during lectures coupled with reading your text will make your accounting experience a successful one.

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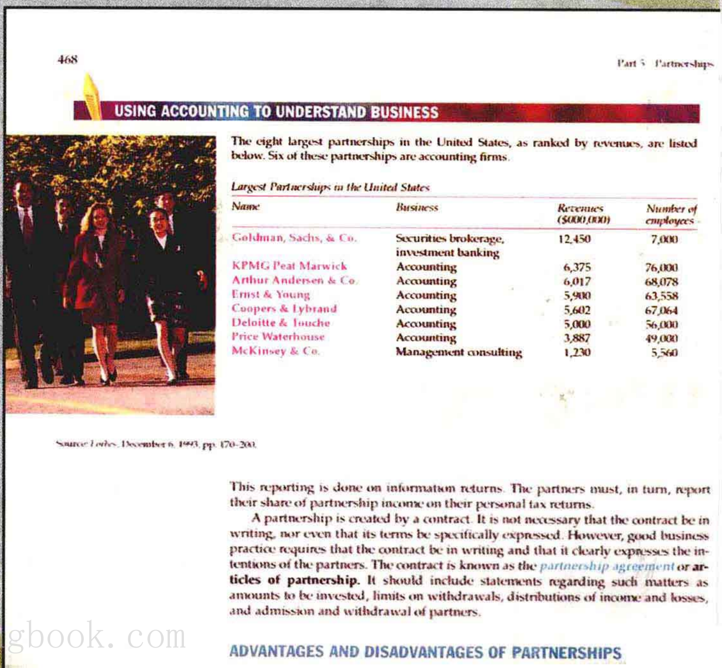
468 Part 5 Partnerships

USING ACCOUNTING TO UNDERSTAND BUSINESS

The eight largest partnerships in the United States, as ranked by revenues, are listed below. Six of these partnerships are accounting firms.

Largest Partnerships in the United States

Name	*Business*	*Revenues ($000,000)*	*Number of employees*
Goldman, Sachs, & Co.	Securities brokerage, investment banking	12,450	7,000
KPMG Peat Marwick	Accounting	6,375	76,000
Arthur Andersen & Co.	Accounting	6,017	68,078
Ernst & Young	Accounting	5,900	63,558
Coopers & Lybrand	Accounting	5,602	67,064
Deloitte & Touche	Accounting	5,000	56,000
Price Waterhouse	Accounting	3,887	49,000
McKinsey & Co.	Management consulting	1,230	5,560

Source: *Forbes*, December 6, 1993, pp. 170-200.

This reporting is done on information returns. The partners must, in turn, report their share of partnership income on their personal tax returns.

A partnership is created by a contract. It is not necessary that the contract be in writing, nor even that its terms be specifically expressed. However, good business practice requires that the contract be in writing and that it clearly expresses the intentions of the partners. The contract is known as the *partnership agreement* or **articles of partnership.** It should include statements regarding such matters as amounts to be invested, limits on withdrawals, distributions of income and losses, and admission and withdrawal of partners.

ADVANTAGES AND DISADVANTAGES OF PARTNERSHIPS

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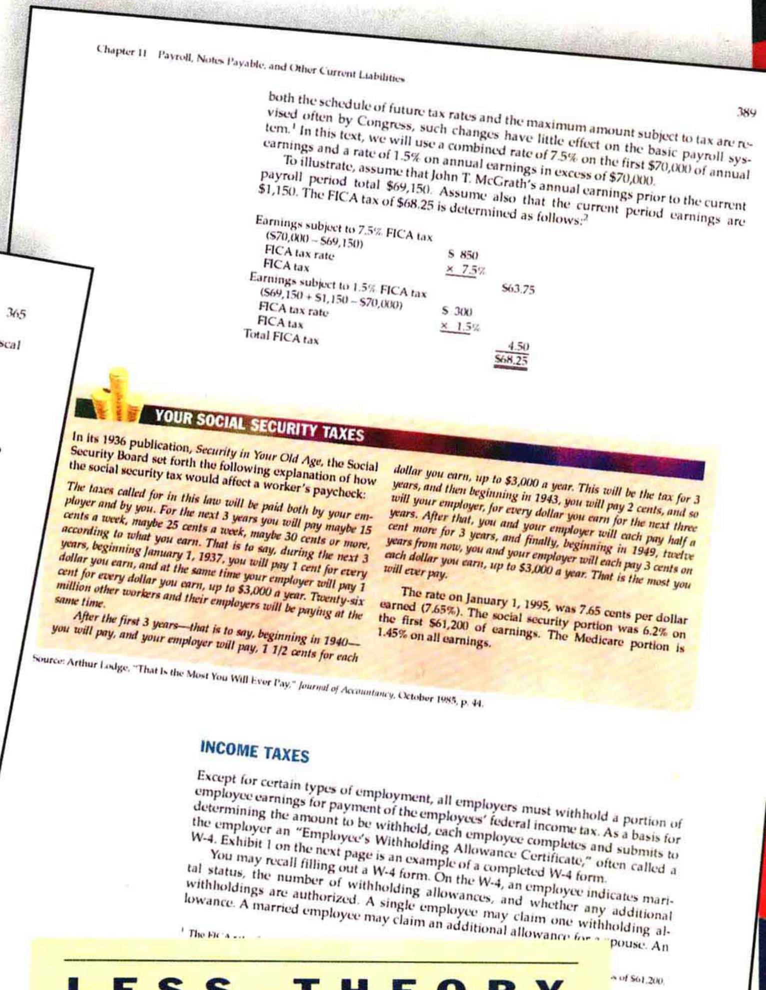
This learning package is current in its content, its style of teaching, and as a flexible learning system. It's the culmination of our asking instructors what they need for teaching, what works with students, and which teaching tools really make a difference in the classroom. Count on ***Accounting*** to be the learning package that will help you succeed in the accounting portion of your business curriculum.

WHAT CAN YOU EXPECT?

Content that's relevant to you. A format and writing style that students like you told us you like. And examples that make accounting more interesting, more pertinent, more real world. We even bring you video lecture tapes and a Student Tutorial Software in case you miss class or need extra help. We want you to succeed so we offer an unparalleled supplemental learning package to help you do just that. That's why *Accounting, 18e,* stays number one —— by making you number one!



Chapter 11 Payroll, Notes Payable, and Other Current Liabilities 389

both the schedule of future tax rates and the maximum amount subject to tax are revised often by Congress, such changes have little effect on the basic payroll system.[1] In this text, we will use a combined rate of 7.5% on the first $70,000 of annual earnings and a rate of 1.5% on annual earnings in excess of $70,000.

To illustrate, assume that John T. McGrath's annual earnings prior to the current payroll period total $69,150. Assume also that the current period earnings are $1,150. The FICA tax of $68.25 is determined as follows:[2]

Earnings subject to 7.5% FICA tax ($70,000 – $69,150)	$ 850	
FICA tax rate	× 7.5%	
FICA tax		$63.75
Earnings subject to 1.5% FICA tax ($69,150 + $1,150 – $70,000)	$ 300	
FICA tax rate	× 1.5%	
FICA tax		4.50
Total FICA tax		$68.25

YOUR SOCIAL SECURITY TAXES

In its 1936 publication, *Security in Your Old Age*, the Social Security Board set forth the following explanation of how the social security tax would affect a worker's paycheck:

The taxes called for in this law will be paid both by your employer and by you. For the next 3 years you will pay maybe 15 cents a week, maybe 25 cents a week, maybe 30 cents or more, according to what you earn. That is to say, during the next 3 years, beginning January 1, 1937, you will pay 1 cent for every dollar you earn, and at the same time your employer will pay 1 cent for every dollar you earn, up to $3,000 a year. Twenty-six million other workers and their employers will be paying at the same time.

