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A Survey of *Accounting*

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Survey of Accounting

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Preface

All professionals and business managers require a basic knowledge of accounting. During the past several years, many colleges and universities have attempted to provide nonbusiness majors with an introductory, one-semester accounting course, typically titled Survey of Accounting, that satisfies these students' need to understand the accounting process. However, the supply of texts available for these courses is limited, and most of the available texts are simply watered-down versions of previously published accounting principles texts. Because these texts are not specifically suited to the needs of nonbusiness majors, students often rapidly lose interest in the subject matter. This text is specifically designed to meet the needs of nonbusiness majors.

FOCUS

Because many of the students enrolled in Survey of Accounting courses are or will be self-employed or work in small, unincorporated businesses, this text, in the early chapters, emphasizes accounting for sole proprietorships. Later, it introduces accounting for corporations and partnerships, and finally, it discusses some of the managerial accounting topics most useful to the individuals served by this course.

The text is divided into four sections. Section I introduces the accounting cycle as well as accounting for service and merchandising companies. Section II presents the reporting and measurement issues associated with assets, liabilities, and equity. Section III reviews special reporting issues including financial statement analysis, international accounting, accounting for changing prices, and income taxation. Finally, Section IV presents managerial accounting and introduces such topics as planning and controlling, cost behavior analysis, product costing, budgeting, and standard costing.

FEATURES

We have supplied this text with a wealth of pedagogical features to facilitate student learning and retention.

- **Learning Objectives** are outlines at the beginning of the chapter. Later, each learning objective is highlighted in the margin at the point it is discussed in the chapter.
- The **Practical Insight**, a relevant excerpt from the financial press, piques student interest in the topic at hand.
- **Key Terms** are supplied at the end of each chapter for review purposes.
- A **Demonstration Problem** summarizes the major topics covered in each chapter and illustrates key concepts.
- **Questions** summarize the chapter contents: students who thoroughly understand the issues addressed in the chapter should be able to answer each and every one.
- **Exercises** review each of the major topics in the chapter. Since each exercise covers *only* one topic, the instructor can use the exercises to illustrate chapter topics without confounding the presentation with multiple issues.
- **Problems** review the more complex issues covered in the chapter, frequently addressing more than one issue in a single problem.
- A **Comprehensive Problem** functions as a capstone for the problem material in each chapter. This problem deals with several chapter topics simultaneously, showing the interaction of various concepts.
- The **Decision Case** centers on an issue that may be encountered by Survey students in their future careers.

In addition to these features, we offer a **Glossary** at the end of the text. With it, students are enabled to easily access definitions of terms which were defined in earlier chapters. By eliminating this sort of endless page turning, we hope students will spend their extra time studying! Once the course is over, this feature turns the book into a useful reference tool.

Finally, we have incorporated a feature never before offered in a Survey of Accounting text: **Review Cases** *specifically* geared to some of the fields your Survey students most commonly enter.

Legal	Review Case 1, summarizing Chapters 1–4, illustrates the accounting cycle for an attorney. The students are asked to assist in developing a suitable accounting systems for the practice.
Hotel Management	Review Case 2, summarizing Chapters 5–8, involves some reporting and measurement issues for a hotel and casino under restoration.

Engineering	Review Case 3, summarizing Chapters 9–12, introduces students to an engineering partnership about to decide whether they should accept the terms of a new project.
Health Administration	Review Case 4, summarizing Chapters 13–18, calls for managerial accounting knowledge to assist a nonprofit health safety organization in their search for appropriate equipment.

We have developed all of these pedagogical features with the needs of Survey of Accounting students in mind. Further, we have strived to create an easy-to-teach format to assist both instructors as well as students in the educational process.

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This project would not have been possible without the help and cooperation of many individuals. We are especially indebted to the following reviewers who provided many helpful comments and suggestions:

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Richard G. Schroeder
Charles P. Zlatkovich

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Review Cases

▣ PART I

Review Case 1

Chapters 1–4

Alex Lindoski, Attorney at Law

Students are required to follow a legal practice through an accounting cycle and to develop an appropriate accounting system.

▣ PART II

Review Case 2

Chapters 5–8

The Del Norte Hotel and Casino

Students evaluate the restoration of a historical hotel and casino and consider its investment potential.

▣ PART III

Review Case 3

Chapters 9–12

Hudson and Pensock Engineers

Students advise an engineering partnership about the viability of a new project with unusual terms of payment.

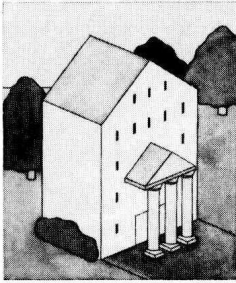
▣ PART IV

Review Case 4

Chapters 13–18

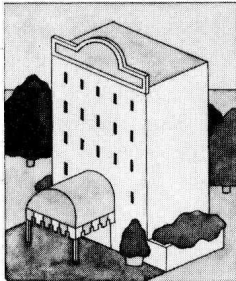
Central States Regional Health Laboratories

Students analyze the merits of different types of equipment for a nonprofit water testing laboratory.

