

Contents in brief

Preface to the fourth edition	xx
Guided tour of the book	xxvi

FINANCIAL ACCOUNTING

Part 1 A conceptual framework: setting the scene	3
1 Who needs accounting?	4
2 A systematic approach to financial reporting: the accounting equation	26
3 Financial statements from the accounting equation	50
4 Ensuring the quality of financial statements	73
Part 2 Reporting the transactions of a business	101
5 Accounting information for service businesses	102
6 Accounting information for trading businesses	131
Part 3 Recognition in financial statements	157
7 Published financial statements	158
8 Non-current (fixed) assets	196
9 Current assets	234
10 Current liabilities	263
11 Provisions and non-current (long-term) liabilities	282
12 Ownership interest	304
Part 4 Analysis and issues in reporting	333
13 Ratio analysis	334
14 Reporting corporate performance	361
15 Reporting cash flows	393

MANAGEMENT ACCOUNTING

Part 5 Setting the scene and defining the basic tools of management accounting	421
16 Functions of management accounting	422
17 Classification of costs	447
18 Product costs: materials, labour and overheads	469

Part 6 Product costs and stock valuation	505
19 Job costing	506
Part 7 Decision making	529
20 Breakeven analysis and short-term decision making	530
Part 8 Planning and control	559
21 Preparing a budget	560
22 Standard costs	598
23 Performance evaluation and feedback reporting	628
Part 9 Capital investment appraisal and business strategy	651
24 Capital investment appraisal	652
25 Business strategy and management accounting	682
Financial accounting terms defined	G1
Management accounting terms defined	G11
Appendices	
I Information extracted from annual report of Safe and Sure plc, used throughout Financial Accounting	A1
II Solutions to numerical and technical questions in Financial Accounting	A15
III Solutions to numerical and technical questions in Management Accounting	A39
Index	I1

Contents

Preface to the fourth edition	xx
Guided tour of the book	xxvi
Publisher's acknowledgements	xxviii

FINANCIAL ACCOUNTING

Part 1 A conceptual framework: setting the scene

Chapter 1 Who needs accounting?	4
Real World Case	4
Learning outcomes	5
1.1 Introduction	5
1.2 The development of a conceptual framework	7
1.3 Framework for the preparation and presentation of financial statements	8
1.4 Types of business entity	8
1.5 Users and their information needs	12
1.6 General purpose or specific purpose financial statements?	17
1.7 Stewards and agents	17
1.8 Who needs financial statements?	18
1.9 Summary	19
Further reading	20
Questions	20
A Test your understanding	20
B Application	21
C Problem solving and evaluation	21
Activities for study groups	22
Notes and references	22
Supplement: Introduction to the terminology of business transactions	24
Test your understanding	25
Chapter 2 A systematic approach to financial reporting: the accounting equation	26
Real World Case	26
Learning outcomes	27
2.1 Introduction	28
2.2 The accounting equation	28

2.3	Defining assets	29
2.4	Examples of assets	31
2.5	Recognition of assets	33
2.6	Defining liabilities	35
2.7	Examples of liabilities	36
2.8	Recognition of liabilities	37
2.9	Defining the ownership interest	39
2.10	Recognition	39
2.11	Changes in the ownership interest	39
2.12	Assurance for users of financial statements	41
2.13	Summary	42
	Further reading	44
	Questions	44
A	Test your understanding	44
B	Application	45
C	Problem solving and evaluation	45
	Activities for study groups	46
	Notes and references	46
	Supplement: Debit and credit bookkeeping	47
	Test your understanding	49
Chapter 3	Financial statements from the accounting equation	50
	Real World Case	50
	Learning outcomes	51
3.1	Introduction	51
3.2	Who is in charge of the accounting rules?	52
3.3	The accounting period	52
3.4	The balance sheet	53
3.5	The income statement (profit and loss account)	57
3.6	The cash flow statement	59
3.7	Usefulness of financial statements	62
3.8	Summary	63
	Questions	63
A	Test your understanding	63
B	Application	64
	Activities for study groups	65
	Supplement: Using the accounting equation to analyse transactions	66
	Test your understanding	72
Chapter 4	Ensuring the quality of financial statements	73
	Real World Case	73
	Learning outcomes	74
4.1	Introduction	75
4.2	Qualitative characteristics of financial statements	75
4.3	Measurement in financial statements	79
4.4	Views on prudence	82

4.5 Regulation of financial reporting	84
4.6 Reviewing published financial statements	92
4.7 Summary	97
Further reading	98
Questions	98
A Test your understanding	98
B Application	99
C Problem solving and evaluation	99
Activities for study groups	100
Notes and references	100

Part 2 Reporting the transactions of a business

Chapter 5 Accounting information for service businesses	102
Real World Case	102
Learning outcomes	103
5.1 Introduction	103
5.2 Analysing transactions using the accounting equation	104
5.3 Illustration of accounting for a service business	107
5.4 A process for summarising the transactions: a spreadsheet	111
5.5 Financial statements as a means of communication	113
5.6 Summary	116
Questions	116
A Test your understanding	116
B Application	117
Supplement: Recording transactions in ledger accounts – a service business	118
Test your understanding	130
Chapter 6 Accounting information for trading businesses	131
Real World Case	131
Learning outcomes	132
6.1 Introduction	133
6.2 Goods purchased for resale	133
6.3 Manufacturing goods for resale	135
6.4 Illustration of accounting for a trading business	138
6.5 A process for summarising the transactions: a spreadsheet	142
6.6 Financial statements of M. Carter, wholesaler	144
6.7 Summary	146
Questions	147
A Test your understanding	147
B Application	148
Supplement: Recording transactions in ledger accounts: a trading business	149
Test your understanding	156

