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# FINANCIAL ACCOUNTING

*Information for Business Decisions*

*Seventh Edition*

**Kermit D. Larson**

*University of Texas–Austin*



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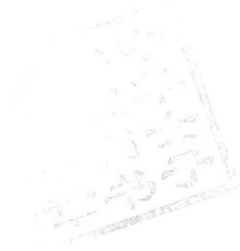
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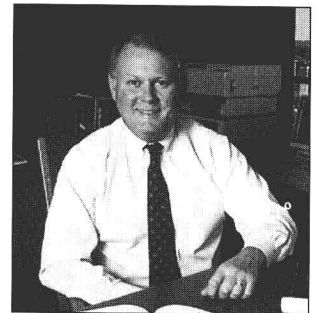


# About the Author

**Kermit D. Larson** is the Arthur Andersen & Co. Alumni Professor of Accounting Emeritus at The University of Texas at Austin. He served as chairman of the U.T. Department of Accounting and was Visiting Associate Professor at Tulane University. His scholarly articles have been published in a variety of journals, including *The Accounting Review*, *Journal of Accountancy*, and *Abacus*. He is the author of several books, including *Fundamental Accounting Principles* and *Fundamentals of Financial and Managerial Accounting*, both published by Richard D. Irwin, Inc.

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Professor Larson's other activities have included serving on the Accounting Accreditation Committee and on the Accounting Standards Committee of the AACSB. He was a member of the Constitutional Drafting Committee of the Federation of Schools of Accountancy and a member of the Commission on Professional Accounting Education. He has been an expert witness on cases involving mergers, antitrust litigation, consolidation criteria, franchise taxes, and expropriation of assets by foreign governments. Professor Larson served on the Board of Directors and Executive Committee of Tekcon, Inc., and on the National Accountant Advisory Board of Safe-Guard Business Systems. In his leisure time, he enjoys skiing and is an avid sailor and golfer.



# Preface

*Essentials of Financial Accounting* introduces students to accounting information, how it is developed, and how it is used to make decisions about corporations and other economic organizations. The text provides an efficient, clear presentation that is student friendly. It supports a variety of teaching approaches and now is very supportive of those who want to emphasize decision making, critical thinking, and communication skills.

This edition incorporates several major changes. Most notable are the following:

1. A new Chapter 1 explains the relevance of accounting to business decisions and to the future careers of business students. The chapter describes the role of accounting in the context of other organizational functions such as finance, human resources, research and development, production, marketing, and executive management. It also explains the work accountants do, their certifications, and the pervasive importance of ethics in accounting.
2. Corporations are now used in the illustrations and examples throughout the early chapters of the book. Students will find the presentation easy to understand and it is responsive to the requests of many adopters.
3. The text consistently places the student reader in the role of an information user. Thus, selected procedural matters such as the work sheet have been minimized or removed from the body of specific chapters. (Appropriate work sheet coverage is provided in an appendix.)
4. The chapter on merchandising operations has been completely rewritten to focus on perpetual inventory systems. This change reflects the increasing use of perpetual systems. It also shows students more clearly how accounting deals with both the cost and revenue aspects of sales transactions.
5. Chapter 9 includes a new explanation of periodic inventories with a transaction-by-transaction comparison to perpetual systems.
6. Chapter 13 contains new material that describes the differences between “C” corporations, “S” corporations, limited liability companies, partnerships, proprietorships, limited partnerships, and limited liability partnerships.
7. New Progress Check questions are spaced appropriately throughout each chapter with answers provided at the end of the chapter. These review questions get students to stop momentarily and reflect on whether they should spend more time studying a given section of the text before moving on.
8. A new Quick Study category of five-minute exercises is provided after each chapter. Instructors confirm an increasing reliance on shorter problem material for use



