

**Getting Started** ..... vi

**Section 1**  
**Income Statements**

Section Objectives ..... 1.1

Introduction ..... 1.1

Reporting Periods ..... 1.2

Basic Elements ..... 1.4

    Understanding the Numbers ..... 1.5

    Identifying the Reported Time Period ..... 1.6

Revenue (Sales) ..... 1.7

    Information on Invoices ..... 1.8

    Payment Terms ..... 1.10

Expense ..... 1.12

    Cost of Goods Sold (Cost of Sales) ..... 1.14

        Raw Materials Cost ..... 1.15

        Labor Cost ..... 1.15

        Utilities Cost ..... 1.17

        Depreciation Cost ..... 1.18

        All Other Costs ..... 1.20

    Selling Expense ..... 1.21

        Labor Expense ..... 1.22

        Commissions Expense ..... 1.22

        Travel Expense ..... 1.23

        Marketing/Advertising Expense ..... 1.24

        Office Expense ..... 1.24

    Research and Development Expense ..... 1.25

    Administrative Expense ..... 1.26

Expense Allocation ..... 1.27

    Physical Measures Approach ..... 1.28

    Sales Dollars Approach ..... 1.29

    Net Realizable Value Approach ..... 1.30

Pretax Income ..... 1.30

Taxes ..... 1.31

Net Income ..... 1.32

Income Statement Design ..... 1.33

Section Summary ..... 1.36

**Section 2**  
**Balance Sheets**

Section Objectives .....	2.1
Introduction .....	2.1
Assets	
Current Assets .....	2.2
Cash .....	2.3
Marketable Securities .....	2.4
Accounts Receivable .....	2.6
Inventories .....	2.7
Determining Total Value .....	2.8
Inventory Records .....	2.10
Raw Materials Inventory Records .....	2.10
Semi-finished and Finished Goods Inventory Records .....	2.11
Valuation Methods .....	2.11
Valuation Methods— Average Cost .....	2.12
Valuation Methods— Last In First Out (LIFO) .....	2.13
Valuation Methods— First In First Out (FIFO) .....	2.15
Valuation Methods— Actual .....	2.16
Valuation Method and Profitability .....	2.17
Valuation Methods Restrictions .....	2.18
Other Current Assets .....	2.19
Fixed Assets .....	2.20
Property .....	2.20
Buildings .....	2.21
Equipment .....	2.22
Straight Line Depreciation .....	2.22
Salvage Value of Equipment .....	2.24
Possible Extra Costs Associated with Equipment .....	2.25
Accelerated Depreciation .....	2.26
Actual Use Depreciation .....	2.27
Intangible Assets .....	2.27
Amortization of Intangible Assets .....	2.28
Value Determination for Patents .....	2.28
Value Determination for Copyrights and Trademarks .....	2.29

*Table of Contents* .....

---

Other Long-Term Assets .....	2.29
Liabilities .....	2.31
Short-Term Liabilities .....	2.31
Accounts Payable .....	2.31
Short-Term Debt .....	2.32
Accrued Liabilities .....	2.33
Long-Term Debt .....	2.34
Other Long-Term Debt .....	2.35
Shareholders' Equity .....	2.36
Stock .....	2.36
Retained Earnings .....	2.37
Section Summary .....	2.40

**Section 3**  
**Cash Flow Statement**

Section Objectives .....	3.1
Introduction .....	3.1
Accounting Practices .....	3.3
Cash Accounting .....	3.3
Accrual Accounting .....	3.3
Net Cash Flow .....	3.6
Cash Inflow and Outflow .....	3.9
Operations .....	3.10
Net Income .....	3.10
Adjustments .....	3.10
Depreciation .....	3.10
Effect of Depreciation on Pretax Income .....	3.11
Effect on Cash Flow of Amount of Depreciation Taken .....	3.13
Effect of the Sale of an Asset on Cash Flow .....	3.15
Amortization .....	3.19
Accounts Receivable Change .....	3.20
Inventory Change .....	3.21
Accounts Payable Change .....	3.22
Investments .....	3.23
Capital Expenditures .....	3.23
Short-term Investments .....	3.24

*Table of Contents* .....

---

Financing .....	3.25
New Debt .....	3.25
Stock Sales .....	3.26
Dividends .....	3.26
Net Cash Inflow/Outflow .....	3.27
Prepare a Cash Flow Statement .....	3.28
Operations .....	3.29
Net Income .....	3.29
Adjustments .....	3.29
Depreciation .....	3.29
Change in Accounts Receivable .....	3.30
Change in Inventory .....	3.30
Change in Other Current Assets .....	3.32
Change in Accounts Payable .....	3.32
Cash From (Used for) Operations .....	3.33
Investments .....	3.35
Capital Expenditures .....	3.35
Short-term Investments .....	3.35
Cash From/Used for Investments .....	3.36
Financing .....	3.36
Net Cash Inflow (Outflow) .....	3.37
Interpret Information on a Cash Flow Statement .....	3.39
Quick Observations .....	3.39
Broader Picture .....	3.39
Analyze How Cash Is Generated and Used .....	3.40
Accounts Receivable .....	3.42
Inventory .....	3.42
Accounts Payable .....	3.43
Cash Flow Statement Formats .....	3.46
Notes to Consolidated Financial Statements .....	3.48
Financial Report Information and Business Decisions .....	3.50
Applying What You Have Learned .....	3.55
Summary .....	3.57

*Table of Contents* .....

---

**Review Exercise**

Objectives ..... R1.1  
Questions ..... R1.1

**Appendix**

Enlarged Copy of Figure 3.8 ..... A.1