

GLOBAL
EDITION



Horngren's Financial & Managerial Accounting

The Financial Chapters

SIXTH EDITION

Tracie Miller-Nobles • Brenda Mattison • Ella Mae Matsumura



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**Financial & Managerial
Accounting**

THE FINANCIAL CHAPTERS

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Changes to This Edition

General

Revised end-of-chapter short exercises, exercises, problems, continuing problems, comprehensive problems, and critical thinking cases.

NEW! Using Excel. This end-of-chapter problem introduces students to Excel to solve common accounting problems as they would in the business environment.

NEW! Tying It All Together feature ties together key concepts from the chapter using the company highlighted in the chapter opener. The in-chapter box feature presents scenarios and questions that the company could face and focuses on the decision-making process. The end-of-chapter business case helps students synthesize the concepts of the chapter and reinforce critical thinking.

NEW! A Continuing Problem starts in Chapter 1 and runs through the financial chapters.

Chapter 1

NEW! Added discussion about why accounting is important to non-accounting majors.

Chapter 3

Updated discussion of the revenue recognition principle for the newly released standard.

Added a discussion on how to calculate interest for notes receivable and notes payable.

Changed interest calculations to use a 365-day year rather than a 360-day year to better reflect how actual lenders calculate interest.

Chapter 4

Increased the usage of the classified balance sheet as a requirement for end-of-chapter problems.

Changed the balance sheet presentation to reflect Property, Plant, and Equipment rather than Plant Assets.

Chapter 5

REVISED! Discussion on sales of merchandise revised to reflect the newly released revenue recognition standard, including reporting sales on account at the net amount and introduction of the Sales Discounts Forfeited account.

Changed income statement presentation to reflect Other Income and (Expenses) instead of Other Revenue and (Expenses) to better reflect how actual income statements are presented.

NEW! Added Appendix 5A that discusses multiple performance obligations.

Chapter 6

NEW! Added a comprehensive problem for Chapters 5 and 6 which includes the complete accounting cycle for a merchandising company with ratio analysis.

Chapter 7

NEW! Added coverage of credit card sales. In previous editions, this topic was covered in Chapter 8.

Chapter 8

Expanded coverage of estimating bad debts to help students understand why the Allowance for Bad Debts account may have either a debit or credit unadjusted balance due to previously overestimated or underestimated adjustments.

Chapter 9

NEW! Added comprehensive problem for Chapters 7–9 which includes transactions and analysis for cash, receivables, and long-term assets.

Chapter 10

REVISED! Discussion on debt and equity securities revised to reflect newly released financial instrument standard including the elimination of trading investments (equity) and available-for-sale investments (equity).

Chapter 11

Updated the payroll section for consistency with current payroll laws at the time of printing.
Added a section to illustrate how companies record the payment of payroll liabilities.

Chapter 12

NEW! Added discussion on future value, including determining the future value of a lump sum and of an annuity.

Chapter 13

NEW! Moved the corporate income statement, including calculating earnings per share, from the Chapter 15 Appendix to Chapter 13. The discussion on the Extraordinary Items section has been removed to align with current standards.

NEW! Added comprehensive problem for Chapters 11–13 which includes payroll, other current liabilities, long-term liabilities, and stockholders' equity transactions and analysis.

Chapter 14

Modified the wording in Changes to Current Assets and Current Liabilities section of preparing the statement of cash flows, indirect method, to emphasize adjustments are made to net income to convert from accrual basis to cash basis.

Chapter 15

Rearranged the liquidity ratios from most stringent to least stringent (cash ratio, acid-test ratio, current ratio).

NEW! Added problem (both A and B series) that has students complete a trend analysis and ratios to analyze a company for its investment potential.

<http://www.pearsonglobaleditions.com/Sitemap/Horngren/>

Financial & Managerial Accounting . . . Expanding on Proven Success

Accounting Cycle Tutorial

Pearson MyLab Accounting's interactive tutorial helps students master the Accounting Cycle for early and continued success in the Introduction to Accounting course. The tutorial, accessed by computer, smartphone, or tablet, provides students with brief explanations of each concept of the Accounting Cycle through engaging, interactive activities. Students are immediately assessed on their understanding and their performance is recorded in the Pearson MyLab Accounting Gradebook. Whether the Accounting Cycle Tutorial is used as a remediation self-study tool or course assignment, students have yet another resource within Pearson MyLab Accounting to help them be successful with the accounting cycle.