After the first 3 years—that is to say, beginning in 1940—you will pay, and your employer will pay, 1 1/2 cents for each dollar you earn, up to $3,000 a year. This will be the tax for 3 years, and then beginning in 1943, you will pay 2 cents, and so will your employer, for every dollar you earn for the next three years. After that, you and your employer will each pay half a cent more for 3 years, and finally, beginning in 1949, twelve years from now, you and your employer will each pay 3 cents on each dollar you earn, up to $3,000 a year. That is the most you will ever pay.

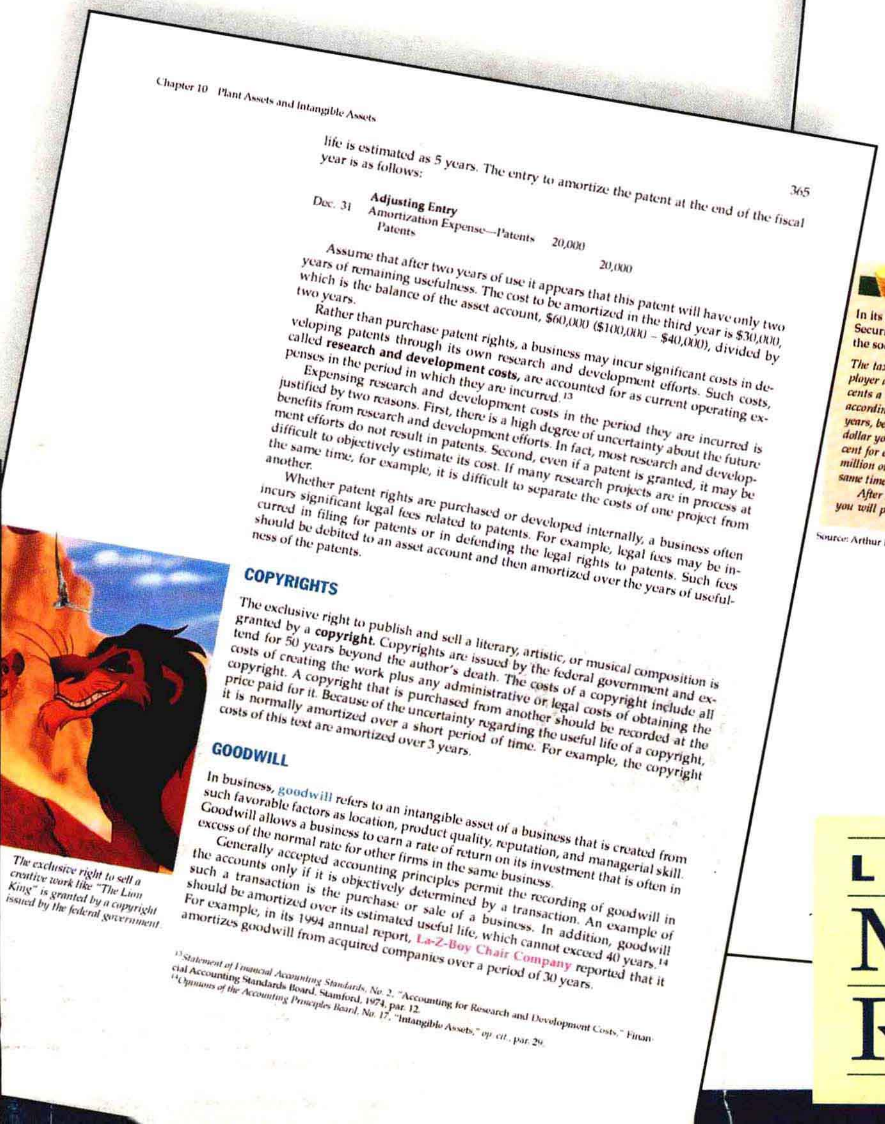
The rate on January 1, 1995, was 7.65 cents per dollar earned (7.65%). The social security portion was 6.2% on the first $61,200 of earnings. The Medicare portion is 1.45% on all earnings.

Source: Arthur Lodge, "That Is the Most You Will Ever Pay," *Journal of Accountancy*, October 1985, p. 44.

INCOME TAXES

Except for certain types of employment, all employers must withhold a portion of employee earnings for payment of the employees' federal income tax. As a basis for determining the amount to be withheld, each employee completes and submits to the employer an "Employee's Withholding Allowance Certificate," often called a W-4. Exhibit 1 on the next page is an example of a completed W-4 form.

You may recall filling out a W-4 form. On the W-4, an employee indicates marital status, the number of withholding allowances, and whether any additional withholdings are authorized. A single employee may claim one withholding allowance. A married employee may claim an additional allowance for a spouse. An



Chapter 10 Plant Assets and Intangible Assets 365

life is estimated as 5 years. The entry to amortize the patent at the end of the fiscal year is as follows:

Dec. 31	**Adjusting Entry**		
	Amortization Expense—Patents	20,000	
	Patents		20,000

Assume that after two years of use it appears that this patent will have only two years of remaining usefulness. The cost to be amortized in the third year is $30,000, which is the balance of the asset account, $60,000 ($100,000 – $40,000), divided by two years.

Rather than purchase patent rights, a business may incur significant costs in developing patents through its own research and development efforts. Such costs, called **research and development costs**, are accounted for as current operating expenses in the period in which they are incurred.[13]

Expensing research and development costs in the period they are incurred is justified by two reasons. First, there is a high degree of uncertainty about the future benefits from research and development efforts. In fact, most research and development efforts do not result in patents. Second, even if a patent is granted, it may be difficult to objectively estimate its cost. If many research projects are in process at the same time, for example, it is difficult to separate the costs of one project from another.

Whether patent rights are purchased or developed internally, a business often incurs significant legal fees related to patents. For example, legal fees may be incurred in filing for patents or in defending the legal rights to patents. Such fees should be debited to an asset account and then amortized over the years of usefulness of the patents.

COPYRIGHTS

The exclusive right to publish and sell a literary, artistic, or musical composition is granted by a **copyright**. Copyrights are issued by the federal government and extend for 50 years beyond the author's death. The costs of a copyright include all costs of creating the work plus any administrative or legal costs of obtaining the copyright. A copyright that is purchased from another should be recorded at the price paid for it. Because of the uncertainty regarding the useful life of a copyright, it is normally amortized over a short period of time. For example, the copyright costs of this text are amortized over 3 years.

GOODWILL

In business, goodwill refers to an intangible asset of a business that is created from such favorable factors as location, product quality, reputation, and managerial skill. Goodwill allows a business to earn a rate of return on its investment that is often in excess of the normal rate for other firms in the same business.

Generally accepted accounting principles permit the recording of goodwill in the accounts only if it is objectively determined by a transaction. An example of such a transaction is the purchase or sale of a business. In addition, goodwill should be amortized over its estimated useful life, which cannot exceed 40 years.[14] For example, in its 1994 annual report, La-Z-Boy Chair Company reported that it amortizes goodwill from acquired companies over a period of 30 years.

The exclusive right to sell a creative work like "The Lion King" is granted by a copyright issued by the federal government.