**MAJOR CHANGES  
IN THE TEXT**



- as in-class illustrations as well as homework assignments. Undoubtedly, the prospect of solving problems in a short time and the rapid feedback of having done so successfully are motivating factors that lead students to extend their study efforts. We provide at least one Quick Study exercise for each learning objective.
9. A selected number of problems and alternate problems now have requirements that are separated into a *Preparation Component* and an *Analysis Component*. The analysis component typically requires students to consider the financial statement effects of alternative situations and present their analysis in the form of an essay.
  10. Each chapter includes a new category of assignments under the heading Critical Thinking: Essays, Problems, and Cases. These include:
    - Analytical Essays.
    - Business Communication Cases.
    - Financial Reporting Problems.
    - Financial Statement Analysis Cases.
    - Managerial Decision Cases.
    - Managerial Analysis Problems.
    - Ethical Issues Essays.
  11. A new Concept Tester question, designed as a crossword puzzle, is provided at the end of many chapters. These puzzles motivate students to learn the meaning of the glossary terms and are supported by the working papers.
  12. A new opening scenario for each chapter draws on the facts of a real company to identify some of the analysis and decision questions addressed in the chapter. Later in the chapter, one or more references show how the ideas being explained at that point apply to the company that was described in the chapter opening.
  13. The entire text reflects a dramatically expanded emphasis on real-world examples that have been carefully selected and integrated into the discussion. Most of these references are accompanied by photos that draw attention to the nature of the business or the specific company used as the example.
  14. The book has been carefully redesigned to generate student interest and yet provide a basis for pricing the text in a manner that is responsive to increasing student concerns with the high cost of textbooks.



## ADDITIONAL NOTEWORTHY FEATURES

Several features of this text warrant special consideration in your adoption decision. These include the following:

1. In every chapter, the book is now written so that students learn and practice how to use accounting information in making decisions. This shift in focus has been accomplished while maintaining the appropriate goal of showing students how the information is developed. Too often, the importance of this understanding to managers and other nonaccountant decision makers has been overlooked or dismissed. By gaining an introductory understanding of the processes by which accounting information and reports are generated, future decision makers learn the limits of accounting information. They learn to avoid overstating or misinterpreting the information. Thus, they are less apt to confuse such things as book values and market values, accumulated depreciation and spendable funds, or net income and cash inflows.
2. An increasing number of companies routinely convert their receivables into cash without waiting to receive customer payments. In dealing with this modern business practice, this text replaces the traditional discussion of discounting notes receivable with a more general examination of the various ways businesses convert receivables into cash.

3. Streamlined discussions provide clear treatment of topics such as lower of cost or market, retail inventory methods, accelerated depreciation, MACRS, and leases.
4. The text has a uniquely balanced set of asset chapters. In particular, the coverage of Chapter 11 is notable. It completes the asset coverage by discussing natural resources, intangible assets, and long-term investments. The long-term investments portion naturally concludes with a discussion of investments in international operations.
5. Instructors and reviewers have uniformly called for a new commitment to show students the relevance of accounting information and to teach them how to use the information. The text responds to this in a variety of ways. Most obviously, each chapter includes a section under the general heading Using the Information. These sections show students how to calculate, interpret, and use information. In addition, a large number of the assignments require students to analyze and/or interpret the financial statement consequences of various transactions or events.
6. A complete set of Alternate Problems is published in a separate booklet that is available in quantity to adopters.
7. A variety of assignments in each chapter introduce students to the complete financial statements with footnotes and related disclosures for two companies in different industries, Southwest Airlines Co. and Lands' End, Inc.
8. Mark-to-market accounting is a major break from the tradition of historical cost accounting. As a result, the text reflects a special effort to clearly explain it in the contexts of short-term investments, long-term investments, and alternative valuation models.

A full set of supplements accompany *Essentials of Financial Accounting*. Additional information about each of them is available from the publisher's representatives. The supplements include:

- *Solutions Manual.*
- *Working Papers.*
- *Study Guide.*
- *Practice Sets.*
- *Test Bank.*
- *Computest.*
- *Teletest.*
- *GLAS (General Ledger Applications Software.).*
- *SPATS (Spreadsheet Applications Template Software).*
- *Tutorial Software.*
- *Solutions Transparencies.*
- *Teaching Transparencies.*
- *Video Library.*
- *Lecture Review Videos.*



**SUPPLEMENTS  
THAT SUPPORT  
THE TEXT**



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**Kermit D. Larson**

*Essentials of*

# **FINANCIAL ACCOUNTING**

*Information for Business Decisions*

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