NEW! ACT Comprehensive Problem

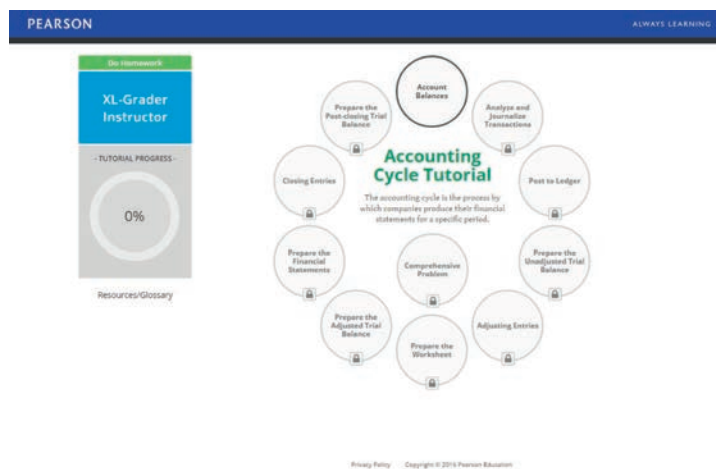
The Accounting Cycle Tutorial now includes a comprehensive problem that allows students to work with the same set of transactions throughout the accounting cycle. The comprehensive problem, which can be assigned at the beginning or the end of the full cycle, reinforces the lessons learned in the accounting cycle tutorial activities by emphasizing the connections between the accounting cycle concepts.

Study Plan

The Study Plan acts as a tutor, providing personalized recommendations for each of your students based on his or her ability to master the learning objectives in your course. This allows students to focus their study time by pinpointing the precise areas they need to review, and allowing them to use customized practice and learning aids—such as videos, eText, tutorials, and more—to get them back on track. Using the report available in the Gradebook, you can then tailor course lectures to prioritize the content where students need the most support—offering you better insight into classroom and individual performance.

Dynamic Study Modules

help students study effectively on their own by continuously assessing their activity and performance in real time. Here's how it works: students complete a set of questions with a unique answer format that also asks them to indicate their confidence level. Questions repeat until the student can answer them all correctly and confidently. Once completed, Dynamic Study Modules explain the concept using materials from the text. These are available as graded assignments prior to class, and accessible on smartphones, tablets, and computers. **NEW!** Instructors can now remove questions from Dynamic Study Modules to better fit their course. Available for select titles.



Learning Catalytics

Learning Catalytics helps you generate class discussion, customize your lecture, and promote peer-to-peer learning with real-time analytics. As a student response tool, Learning Catalytics uses students' smartphones, tablets, or laptops to engage them in more interactive tasks and thinking.

- **NEW!** Upload a full PowerPoint® deck for easy creation of slide questions.
- Help your students develop critical thinking skills.
- Monitor responses to find out where your students are struggling.
- Rely on real-time data to adjust your teaching strategy.
- Automatically group students for discussion, teamwork, and peer-to-peer learning.

Depreciation

Related Account: Furniture (Normal DR balance)

Contra Account: Accumulated Depreciation—Furniture (Normal CR balance)

A business may have a separate Accumulated Depreciation account for each depreciable asset

- Accumulated Depreciation – Furniture
- Accumulated Depreciation - Building

PEARSON

NEW! Tying It All Together

This feature ties together key concepts from the chapter using the company highlighted in the chapter opener. The in-chapter box feature presents scenarios and questions that the company could face and focuses on the decision-making process. The end of chapter business case helps students synthesize the concepts of the chapter and reinforce critical thinking.

TYING IT ALL TOGETHER

Hyatt Hotels Corporation was founded in 1957 when Jay Pritzker purchased the first Hyatt hotel next to the Los Angeles International Airport. Today, Hyatt Hotels owns and operates hotels in 52 countries around the world. For the year ended December 31, 2015, the company reported revenues totaling \$4.3 billion with net income of \$124 million. (You can find Hyatt Hotels Corporation's annual report at <https://www.sec.gov/Archives/edgar/data/1468174/000146817416000152/h10-k123115.htm>)

Would Hyatt Hotels Corporation record closing entries and why?

Hyatt Hotels would record closing entries in order to get the accounts ready for next year. All companies record closing entries in order to zero out all revenue and expense accounts. In addition, the closing process updates the Retained Earnings account balance for net income or loss during the period and any dividends paid to stockholders.

Why are temporary accounts important in the closing process? What type of temporary accounts would Hyatt Hotels Corporation have?

Temporary accounts are important in the closing process because these accounts relate to a particular accounting period and are

closed at the end of the period. Revenues, expenses, and dividends are all temporary accounts. Some examples of temporary accounts that Hyatt Hotels might have include Owned and Leased Hotels Revenue; Selling, General, and Administrative Expense; Interest Expense; and Dividends.

When would Hyatt Hotels Corporation prepare its post-closing trial balance? What type of accounts would be reported on this trial balance?

A post-closing trial balance is a list of all permanent accounts and their balances at the end of the accounting period and is prepared after the closing process. Hyatt Hotels would report only permanent accounts on its post-closing trial balance. Some examples of permanent accounts that Hyatt Hotels might have include assets, such as Cash and Property; liabilities, such as Accounts Payable; and equity, such as Common Stock and Retained Earnings.

learning catalytics™

Session 26148360

Multiple choice question

Fernandez Company allocates overhead based on machine hours. Selected data for the most recent year follow:

- Estimated manufacturing overhead cost \$240,000
- Actual manufacturing overhead cost \$215,000
- Estimated machine hours 40,000
- Actual machine hours 41,000

The estimates were made as of the beginning of the year, while the actual results were for the entire year. The amount of manufacturing overhead allocated for the year based on machine hours would have been:

A. \$215,000

B. \$227,500

C. \$240,000

D. \$245,000

Hide response / Change response

Refresh / Send a message to the instructor / Join another session

Animated Lectures

These pre-class learning aids are available for every learning objective and are professor-narrated PowerPoint summaries that will help students prepare for class. These can be used in an online or flipped classroom experience or simply to get students ready for lecture.