[13] *Statement of Financial Accounting Standards, No. 2*, "Accounting for Research and Development Costs," Financial Accounting Standards Board, Stamford, 1974, par. 12.
[14] *Opinions of the Accounting Principles Board, No. 17*, "Intangible Assets," op. cit., par. 29.

LESS THEORY

MORE

REALITY

LEARN TO USE ACCOUNTING TO UNDERSTAND AND SUCCEED IN BUSINESS.

IN ITS SEVENTH DECADE OF PUTTING STUDENTS *FIRST.*

A*CCOUNTING, 18E,* IS FULL OF FEATURES TO HELP YOU UNDERSTAND HOW ACCOUNTING FUNCTIONS IN TODAY'S BUSINESS WORLD. FROM COVER TO COVER, YOU'LL FIND VALUABLE INFORMATION NO MATTER WHAT CAREER PATH YOU CHOOSE. TAKE A LOOK AT SOME OF THE MANY RELEVANT AND INTERESTING TOPICS THAT LIE AHEAD.

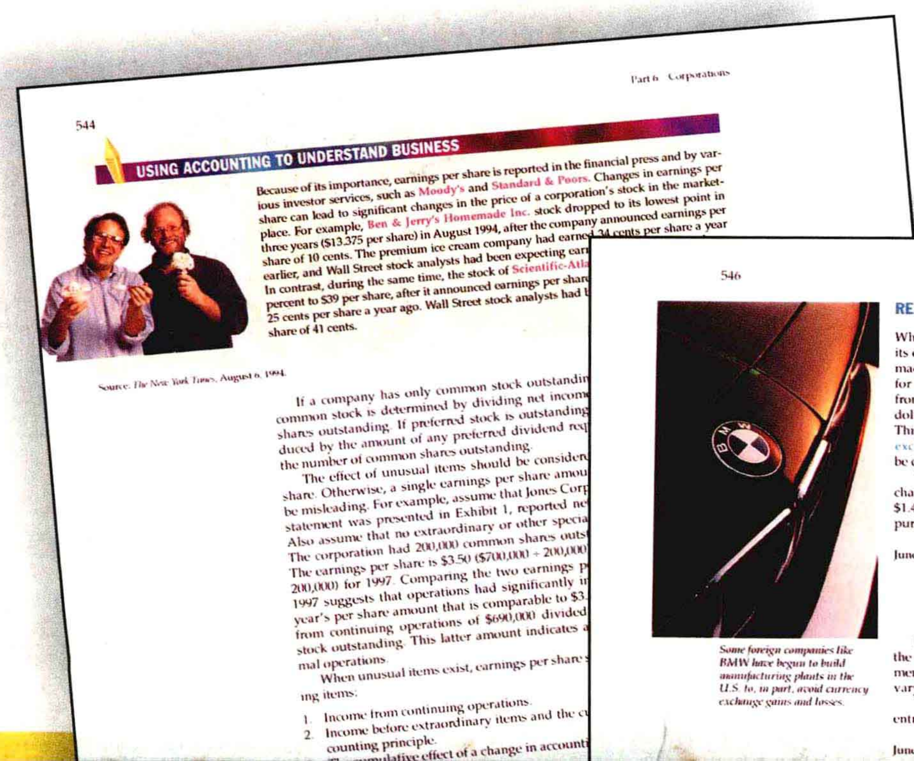
NEW!

"Using Accounting To Understand Business"

Accounting, 18e, puts accounting into real-world context. Each chapter includes one or more informative examples that clearly connect accounting to the business environment and show how, as a future business person, you will use accounting information. See pgs. 14, 91, 135, 388, 544, 679.

Real World Examples

BMW, JCPenney Co., General Electric, Coca-Cola, and numerous other business examples demonstrate how accounting is used in organizations and how it affects businesses worldwide. Integrated throughout the chapters and in the end-of-chapter cases and problems, these examples add concrete meaning to concepts and principles. See pgs. 9, 15, 44, 111, 144, 264, 365, 538.



Part 6 Corporations

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USING ACCOUNTING TO UNDERSTAND BUSINESS

Because of its importance, earnings per share is reported in the financial press and by various investor services, such as Moody's and Standard & Poors. Changes in earnings per share can lead to significant changes in the price of a corporation's stock in the marketplace. For example, Ben & Jerry's Homemade Inc. stock dropped to its lowest point in three years ($13.375 per share) in August 1994, after the company announced earnings per share of 10 cents. The premium ice cream company had earned 34 cents per share a year earlier, and Wall Street stock analysts had been expecting ear
In contrast, during the same time, the stock of Scientific-Atla
percent to $39 per share, after it announced earnings per shar
25 cents per share a year ago. Wall Street stock analysts had b
share of 41 cents.

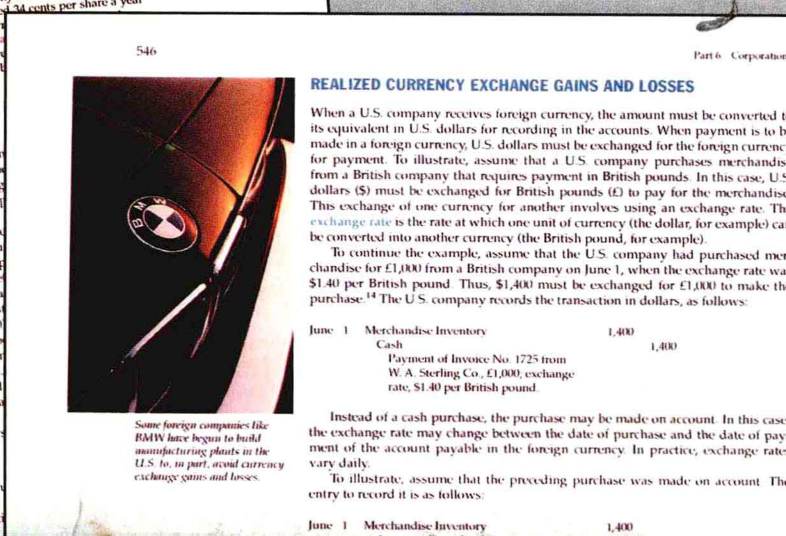
Source: *The New York Times*, August 6, 1994.

If a company has only common stock outstandin common stock is determined by dividing net incom shares outstanding. If preferred stock is outstanding duced by the amount of any preferred dividend req the number of common shares outstanding.

The effect of unusual items should be consider share. Otherwise, a single earnings per share amou be misleading. For example, assume that Jones Corp statement was presented in Exhibit 1, reported ne Also assume that no extraordinary or other specia The corporation had 200,000 common shares outs The earnings per share is $3.50 ($700,000 ÷ 200,000 The earnings per share is $3.50 ($700,000 ÷ 200,000) for 1997. Comparing the two earnings p 1997 suggests that operations had significantly i year's per share amount that is comparable to $3. from continuing operations of $690,000 divided stock outstanding. This latter amount indicates a mal operations.

When unusual items exist, earnings per share ing items:

1. Income from continuing operations.
2. Income before extraordinary items and the c counting principle.



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Part 6 Corporation

REALIZED CURRENCY EXCHANGE GAINS AND LOSSES

When a U.S. company receives foreign currency, the amount must be converted t its equivalent in U.S. dollars for recording in the accounts. When payment is to b made in a foreign currency, U.S. dollars must be exchanged for the foreign currenc for payment. To illustrate, assume that a U.S. company purchases merchandis from a British company that requires payment in British pounds. In this case, U.S dollars ($) must be exchanged for British pounds (£) to pay for the merchandis This exchange of one currency for another involves using an exchange rate. Th exchange rate is the rate at which one unit of currency (the dollar, for example) ca be converted into another currency (the British pound, for example).