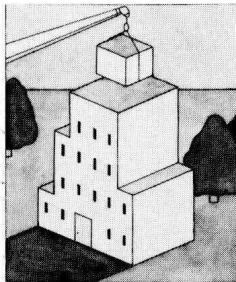


PART I

The Accounting Cycle



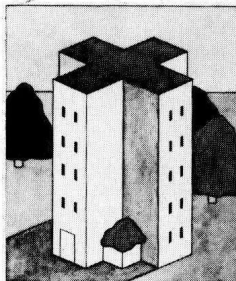
Chapter 1 **Fundamental Accounting Concepts**



Chapter 2 **Processing Accounting Information**

Chapter 3 **Completion of the Accounting Cycle**

Chapter 4 **Accounting for Merchandising Operations**



1

Fundamental Accounting Concepts

This chapter begins by defining the function of accounting. Next, it presents some fundamental concepts and describes the three forms of business organizations. It then introduces the accounting equation and illustrates the impact of business transactions on the accounting equation and on three financial statements. Finally, it discusses the authoritative bodies affecting accounting practice and the role of the accountant in the various sectors of accounting practice.

■ *At the conclusion of this chapter you should be able to:*

1. Define the function of accounting.
2. Describe three fundamental accounting concepts: business entity, monetary unit, and historical cost.
3. Delineate the three forms of business organization.
4. Explain the accounting equation and its elements.
5. Describe the impact of business transactions on the accounting equation.
6. Identify the functions of three major financial statements.
7. Identify the authoritative bodies influencing accounting practice.
8. Describe the role of accountants employed in the three sectors of the accounting profession.

THE FUNCTION OF ACCOUNTING

1. Define the function of accounting.

Accounting provides information about the economic activities of a business that is useful in making decisions. The economic activities of a business include acquiring resources, selling products and services, and paying wages to employees. All information about the economic activities of businesses must be quantified, processed, and communicated by the accounting system in order to be useful. Consequently, accounting can be viewed as a service activity that provides information to decision makers. This process is termed the *accounting decision-making information system* and is illustrated in Exhibit 1-1 below.

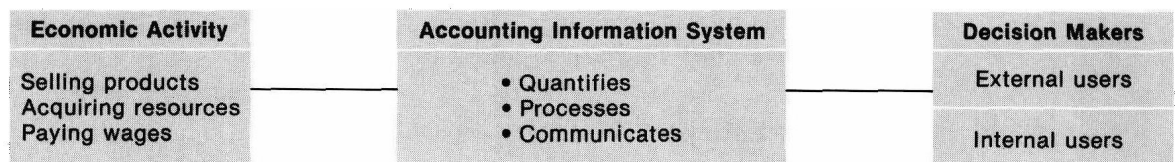
As Exhibit 1-1 illustrates, accounting links decision makers with the economic activities of a business. This text is designed to assist future users of accounting information to (1) understand the quantification, processing, and communication of accounting information and (2) make sound business decisions.

The decision makers or users of accounting information are classified as external users and internal users. *External users* include current or potential investors (owners and creditors), employees, taxing authorities, financial analysts, brokers, and labor unions. *Internal users* are the managers who work within the business.

Investors and creditors are the external users with the closest relationship to the business. They make three basic decisions based on accounting information:

- Buy* A potential investor decides to invest in the business.
A creditor decides to extend credit to a business.
- Hold* A current investor decides to retain an investment in the business.
A creditor decides to continue a credit relationship with the business.
- Sell* A current investor decides to dispose of an investment in the business.

EXHIBIT 1-1 Accounting Decision-Making Information System



A creditor decides to discontinue a credit relationship with the business.


Since these decisions are constantly being reviewed by external users, the timely quantification, processing, and communication of information by the accounting decision-making information system is essential.

In making decisions, external users generally rely on the financial statements published by the business. These financial statements (discussed later in the chapter) are the end product of the quantification, processing, and communication process.

Internal users are responsible for the daily planning and control of operations. In performing their duties, internal users may require, in addition to the published financial statements, various other reports to be prepared from the company's accounting decision-making information system. Later in the text we will discuss some of these reports and the information they provide. For example,

- How does a production manager determine the cost of producing the company's product? (Chapter 14)
- How can a financial manager prepare a budget for the next accounting period? (Chapter 16)

ACCOUNTING MEASUREMENT AND CONCEPTS

 2. Describe the three fundamental accounting concepts: business entity, monetary unit, and historical cost.

The accounting decision-making information system is designed to provide information to users to help them make business decisions. These decisions can have a significant impact on and may cause the success or failure of a particular business. Consequently, it is necessary to have standards to guide accountants in the quantification, processing, and communication of economic activities. The standards for reporting to external users are termed *generally accepted accounting principles* (GAAP). Generally accepted accounting principles are defined as the methods and procedures used in the preparation of financial statements.

Several broad concepts are related to the selection of the specific principle to use in different situations. Among these concepts are business entity, unit of measure, and historical cost. Knowledge of these and other concepts introduced later in the text will assist in developing an understanding of the accounting process.

Business Entity

Business organizations are frequently referred to as *accounting entities* or *business entities*. A business entity is any business organization that exists as an economic unit. In accounting each business entity is con-