Chapter Openers

Chapter openers set up the concepts to be covered in the chapter using stories students can relate to. The implications of those concepts on a company's reporting and decision making processes are then discussed.

> Tying It All Together 4-1

Before you begin this assignment, review the Tying It All Together feature in the chapter. It will also be helpful if you review Hyatt Hotels Corporation's 2015 annual report (<https://www.sec.gov/Archives/edgar/data/1468174/000146817416000152/h10-k123115.htm>).

Hyatt Hotels Corporation is headquartered in Chicago and is a leading global hospitality company. The company develops, owns, and operates hotels, resorts, and vacation ownership properties in 52 different countries. For the year ended December 31, 2015, Hyatt Hotels reported the following select account information (in millions):

Revenue	\$ 4,328
Selling, general, and administrative expense	4,005
Other Expenses	61
Interest Expense	68
Income Tax Expense	70
Dividends	0
Retained Earnings, December 31, 2014	2,165

Requirements

1. Journalize Hyatt Hotels Corporation's closing entries at December 31, 2015.
2. Determine Hyatt Hotels Corporation's ending Retained Earnings balance at December 31, 2015.
3. Review the Hyatt Hotels Corporation's balance sheet included in the 2015 annual report and find ending Retained Earnings, December 31, 2015. Does your ending Retained Earnings calculated in Requirement 2 match?

Effect on the Accounting Equation

Next to every journal entry in the financial chapters, these illustrations help reinforce the connections between recording transactions and the effect those transactions have on the accounting equation.

On November 10, Smart Touch Learning performed services for clients, for which the clients will pay the company later. The business earned \$3,000 of service revenue on account.

This transaction increased Accounts Receivable, so we debit this asset. Service Revenue is increased with a credit.

Date	Accounts and Explanation	Debit	Credit
Nov. 10	Accounts Receivable	3,000	
	Service Revenue		3,000
	<i>Performed services on account.</i>		

$$\left. \begin{array}{l} \underline{A \uparrow} \\ \text{Accounts} \\ \text{Receivable} \uparrow \end{array} \right\} = \left\{ \begin{array}{l} \underline{L} + \underline{E \uparrow} \\ \text{Service} \\ \text{Revenue} \uparrow \end{array} \right.$$

Instructor Tips & Tricks

Found throughout the text, these handwritten notes mimic the experience of having an experienced teacher walk a student through concepts on the “board.” Many include mnemonic devices or examples to help students remember the rules of accounting.

$$\left. \begin{array}{l} \underline{A \downarrow} \\ \text{Accumulated} \\ \text{Depreciation—} \\ \text{Building} \uparrow \end{array} \right\} = \left\{ \begin{array}{l} \underline{L} + \underline{E \downarrow} \\ \text{Depreciation} \\ \text{Expense—} \\ \text{Building} \uparrow \end{array} \right.$$

Date	Accounts and Explanation	Debit	Credit
Dec. 31	Depreciation Expense—Building	250	
	Accumulated Depreciation—Building		250
	<i>To record depreciation on building.</i>		

Remember, an increase in a contra asset, such as Accumulated Depreciation, decreases total assets. This is because a contra asset has a credit balance and credits decrease assets.

Common Questions, Answered

Our authors have spent years in the classroom answering students’ questions and have found patterns in the concepts or rules that consistently confuse students. These commonly asked questions are located in the margin of the text next to where the answer or clarification can be found highlighted in purple text.

Notice that Smart Touch Learning credited the amortization directly to the intangible asset, Patent, instead of using an Accumulated Amortization account. A company may credit an intangible asset directly when recording amortization expense, or it may use the account Accumulated Amortization. **Companies frequently choose to credit the asset account directly because the residual value is generally zero and there is no physical asset to dispose of at the end of its useful life, so the asset essentially removes itself from the books through the process of amortization.**

At the end of the first year, Smart Touch Learning will report this patent at \$160,000 (\$200,000 cost minus first-year amortization of \$40,000), the next year at \$120,000, and so forth. Each year for five years the value of the patent will be reduced until the end of its five-year life, at which point its book value will be \$0.

Why was the account Patent credited instead of Accumulated Amortization—Patent?



Try It! Boxes

Found after each learning objective, Try Its! give students opportunities to apply the concept they've just learned by completing an accounting problem. Links to these exercises appear throughout the eText, allowing students to practice in Pearson MyLab Accounting without interruption.

Try It!

Total Pool Services earned \$130,000 of service revenue during 2018. Of the \$130,000 earned, the business received \$105,000 in cash. The remaining amount, \$25,000, was still owed by customers as of December 31. In addition, Total Pool Services incurred \$85,000 of expenses during the year. As of December 31, \$10,000 of the expenses still needed to be paid. In addition, Total Pool Services prepaid \$5,000 cash in December 2018 for expenses incurred during the next year.