To continue the example, assume that the U.S. company had purchased mer chandise for £1,000 from a British company on June 1, when the exchange rate wa $1.40 per British pound. Thus, $1,400 must be exchanged for £1,000 to make th purchase.[14] The U.S. company records the transaction in dollars, as follows:

June 1	Merchandise Inventory	1,400	
	Cash		1,400
	Payment of Invoice No. 1725 from W. A. Sterling Co., £1,000; exchange rate, $1.40 per British pound.		

Some foreign companies like BMW have begun to build manufacturing plants in the U.S. to, in part, avoid currency exchange gains and losses.

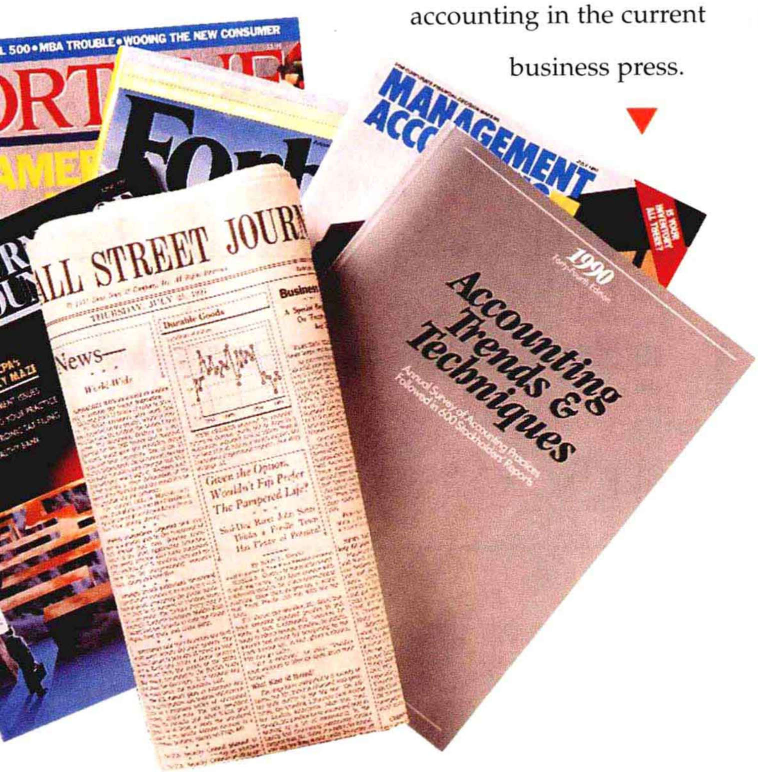
Instead of a cash purchase, the purchase may be made on account. In this case the exchange rate may change between the date of purchase and the date of pay ment of the account payable in the foreign currency. In practice, exchange rate vary daily.

To illustrate, assume that the preceding purchase was made on account. The entry to record it is as follows:

June 1	Merchandise Inventory	1,400

Excerpts From Popular Journals

What's "in the news" is in this text. Brief excerpts from *The Wall Street Journal*, *Forbes*, *Business Week*, and other periodicals generate stimulating discussions and help you see accounting in the current business press.

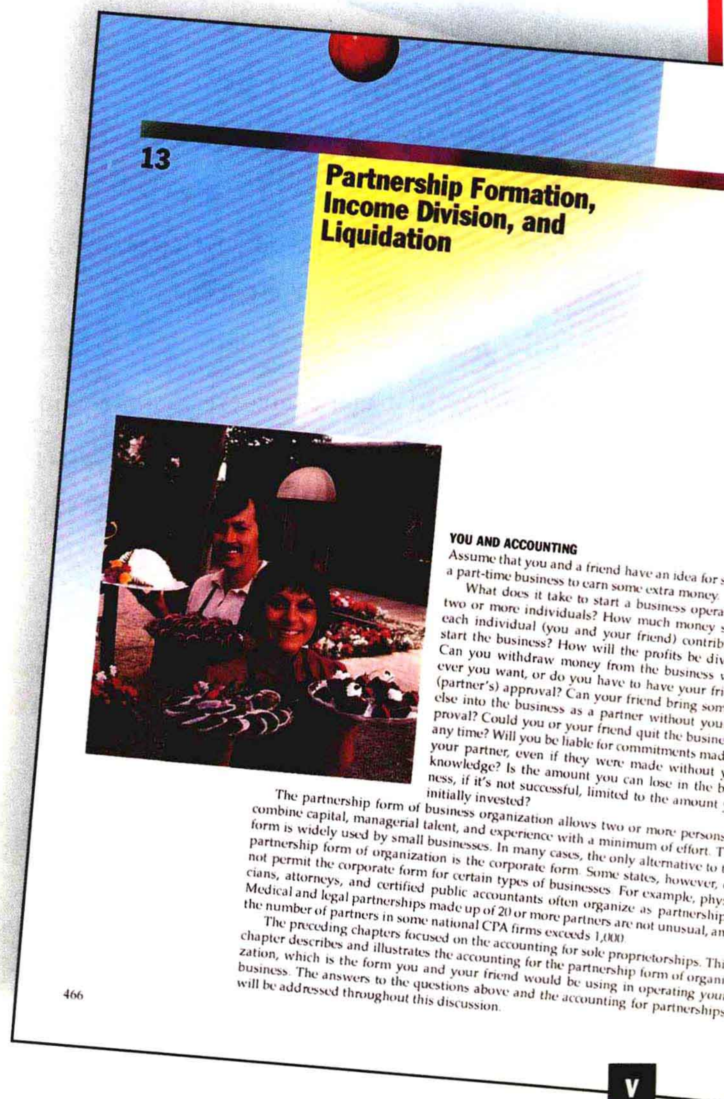


Take a look at just a few of the numerous companies cited throughout the text.

Anheuser-Busch
Apple Computer, Inc.
AT&T
BMW
British-Petroleum
Campbell Soup Company
Coca-Cola Enterprises Inc.
Delta Air Lines, Inc.
Fisher Price
Ford
Gillette
Goodyear
Harley-Davidson
Hershey Foods Corporation
Hewlett-Packard
La-Z-Boy
Mercedes-Benz
Microsoft Inc.
Orion Pictures
PepsiCo, Inc.
Pier 1 Imports, Inc.
Price Waterhouse
RCA
The Limited, Inc.
Time Incorporated
U-Haul
Walt Disney Co.
Zenith

"You And Accounting"

Found at the beginning of each chapter, these short "stories" relate your personal experience to the chapter's topic, making the material more enjoyable to read and easier to grasp. See pgs. 8, 42, 89, 124, 282, 572, 743.



"What's Wrong With This?"

These unique exercises will challenge you to

analyze and discover what is wrong with a financial statement, report, or management decision. You'll gain practical experience and critical-thinking skills that will assist you in the business world. See pgs. 31, 84, 148, 271, 523, 764.