1. Determine the amount of service revenue and expenses for 2018 using a cash basis accounting system.
2. Determine the amount of service revenue and expenses for 2018 using an accrual basis accounting system.

Check your answers online in Pearson MyLab Accounting or at <http://www.pearsonglobaleditions.com/Sitemap/Horngren/>.

For more practice, see Short Exercises S3-1 and S3-2. [Pearson MyLab Accounting](#)

Try It! Solution Videos

Author-recorded and accompanying Try It! Exercises, these videos walk students through the problem and the solution.

Startech Surveillance Services had the following adjustments as of the end of the year:

- a. Equipment depreciation was \$1,500. **D**
- b. \$700 of advertising expense was incurred but not paid. (Use Advertising Payable.) **A**
- c. Office Supplies on hand at the end of the year totaled \$250. The beginning balance of Office Supplies was \$600. **D**
- d. \$1,200 of rent revenue was earned but not recorded or received. **A**
- e. Unearned revenue of \$3,000 had been earned. **D**

6. For each situation, indicate which category of adjustment (deferral or accrual) is described.
7. Journalize the adjusting entry needed.

Deferral: Cash occurs before revenue or expense
Accrual: Cash occurs after revenue or expense

a. Dep. Exp.	1500	b. Adv. Exp.	700
Acc. Dep.	1500	Adv. Pay.	700

IFRS

Information on IFRS provides guidance on how IFRS differs from U.S. GAAP throughout the financial chapters.



Decision Boxes

This feature provides common questions and potential solutions business owners face. Students are asked to determine the course of action they would take based on concepts covered in the chapter and are then given potential solutions.

DECISIONS

Can we cut these costs?

The management team of Puzzle Me is looking at the production cost reports for July, and discussing opportunities for improvement. The production manager thinks the production process is very efficient, and there is little room for cost savings in conversion costs. The purchasing manager tells the team that he was recently approached by a supplier with an excellent reputation for quality. This supplier submitted a bid for cardboard that was a little thinner but would allow the company to decrease direct materials costs by 5%. What should the team do?

Solution

The production cost reports for the Assembly and Cutting Departments show direct materials costs of \$2.80 and \$0.50 per puzzle, respectively, for total direct materials cost of \$3.30 per puzzle. A decrease of 5% in direct materials costs would result in a savings

of \$0.165 per puzzle ($\$3.30 \times 5\%$) and decrease total costs from \$5.30 to \$5.135 per puzzle. Based on the completed production of 38,000 puzzles in July, the total cost savings would be \$6,270 per month ($\$0.165 \text{ per puzzle} \times 38,000 \text{ puzzles}$). The purchasing manager recommends using the new supplier.

Alternate Solution

The marketing manager has a different perspective. He points out that most of the puzzles produced are for toddlers. Based on market research, the adults who purchase these puzzles like the sturdy construction. If Puzzle Me changes materials and the puzzles do not stand up well to the treatment they receive by young children, the company could rapidly lose market share. The marketing manager does not recommend using a thinner cardboard.

> Things You Should Know

1. Why is accounting important?

- Accounting is the language of business.
- Accounting is used by decision makers including individuals, businesses, investors, creditors, and taxing authorities.
- Accounting can be divided into two major fields: financial accounting and managerial accounting.
- Financial accounting is used by external decision makers, and managerial accounting is used by internal decision makers.
- All businesses need accountants. Accountants work in private, public, and governmental jobs.
- Accountants can be licensed as either a certified public accountant (CPA) or certified management accountant (CMA).

Things You Should Know

Provides students with a brief review of each learning objective presented in a question and answer format.

NEW! Using Excel Problems

This end of chapter problem introduces students to Excel to solve common accounting problems as they would in the business environment. Students will work from a template that will aid them in solving the problem related to accounting concepts taught in the chapter. Each chapter focuses on different Excel skills.

CHAPTER 4

> Using Excel

P4-41 Using Excel to prepare financial statements, closing entries, and the post-closing trial balance

Download an Excel template for this problem online in Pearson MyLab Accounting or at <http://www.pearsonglobaleditions.com/Sitemap/Horngren/>.

Cedar River Corporation started operations on July 1, 2018. On July 31, a trial balance was prepared, adjusting entries were journalized and posted, and an adjusted trial balance was completed. A worksheet is to be used to help prepare the financial statements and the post-closing trial balance.

Requirements

1. Use Excel to complete the Income Statement and Balance Sheet columns of the worksheet. Carry numbers from the adjusted trial balance columns of the worksheet to the income statement and balance sheet columns using Excel formulas.
 - a. Use formulas to total the columns.
 - b. Use a formula to determine the amount of the net income or net loss.
 - c. Format the cells requiring dollar signs.
 - d. Boldface the totals.
2. Prepare the income statement, the statement of retained earnings, and a classified balance sheet.
 - a. Use the Increase Indent button on the Home tab to indent items.
 - b. Use formulas to sum items.

End-of-Chapter Continuing and Comprehensive Problems

> Continuing Problem

P1-55 is the first problem in a continuing problem that will be used throughout the chapters to reinforce the concepts learned.

P1-55 Using the accounting equation for transaction analysis, preparing financial statements, and calculating return on assets (ROA)

Let's Bike Company is a company that rents bicycles for use on cycling trails along the coastline. Leona Cho and Bowie Lee both worked for one of the "Big Four" accounting firms after graduation and became CPAs. As they love cycling, they had a dream of promoting cycling as a healthy activity, which at the same time helps reduce the carbon footprint. They decided to begin a new business that combined their love of cycling with their business knowledge. Leona and Bowie decided that they will create a new corporation, Let's Bike Company, or LBC for short. The business began operations on November 1, 2018.

-
- | | |
|--------|--|
| Nov. 1 | Received \$23,000 cash to begin the company and issued common stock to Leona and Bowie. |
| 2 | Purchased bikes for \$5,400 on account. |
| 3 | Purchased office supplies on account, \$980. |
| 8 | Earned \$2,300 cash for rental of bikes to individual customers. |
| 12 | Paid \$3,400 and \$950 related to the purchases on November 2 and 3, 2018, respectively. |



Continuing Problem—Starts in Chapter 1 and runs through the financial chapters.

Comprehensive Problem 1 for Chapters 1–4—Covers the entire accounting cycle for a service company.

Comprehensive Problem 2 for Chapters 1–4—A continuation of Comprehensive Problem 1. It requires the student to record transactions for the month after the closing process.

NEW! **Comprehensive Problem for Chapters 5 and 6**—Covers the entire accounting cycle for a merchandise company, including analysis.

NEW! **Comprehensive Problem for Chapters 7–9**—Covers cash, receivables, and long-term assets transactions and analysis.

NEW! **Comprehensive Problem for Chapters 11–13**—Covers payroll, other current liabilities, long-term liabilities, and stockholders' equity transactions and analysis.

Comprehensive Problem for Appendix B—Uses special journals and subsidiary ledgers and covers the entire accounting cycle for a merchandise company. Students can complete this comprehensive problem using the Pearson MyLab Accounting General Ledger or Quickbooks™ software.

> Comprehensive Problem 1 for Chapters 1–4

Murphy Delivery Service completed the following transactions during December 2018:

- | | |
|--------|---|
| Dec. 1 | Murphy Delivery Service began operations by receiving \$13,000 cash and a truck with a fair value of \$9,000 from Russ Murphy. The business issued Murphy shares of common stock in exchange for this contribution. |
| 1 | Paid \$600 cash for a six-month insurance policy. The policy begins December 1. |
| 4 | Paid \$750 cash for office supplies. |
| 12 | Performed delivery services for a customer and received \$2,200 cash. |
| 15 | Completed a large delivery job, billed the customer, \$3,300, and received a promise to collect the \$3,300 within one week. |
| 18 | Paid employee salary, \$800. |
| 20 | Received \$7,000 cash for performing delivery services. |
| 22 | Collected \$2,200 in advance for delivery service to be performed later. |
| 25 | Collected \$3,300 cash from customer on account. |
| 27 | Purchased fuel for the truck, paying \$150 on account. (Credit Accounts Payable) |
| 28 | Performed delivery services on account, \$1,400. |
| 29 | Paid office rent, \$1,400, for the month of December. |
| 30 | Paid \$150 on account. |
| 31 | Cash dividends of \$2,500 were paid to stockholders. |

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Dear Colleague,

Thank you for taking the time to review *Hornngren's Financial and Managerial Accounting*. We are excited to share our innovations with you as we expand on the proven success of our revision to the Hornngren franchise. Using what we learned from focus groups, market feedback, and our colleagues, we've designed this edition to focus on several goals.

First, we again made certain that the textbook, student resources, and instructor supplements are clear, consistent, and accurate. As authors, we reviewed each and every component to ensure a student experience free of hurdles. Next, through our ongoing conversations with our colleagues and our time engaged at professional conferences, we confirmed that our pedagogy and content represents the leading methods used in teaching our students these critical foundational topics. Lastly, we concentrated on student success and providing resources for professors to create an active and engaging classroom.

We are excited to share with you some new features and changes in this latest edition. First, we have added a new Tying It All Together feature that highlights an actual company and addresses how the concepts of the chapter apply to the business environment. A Using Excel problem has also been added to every chapter to introduce students to using Excel to solve common accounting problems as they would in the business environment. Chapter 5 (Merchandising Operations) has been updated for the newly released revenue recognition standard.

We trust you will find evidence of these goals throughout our text and in the MyLab Accounting component. We welcome your feedback and comments. Please do not hesitate to contact us at HornngrensAccounting@pearson.com or through our editor, Lacey Vitetta, LaceyVitetta@pearson.com.

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Instructor and Student Resources

Each supplement, including the resources in Pearson MyLab Accounting, has been reviewed by the author team to ensure accuracy and consistency with the text. Given their personal involvement, you can be assured of the high quality and accuracy of all supplements.