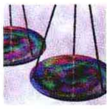
PUT ACCOUNTING INTO PRACTICE

IN ITS SEVENTH DECADE OF PUTTING STUDENTS *FIRST.*

EVEN MORE EXERCISES AND ACTIVITIES HELP YOU APPLY WHAT YOU'VE LEARNED FROM *ACCOUNTING, 18E.*

NEW! Cases

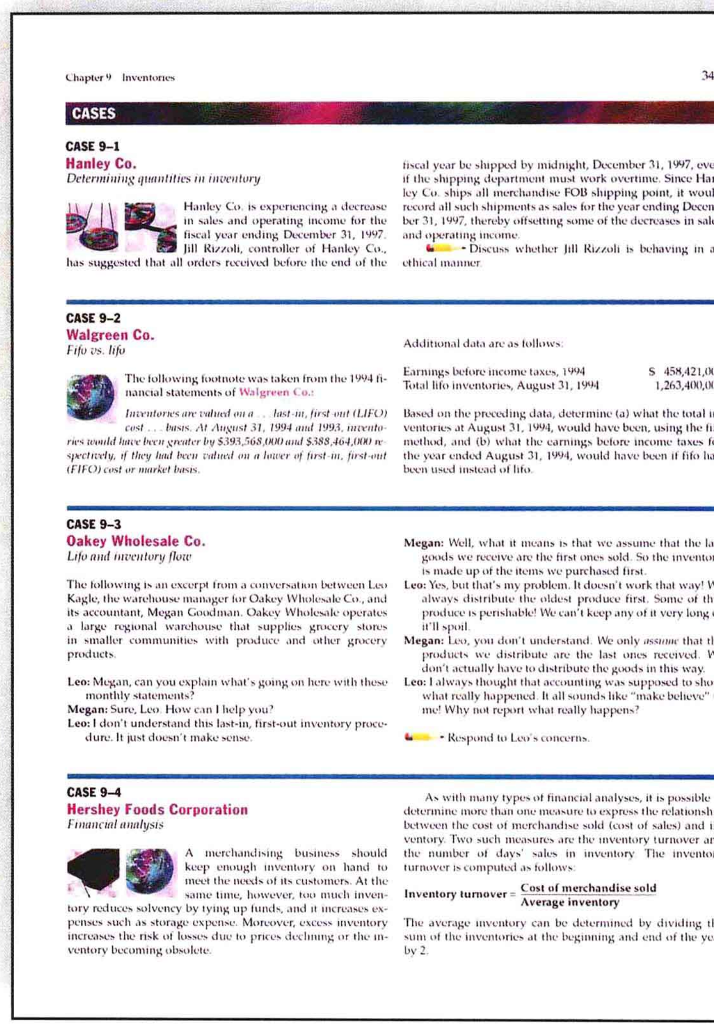
Cases in every chapter are designed to help you use accounting to make business decisions and develop your critical thinking. ▶



- Ethics cases stimulate discussion on ethical dilemmas in business. See pgs. 86, 202, 343.

- *NEW!* Financial analysis cases based on the annual report of Hershey Foods Corporation help you develop analytical skills. See pgs. 87, 311, 534.

- *NEW!* Managerial analysis cases require you to use analytical tools in a decision-making setting. See pgs. 772, 859, 894.



Chapter 9 Inventories 34

CASES

CASE 9–1
Hanley Co.
Determining quantities in inventory

Hanley Co. is experiencing a decrease in sales and operating income for the fiscal year ending December 31, 1997. Jill Rizzoli, controller of Hanley Co., has suggested that all orders received before the end of the fiscal year be shipped by midnight, December 31, 1997, eve if the shipping department must work overtime. Since Ha ley Co. ships all merchandise FOB shipping point, it woul record all such shipments as sales for the year ending Decen ber 31, 1997, thereby offsetting some of the decreases in sal and operating income.

• Discuss whether Jill Rizzoli is behaving in a ethical manner.

CASE 9–2
Walgreen Co.
Fifo vs. lifo

The following footnote was taken from the 1994 financial statements of Walgreen Co.:

Inventories are valued on a . . . last-in, first-out (LIFO) cost . . . basis. At August 31, 1994 and 1993, inventories would have been greater by $393,568,000 and $388,464,000 respectively, if they had been valued on a lower of first-in, first-out (FIFO) cost or market basis.

Additional data are as follows:

Earnings before income taxes, 1994	$ 458,421,0
Total lifo inventories, August 31, 1994	1,263,400,0

Based on the preceding data, determine (a) what the total i ventories at August 31, 1994, would have been, using the fi method, and (b) what the earnings before income taxes f the year ended August 31, 1994, would have been if fifo ha been used instead of lifo.

CASE 9–3
Oakey Wholesale Co.
Lifo and inventory flow

The following is an excerpt from a conversation between Leo Kagle, the warehouse manager for Oakey Wholesale Co., and its accountant, Megan Goodman. Oakey Wholesale operates a large regional warehouse that supplies grocery stores in smaller communities with produce and other grocery products.

Leo: Megan, can you explain what's going on here with these monthly statements?
Megan: Sure, Leo. How can I help you?
Leo: I don't understand this last-in, first-out inventory procedure. It just doesn't make sense.
Megan: Well, what it means is that we assume that the la goods we receive are the first ones sold. So the invento is made up of the items we purchased first.
Leo: Yes, but that's my problem. It doesn't work that way! W always distribute the oldest produce first. Some of th produce is perishable! We can't keep any of it very long it'll spoil.
Megan: Leo, you don't understand. We only *assume* that th products we distribute are the last ones received. W don't actually have to distribute the goods in this way.
Leo: I always thought that accounting was supposed to sho what really happened. It all sounds like "make believe" me! Why not report what really happens?

• Respond to Leo's concerns.

CASE 9–4
Hershey Foods Corporation
Financial analysis

A merchandising business should keep enough inventory on hand to meet the needs of its customers. At the same time, however, too much inventory reduces solvency by tying up funds, and it increases expenses such as storage expense. Moreover, excess inventory increases the risk of losses due to prices declining or the inventory becoming obsolete.

As with many types of financial analyses, it is possible determine more than one measure to express the relationsh between the cost of merchandise sold (cost of sales) and i ventory. Two such measures are the inventory turnover a the number of days' sales in inventory. The invento turnover is computed as follows:

$$\text{Inventory turnover} = \frac{\text{Cost of merchandise sold}}{\text{Average inventory}}$$

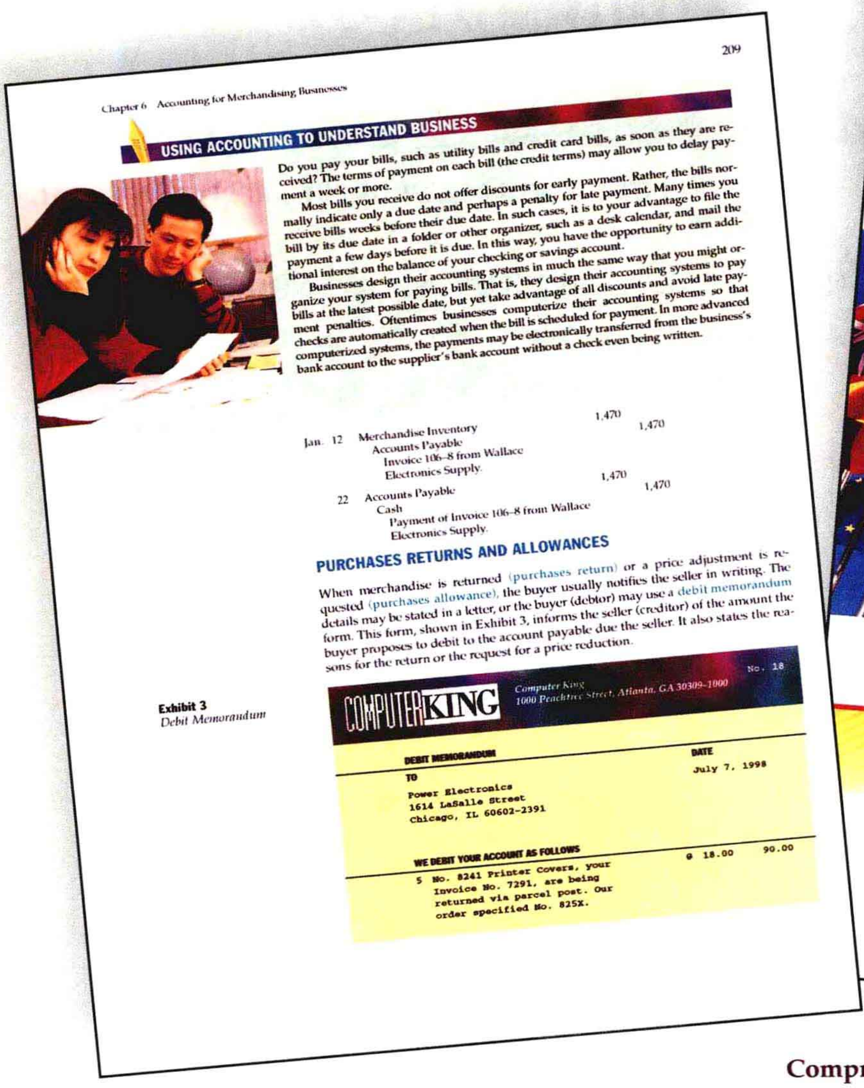
The average inventory can be determined by dividing t sum of the inventories at the beginning and end of the ye by 2.

NEW! Continuing Problem in Chs. 1-4

Here's a great opportunity to practice what you're learning. As you study each step of the accounting cycle, you can follow a single company, Music A La Mode, from its transactions to the effect of those transactions on its financial statements. See pgs. 38, 85, 120, 157.

Communication Items ▲

Communication items at the end of chapters help you develop essential communication skills, key to your business success. See pgs. 112, 121, 341.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Chapter 6 Accounting for Merchandising Businesses

USING ACCOUNTING TO UNDERSTAND BUSINESS

Do you pay your bills, such as utility bills and credit card bills, as soon as they are received? The terms of payment on each bill (the credit terms) may allow you to delay payment a week or more.

Most bills you receive do not offer discounts for early payment. Rather, the bills normally indicate only a due date and perhaps a penalty for late payment. Many times you receive bills weeks before their due date. In such cases, it is to your advantage to file the bill by its due date in a folder or other organizer, such as a desk calendar, and mail the payment a few days before it is due. In this way, you have the opportunity to earn additional interest on the balance of your checking or savings account.

Businesses design their accounting systems in much the same way that you might organize your system for paying bills. That is, they design their accounting systems to pay bills at the latest possible date, but yet take advantage of all discounts and avoid late payment penalties. Oftentimes businesses computerize their accounting systems so that checks are automatically created when the bill is scheduled for payment. In more advanced computerized systems, the payments may be electronically transferred from the business's bank account to the supplier's bank account without a check even being written.

Jan.	12	Merchandise Inventory	1,470	
		Accounts Payable		1,470
		Invoice 106-8 from Wallace Electronics Supply.		
	22	Accounts Payable	1,470	
		Cash		1,470
		Payment of Invoice 106-8 from Wallace Electronics Supply.		

PURCHASES RETURNS AND ALLOWANCES

When merchandise is returned (purchases return) or a price adjustment is requested (purchases allowance), the buyer usually notifies the seller in writing. The details may be stated in a letter, or the buyer (debtor) may use a debit memorandum form. This form, shown in Exhibit 3, informs the seller (creditor) of the amount the buyer proposes to debit to the account payable due the seller. It also states the reasons for the return or the request for a price reduction.

Exhibit 3
Debit Memorandum

COMPUTER KING
Computer King
1000 Peachtree Street, Atlanta, GA 30309-1000
No. 18

DEBIT MEMORANDUM
TO
Power Electronics
1614 LaSalle Street
Chicago, IL 60602-2391

DATE
July 7, 1998

WE DEBIT YOUR ACCOUNT AS FOLLOWS
5 No. 8241 Printer Covers, your Invoice No. 7291, are being returned via parcel post. Our order specified No. 825X. @ 18.00 90.00


Chapter 12 Concepts and Principles

The Internal Revenue Service (IRS) oversees the laws a[t] preparing federal tax returns. These laws and regulations determ reported for federal income tax purposes. These rules sometimes erally accepted accounting principles for preparing financial state

Other regulatory agencies exercise a major influence over the a ples of the industries under their jurisdiction. For example, the Currency and the Federal Deposit Insurance Corporation greatly ally accepted accounting principles used by banks. In rare situatior also enact special laws that require firms to use specific accounting

International Accounting Standards

The United States economy, as well as the economies of other nati the world, is becoming more global in nature. For example, mor vestors are investing in companies outside the United States. Likew other financial institutions frequently loan monies on an internatio many companies are involved in international transactions with suppliers.

Currently, accounting concepts and principles differ greatly am These differences exist because of differences in cultures, legal systems tems, economies, and the processes by which concepts and principles a

As a result of the increasing global business activity, attention has on developing uniform international accounting standards. The prim volved in this effort is the International Accounting Standards Comm The IASC was formed in 1973 by the leading professional accounting b nations: Australia, Canada, France, Germany, Japan, Mexico, the Neth United Kingdom, and Ireland.[3] At the present time, over 101 accounti tions from 77 different countries make up the IASC.

The IASC functions very similarly to the FASB, which we descri For example, after studying an issue, the IASC prepares a preliminar new standard, which is exposed among its members for comments. Aft the proposed standard for any comments, the IASC votes for or against as an International Accounting Standard. Currently, over thirty Stand been issued.

The IASC has no enforcement powers. Instead, the members pledge t best efforts to advocate the adoption of the Standards in their own countri sult, accounting concepts and principles still differ significantly among For example, in the United States and Germany, research and developm are treated as expenses when incurred. In Japan and the United Kingdom, treated as assets when incurred and then amortized as expenses in future Over time, however, as the economies throughout the world become m more interdependent, the trend towards more uniformity will continue.

The need for developing uniform international accounting standards arose from the increase in global business activities in nations throughout the world.

Statements of Financial Accounting Concepts

Objective 2
Describe the Statements of Financial Accounting Concepts.

As we mentioned in the preceding section, the FASB's Statements of Financi counting Concepts are the framework for financial accounting. Four of these ments are relevant to our discussions of accounting for business and are su rized in Exhibit 1.[4]

[3] The United States was represented by the AICPA.
[4] Of the six Statements that have been issued to date, one has been superseded and the other focuses counting for nonbusiness organizations.

Computer King

Computer King, a company introduced in Ch. 1 and used in Chs. 2-7, helps you tie together elements of the accounting cycle. See pgs. 44, 93, 212.

"What Do You Think?" Exercises

Found in the end-of-chapter material, these exercises require analyses beyond the material included in the text. Real companies like Ford and Delta are presented. See pgs. 86, 121.

Comprehensive Problems

Found at the end of Chs. 4, 6, 11, and 16, these learning applications integrate and summarize concepts and principles of several chapters to test your comprehension and help you prepare for and pass your midterm and final exams. You may complete these problems manually or use the available Solutions Software. See pgs. 158, 244, 419.