For Instructors

Pearson MyLab Accounting

Online Homework and Assessment Manager: <http://www.myaccountinglab.com>

Instructor Resource Center: <http://www.pearsonglobaleditions.com/Sitemap/Horngren/>

For the instructor's convenience, the instructor resources can be downloaded from the textbook's catalog page (<http://www.pearsonglobaleditions.com/Sitemap/Horngren/>) and Pearson MyLab Accounting. Available resources include the following:

Online Instructor's Resource Manual:

Course Content:

- Tips for Taking Your Course from Traditional to Hybrid, Blended, or Online
- Standard Syllabi for Financial Accounting (10-week & 16-week)
- Sample Syllabi for 10- and 16-week courses
- "First Day of Class" student handouts include:
 - Student Walk-Through to Set-up Pearson MyLab Accounting
 - Tips on How to Get an A in This Class

Chapter Content:

- Chapter Overview
 - Contains a brief synopsis and overview of each chapter.
- Learning Objectives
- Teaching Outline with Lecture Notes
 - Combines the Teaching Outline and the Lecture Outline Topics, so instructors only have one document to review.
 - Walks instructors through what material to cover and what examples to use when addressing certain items within the chapter.
- Handout for Student Notes
 - An outline to assist students in taking notes on the chapter.
- Student Chapter Summary
 - Aids students in their comprehension of the chapter.
- Assignment Grid
 - Indicates the corresponding Learning Objective for each exercise and problem.
 - Answer Key to Chapter Quiz
- Ten-Minute Quiz
 - To quickly assess students' understanding of the chapter material.
- Extra Critical Thinking Problems and Solutions
 - Critical Thinking Problems previously found in the text were moved to the IRM so instructors can continue to use their favorite problems.
- Guide to Classroom Engagement Questions
 - Author-created element will offer tips and tricks to instructors in order to help them use the Learning Catalytic questions in class.

Online Instructor's Solutions Manual:

- Contains solutions to all end-of-chapter questions, short exercises, exercises, and problems.
- The Try It! Solutions, previously found at the end of each chapter, are now available for download with the ISM.
- Using Excel templates, solutions, and teaching tips.
- All solutions were thoroughly reviewed by the author team and other professors.

Online Test Bank:

- Includes more than 3,900 questions, including NEW multi-level questions.
- Both conceptual and computational problems are available in true/false, multiple choice, and open-ended formats.
- Algorithmic test bank is available in Pearson MyLab Accounting.

PowerPoint Presentations:***Instructor PowerPoint Presentations:***

- Complete with lecture notes.
- Mirrors the organization of the text and includes key exhibits.

Student PowerPoint Presentations:

- Abridged versions of the Instructor PowerPoint Presentations.
- Can be used as a study tool or note-taking tool for students.

Demonstration Problem PowerPoint Presentations:

- Offers instructors the opportunity to review in class the exercises and problems from the chapter using different companies and numbers.

Clicker Response System (CRS) PowerPoint Presentations:

- 10 multiple-choice questions to use with a Clicker Response System.

Image Library:

- All image files from the text to assist instructors in modifying our supplied PowerPoint presentations or in creating their own PowerPoint presentations.

For Students

[Pearson MyLab Accounting](#)

Online Homework and Assessment Manager: <http://www.myaccountinglab.com>

- Pearson eText
- Using Excel templates
- Animated Lectures
- Interactive Figures
- Student PowerPoint® Presentations
- Flash Cards

Student Resource Web site: <http://www.pearsonglobaleditions.com/Sitemap/Horngren/>

The book's Web site contains the following:

- Data Files: Select end-of-chapter problems have been set up in QuickBooks software and the related files are available for download.
- Working Papers
- Try It! Solutions: The solutions to all in-chapter Try Its! are available for download.
- Links to Target Corporation's Annual Report and Kohl's Corporation's Annual Report

<http://www.pearsonglobaleditions.com/Sitemap/Horngren/>

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Ella Mae Matsumura thanks her family for their longstanding love and support in her endeavors: husband, Kam-Wab Tsui; son, David Tsui; sister and late parents, Linda, Lester, and Eda Matsumura. She would also like to express her appreciation to: the numerous colleagues and friends who have encouraged her and helped her grow as a scholar and a person; the many students who have provided constructive feedback that has shaped her teaching; and her faith community for its enduring love and affirmation.

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Accounting and the Business Environment

1



Coffee, Anyone?

Aiden Jackson stared at the list the banker had given him during their meeting. *Business plan, cash flow projections, financial statements, tax returns.* Aiden had visited with the banker because he had a dream of opening a coffee shop near campus. He knew there was a need; students were always looking for a place to study and visit with their friends. He also had the experience. He had worked for the past three years as a manager of a coffee shop in a neighboring town. Aiden needed one thing, though—money. He had saved a small amount of money from his job and received several contributions from family and friends, but he still didn't have enough to open the business. He had decided the best option

was to get a loan from his bank. After the meeting, Aiden felt overwhelmed and unsure of the future of his business.