The Basics

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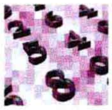

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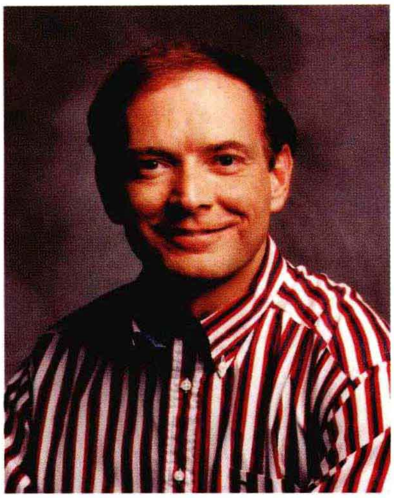

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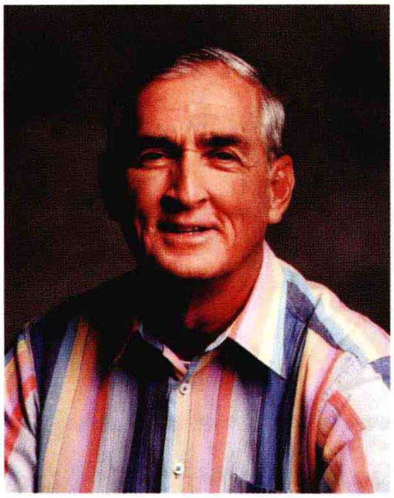
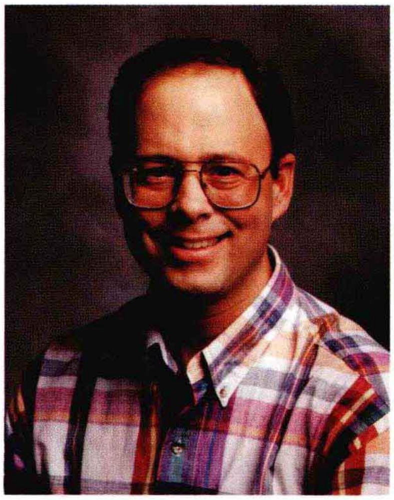
Dr. Carl S. Warren is the Arthur Andersen & Co. Alumni Professor of Accounting at the J.M. Tull School of Accounting at the University of Georgia, Athens. Professor Warren received his Ph.D. from Michigan State University in 1973. Dr. Warren's experience in listening to users of his texts sharpens his keen focus on helping students learn. When he is not teaching classes or writing textbooks, Dr. Warren enjoys golf, racquetball, and fishing.



PHILIP E. FESS

Dr. Philip E. Fess is the Arthur Andersen & Co. Alumni Professor of Accountancy Emeritus at the University of Illinois, Champaign-Urbana. He received his Ph.D. from the University of Illinois. Dr. Fess has been involved in writing textbooks for over twenty-five years, and his knowledge of how to make texts user-friendly is reflected on the pages of this edition. Dr. Fess plays golf and tennis, and he has represented the United States in international tennis competition.



JAMES M. REEVE

Dr. James M. Reeve is Professor of Accounting at the University of Tennessee, Knoxville. He received his Ph.D. from Oklahoma State University in 1980. Dr. Reeve is founder of the Cost Management Institute and a member of the Institute for Productivity Through Quality faculty at the University of Tennessee. In addition to his teaching experience, Dr. Reeve brings to this text a wealth of experience consulting on managerial accounting issues with numerous companies, including Procter and Gamble, AMOCO, Rockwell International, Harris Corporation, and Freddie Mac. Dr. Reeve's interests outside the classroom and the business world include golf, skiing, reading, and travel.

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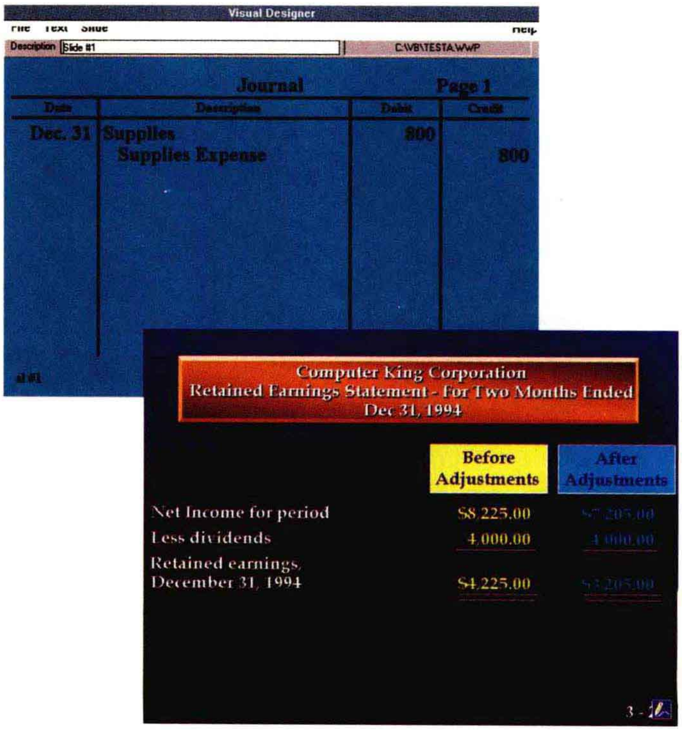

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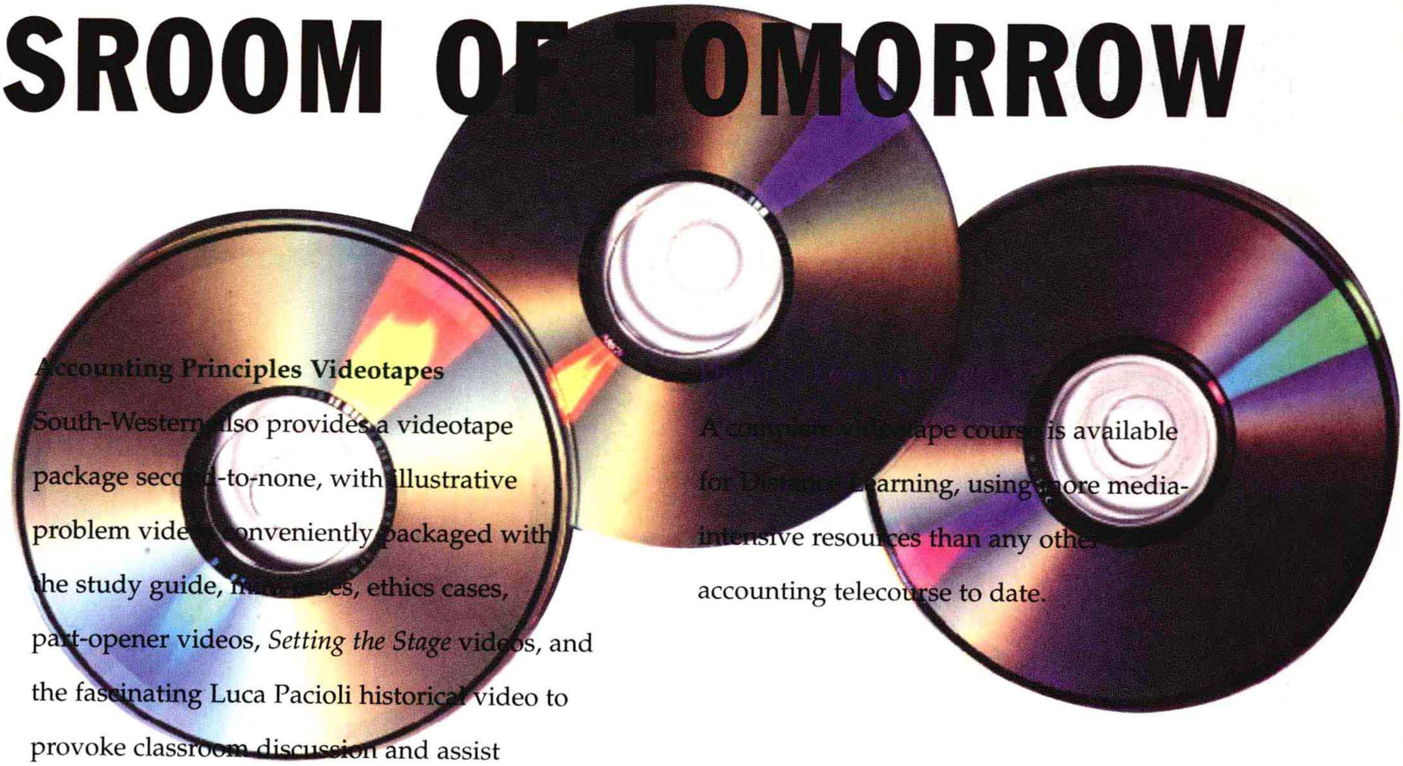

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Summary of Contents and Changes

The most significant changes made in the 18th Edition of Accounting were reducing the number of chapters from 28 to 26. This reduction was accomplished by condensing three corporate equity chapters into two, and integrating much of the financial statement analysis material into cases at the end of the financial chapters. Below you'll find a chapter-by-chapter account of the changes made in the 18th Edition of Accounting. You'll see how Warren/Fess/Reeve have streamlined coverage and expanded other areas for a greater understanding of accounting principles. You'll also find a continued adherence to AECC recommendations that help your students excel in their learning and help you emphasize important aspects in your classroom. Who ever said change isn't good?

Chapter 1
Introduction to Accounting Concepts and Practice 8

Financial and managerial accounting are emphasized in the discussion of specialized accounting fields. The format of the statement of owner's equity was revised to show a beginning balance of zero for a start-up business.

Chapter 2
Analyzing Transactions 42

Chapter 3
The Matching Concept and the Adjusting Process 89

A new exhibit was added to illustrate the difference between deferrals and accruals.

Chapter 4
Completing the Accounting Cycle 124

Chapter 5
Accounting Systems, Internal Control, and Special Journals 162

The section on internal control framework was revised to follow the recommendations of the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. The special journals section of this chapter was recast in the context of a service business, rather than a merchandising business. By presenting simple revenue, purchases, cash payments, and cash receipts journals, the emphasis on special journals is reduced. A new exhibit illustrating a computerized accounts receivable system was added.

Chapter 6
Accounting for Merchandising Businesses 205
Merchandising is covered in one chapter, rather than two. Purchases are discussed prior to sales. The perpetual inventory system is emphasized, which simplifies the recording of purchases and sales transactions. Purchases are recorded at their net amount. The work sheet and closing entries are covered in a chapter appendix. The periodic inventory system is covered in an end-of-text appendix.

Chapter 7
Cash 250
The discussion of internal controls for cash was moved to the beginning of the chapter. The voucher register and the check register are no longer illustrated.

Chapter 8
Receivables and Temporary Investments 282
The discussion of accounts receivable and uncollectible receivables was moved to the beginning of the chapter. The discussion of temporary investments was updated to reflect FASB 115.

Chapter 9
Inventories 313
The discussion of inventory costing under a perpetual system is presented prior to the discussion of inventory costing under a periodic system.

Chapter 10
Plant Assets and Intangible Assets 346
A new exhibit summarizing the costs of acquiring plant assets was added. The sum-of-the-years-digits method of depreciation is covered in a chapter appendix.

Chapter 11
Payroll, Notes Payable, and Other Current Liabilities 386
The illustration of income-sharing bonuses was eliminated. Form 941 is now a transparency master in the Instructor's Resource package. The pension discussion was revised to present pensions as either defined contribution plans or defined benefit plans.

Chapter 12
Concepts and Principles 426
Sections on international accounting standards and the role of auditing of financial statements were added.

Chapter 13
Partnership Formation, Income Division, and Liquidation 466

Chapter 14
Corporations: Organization and Equity Rights 498
A section on forming a corporation, including the discussion of organization costs, was added at the beginning of the chapter. The discussion of stock subscriptions was eliminated. The discussions of stock splits, cash dividends, stock dividends, appropriations of retained earnings, and reporting retained earnings were moved from former Chapter 16. The discussion of the statement of stockholders' equity was moved from former Chapter 18.

Chapter 15
Corporate Earnings, International Transactions, and Investments in Stocks 537
The discussions of corporate income taxes, unusual items that affect the income statement and retained earnings statement, and earnings per share were moved from former Chapter 16. The discussion of equity per share was retained from former Chapter 15. The coverage of consolidated financial statements was significantly reduced.

Chapter 16
Bonds Payable and Investments in Bonds 572
Amortization of premium and discount by the interest method was moved to a chapter appendix. The coverage of bond sinking funds was significantly reduced.

Chapter 17
Statement of Cash Flows 605

Chapter 18
Managerial Accounting Concepts and Principles 662
The discussion of the characteristics of managerial accounting reports was integrated into the chapter. The section on cost terminology was eliminated and the terms defined as they are introduced in subsequent chapters. A hypothetical printing company is used in this chapter to introduce managerial accounting. The income statement illustration was revised to reflect a perpetual inventory system. The appendix on traditional versus JIT systems was incorporated into new Chapter 20. A new end-of-text appendix on periodic inventory systems for manufacturing businesses was added.

Chapter 19
Job Order Cost Systems 699
The hypothetical printing company introduced in Chapter 18 is used to illustrate a job order costing system. A section on selecting an activity base for allocating factory overhead was added. A section on using job order costing in decision making was added. The appendix on activity-based costing at the end of former Chapter 23 was condensed and moved to the end of new Chapter 19.

Chapter 20
Process Cost Systems 743

A new exhibit comparing job order and process cost systems was added. A new exhibit illustrating the physical flows for a process manufacturer was added. The discussion of equivalent units was revised to emphasize a step-by-step calculation. The cost of production report format was revised. A section on using the cost of production report for decision making was added. The coverage of joint products and by-products was eliminated. The illustration of the average cost method was eliminated.

Chapter 21
Cost Behavior and Cost-Volume-Profit Analysis 776

Chapter 22
Budgeting 820

The discussion of standard costs was moved to new Chapter 23. A section on human behavior and budgeting was added. The terms "static budget" and "flexible budget" are introduced prior to the discussion of the master budget. The illustration of the cash budget was expanded.

Chapter 23
Performance Evaluation Using Variances from Standard Costs 862

This is a new chapter on standard costs that expands on the discussion in former Chapter 25. A new section on nonfinancial performance measures was added at the end of the chapter.

Chapter 24
Performance Evaluation for Decentralized Operations 897

The discussion of responsibility accounting for profit centers was revised to focus on operating income, service department charges, and controllable operating income. The discussion of investment centers was revised to use terminology consistent with that of profit centers.

Chapter 25
Differential Analysis and Product Pricing 934

The discussion of the economic theory of product pricing was eliminated. A new section on profitability and pricing under production bottlenecks was added.

Chapter 26
Capital Investment Analysis 967

A brief discussion of present value concepts was added.