You might think that Aiden was facing an impossible situation, but you'd be wrong. Almost every new business faces a similar situation. The owner starts with an inspiration, and then he or she needs to provide enough continuous cash flow to build the business. In addition, the owner has to make decisions such as: *Should we expand to another location? Do we have enough money to purchase a new coffee roaster? How do I know if the business made a profit?*

So how does Aiden get started? Keep reading. That's what accounting teaches you.



Why Study Accounting?

The situation that Aiden faced is similar to the situations faced in the founding of most businesses. **Starbucks Corporation**, for example, first opened its doors in Seattle, Washington, in 1971. Three partners, Jerry Baldwin, Zev Siegl, and Gordon Bowker, were inspired by a dream of selling high-quality coffee. We know their dream was successful because Starbucks currently has more than 22,000 stores in 67 countries. How did Starbucks grow from a small one-store shop to what it is today? The partners understood accounting—the language of business. They understood how to measure the activities of the business, process that information into reports (financial statements), and then use those reports to make business decisions. Your knowledge of accounting will help you better understand businesses. It will make you a better business owner, employee, or investor.





Chapter 1 Learning Objectives



- 1 Explain why accounting is important and list the users of accounting information
- 2 Describe the organizations and rules that govern accounting
- 3 Describe the accounting equation and define assets, liabilities, and equity
- 4 Use the accounting equation to analyze transactions
- 5 Prepare financial statements
- 6 Use financial statements and return on assets (ROA) to evaluate business performance

WHY IS ACCOUNTING IMPORTANT?

Learning Objective 1

Explain why accounting is important and list the users of accounting information

Accounting

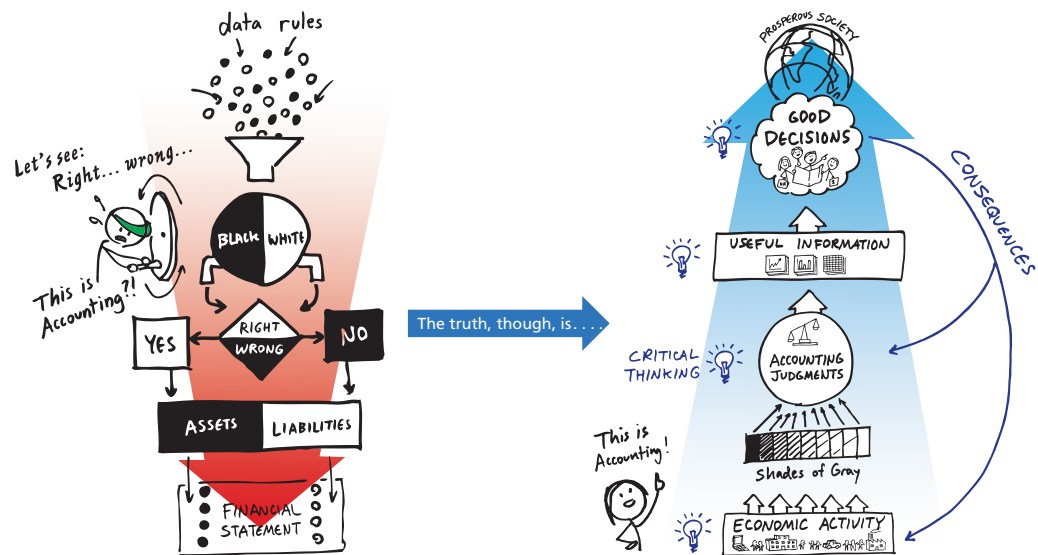
The information system that measures business activities, processes the information into reports, and communicates the results to decision makers.

You've heard the term *accounting*, but what exactly is it? **Accounting** is the information system that measures business activities, processes the information into reports, and communicates the results to decision makers. Accounting is the language of business. The better you understand the language of business, the better you can manage your own business, be a valuable employee, or make wise investments.

We tend to think of accountants as boring and dry. However, accounting is much more than simple recordkeeping or bookkeeping. Today's accountants participate in a broad range of activities such as the investigation of financial evidence, the development of computer programs to process accounting information, and the communication of financial results to interested parties. The knowledge of accounting is used every day to help make business decisions.

Recently, leaders from across the accounting community, called the Pathways Commission, came together to create a vision model (see Exhibit 1-1) to help students and

Exhibit 1-1 Pathways Vision Model



We tend to think of accountants as boring and dry.

Accountants are instrumental in helping to create a prosperous society.




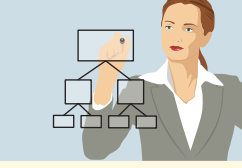
the public understand what accounting is. The model is intended to explain in a visual way what accountants really do. Accounting starts with economic activities that accountants review and evaluate using critical thinking and judgment to create useful information that helps individuals make good decisions. The model emphasizes that good decisions have an impact on accounting judgments and economic activity, thus creating a circular flow of cause and effect. Accountants are more than boring, tedious number crunchers. Instead, accountants play a critical role in supporting a prosperous society.

Decision Makers: The Users of Accounting Information

We can divide accounting into two major fields: financial accounting and managerial accounting. **Financial accounting** provides information for external decision makers, such as outside investors, lenders, customers, and the federal government. **Managerial accounting** focuses on information for internal decision makers, such as the company's managers and employees.

Exhibit 1-2 illustrates the difference between financial accounting and managerial accounting. Regardless of whether they are external or internal to the company, all decision makers need information to make the best choices. The bigger the decision, the more information decision makers need. Let's look at some ways in which various people use accounting information to make important decisions.

Exhibit 1-2 | Decision Making: Financial Versus Managerial Accounting

Financial Accounting	Managerial Accounting
	
<p>External Decision Makers:</p> <p>Should I invest in the business? Is the business profitable? Should we lend money to the business? Can the business pay us back?</p>	<p>Internal Decision Makers:</p> <p>How much money should the business budget for production? Should the business expand to a new location? How do actual costs compare to budgeted costs?</p>

Individuals

How much cash do you have? How much do you need to save each month to retire at a certain age or pay for your children's college education? Accounting can help you answer questions like these. By using accounting information, you can manage your money, evaluate a new job, and better decide whether you can afford to buy a new computer. Businesses need accounting information to make similar decisions.

Businesses

Business owners use accounting information to set goals, measure progress toward those goals, and make adjustments when needed. The financial statements give owners the information they need to help make those decisions. Financial statements are helpful when, for example, a business owner wants to know whether his or her business has enough cash to purchase another computer.

Financial Accounting

The field of accounting that focuses on providing information for external decision makers.

Managerial Accounting

The field of accounting that focuses on providing information for internal decision makers.



Accounting is alive! As businesses evolve and the type of business transactions change, so must the language of business. The most significant changes in the business world in the last decade have been the huge increases in international commerce. Because more business is conducted internationally, decision makers are looking for an international accounting language.

Look for more information about International Financial Reporting Standards (IFRS) anywhere that you see this image.



Creditor

Any person or business to whom a business owes money.

Certified Public Accountants (CPAs)

Licensed professional accountants who serve the general public.

What if I want more information about becoming a CPA or CMA?



Certified Management Accountants (CMAs)

Certified professionals who specialize in accounting and financial management knowledge. They typically work for a single company.

Investors

Outside investors who have some ownership interest often provide the money to get a business going. Suppose you're considering investing in a business. How would you decide whether it is a good investment? In making this decision, you might try to predict the amount of income you would earn on the investment. Also, after making an investment, investors can use a company's financial statements to analyze how their investment is performing.

You might have the opportunity to invest in the stock market through your company's retirement plan. Which investments should you pick? Understanding a company's financial statements will help you decide. You can view the financial statements of large companies that report to the Securities and Exchange Commission (SEC) by logging on to <http://www.finance.yahoo.com>, <http://www.google.com/finance>, or the SEC's EDGAR database (<http://www.sec.gov/edgar.shtml>).

Creditors

Any person or business to whom a business owes money is a **creditor**. Before extending credit to a business, a creditor evaluates the company's ability to make the payments by reviewing its financial statements. Creditors follow the same process when you need to borrow money for a new car or a house. The creditor reviews accounting data to determine your ability to make the loan payments. What does your financial position tell the creditor about your ability to repay the loan? Are you a good risk for the bank?

Taxing Authorities

Local, state, and federal governments levy taxes. Income tax is calculated using accounting information. Good accounting records can help individuals and businesses take advantage of lawful deductions. Without good records, the Internal Revenue Service (IRS) can disallow tax deductions, resulting in a higher tax bill plus interest and penalties.

Accounting Matters

What do businesses such as Amazon.com, Walmart, or even your local sandwich shop across from campus have in common? They all rely upon accounting information to make business decisions. Even if you don't plan on majoring in accounting, the knowledge of accounting helps all businesses plan for the future and evaluate past performance. The skills you learn in this class will help you be a better business professional. Businesses can't function, though, without accountants. That is why a degree in accounting opens so many doors upon graduation. A bachelor's degree in accounting could lead you to several different accounting careers.

You've probably heard of a CPA before. **Certified Public Accountants**, or **CPAs**, are licensed professional accountants who serve the general public. CPAs work for public accounting firms, businesses, government entities, or educational institutions. What does it take to be a CPA? Although requirements vary between states, to be certified in a profession, one must meet the educational and/or experience requirements *and* pass a qualifying exam. **The American Institute of Certified Public Accountants (AICPA) Web site (<http://www.thiswaytocpa.com>) contains a wealth of information about becoming a CPA, career opportunities, and exam requirements.**

Certified Management Accountants, or **CMAs**, are certified professionals who specialize in accounting and financial management knowledge. Generally, CMAs work for a single company. **You can find information about becoming a CMA, how a CMA differs from a CPA, and why employers are recognizing the CMA certification on the Institute of Management Accountants (IMA) Web site (<http://www.imanet.org>).** It's worth spending the time and energy for accountants to get certified—certified accountants generally make 10–15% more than their noncertified colleagues when they enter the workforce.

Studying accounting and becoming certified professionally can lead to a financially secure job. According to Robert Half's *2016 Salary Guide*, the top positions in demand that rely on