Part 3 Recognition in financial statements

Chapter 7 Published financial statements	158
Real World Case	158
Learning outcomes	160
7.1 Introduction	160
7.2 International influences	161
7.3 Accounting framework	162
7.4 Balance sheet	166
7.5 Income statement (profit and loss account)	171
7.6 Cash flow statement	173
7.7 Group structure of companies	177
7.8 Group financial statements	179
7.9 Beyond the annual report	182
7.10 Summary	186
Further reading	187
Useful websites	187
Questions	187
A Test your understanding	187
B Application	189
C Problem solving and evaluation	189
Activities for study groups	189
Notes and references	190
Supplement 7.1: Information to be presented on the face of the Balance Sheet, as required by IAS 1	191
Supplement 7.2: Balance sheet format 1, as prescribed by the Companies Act 1985	192
Supplement 7.3: Information to be presented on the face of the Income Statement as required by IAS 1	194
Supplement 7.4: UK Companies Act: Profit and loss account format 1 – list of contents	195
Chapter 8 Non-current (fixed) assets	196
Real World Case	196
Learning outcomes	197
8.1 Introduction	198
8.2 Definitions	198
8.3 Recognition	200
8.4 Users' needs for information	202
8.5 Information provided in the financial statements	203
8.6 Usefulness of published information	205
8.7 Depreciation: an explanation of its nature	206
8.8 Reporting non-current (fixed) assets and depreciation in financial statements	211
8.9 Summary	219

Further reading	220
Questions	220
A Test your understanding	220
B Application	221
C Problem solving and evaluation	221
Activities for study groups	222
Notes and references	223
Supplement: Recording non-current (fixed) assets and depreciation	224
Test your understanding	233
Chapter 9 Current assets	234
Real World Case	234
Learning outcomes	236
9.1 Introduction	236
9.2 Definitions	236
9.3 The working capital cycle	237
9.4 Recognition	238
9.5 Users' needs for information	241
9.6 Information provided in the financial statements	242
9.7 Measurement and recording	244
9.8 Inventories (stocks) of raw materials and finished goods	245
9.9 Receivables (debtors)	249
9.10 Prepayments	251
9.11 Revenue recognition	252
9.12 Summary	254
Questions	254
A Test your understanding	255
B Application	255
C Problem solving and evaluation	256
Activities for study groups	257
Notes and references	257
Supplement: Bookkeeping entries for (a) bad and doubtful debts; and (b) prepayments	258
Test your understanding	262
Chapter 10 Current liabilities	263
Real World Case	263
Learning outcomes	264
10.1 Introduction	264
10.2 Definitions	265
10.3 Recognition	266
10.4 Users' needs for information	267
10.5 Information provided in the financial statements	268
10.6 Measurement and recording	269
10.7 Accruals and the matching concept	271
10.8 Liabilities for taxation	274
10.9 Summary	275

Questions	276
A Test your understanding	276
B Application	276
C Problem solving and evaluation	277
Activities for study groups	277
Notes and references	278
Supplement: Bookkeeping entries for accruals	279
Test your understanding	281
Chapter 11 Provisions and non-current (long-term) liabilities	282
Real World Case	282
Learning outcomes	283
11.1 Introduction	284
11.2 Users' needs for information	285
11.3 Information provided in the financial statements	285
11.4 Provisions	288
11.5 Deferred income	291
11.6 Non-current (long-term) liabilities	292
11.7 Summary	298
Questions	299
A Test your understanding	299
B Application	299
C Problem solving and evaluation	300
Activities for study groups	301
Notes and references	301
Supplement: Bookkeeping entries for provisions and deferred income	302
Test your understanding	303
Chapter 12 Ownership interest	304
Real World Case	304
Learning outcomes	305
12.1 Introduction	306
12.2 Definition and recognition	306
12.3 Presentation of ownership interest	307
12.4 Additional primary financial statements	314
12.5 Users' needs for information	315
12.6 Information provided in the financial statements	315
12.7 Dividends	319
12.8 Issue of further shares on the Stock Exchange	320
12.9 Summary	323
Questions	324
A Test your understanding	324
B Application	324
C Problem solving and evaluation	325
Activities for study groups	327
Notes and references	327
Supplement: A spreadsheet for adjustment to a trial balance at the end of the accounting period	328
Test your understanding	332

Part 4 Analysis and issues in reporting

Chapter 13 Ratio analysis	334
Real World Case	334
Learning outcomes	335
13.1 Introduction	335
13.2 A note on terminology	336
13.3 Systematic approach to ratio analysis	336
13.4 Investors' views on risk and return	343
13.5 Pyramid of ratios	346
13.6 Use and limitations of ratio analysis	347
13.7 Worked example of ratio analysis	348
13.8 Linking ratios to the cash flow statement	354
13.9 Summary	357
Questions	357
A Test your understanding	358
B Application	358
C Problem solving and evaluation	360
Chapter 14 Reporting corporate performance	361
Real World Case	361
Learning outcomes	363
14.1 Introduction	363
14.2 Operating and Financial Review (OFR)	363
14.3 Other guidance in analysis	367
14.4 Segmental information	371
14.5 Off-balance sheet finance	376
14.6 Corporate social responsibility	377
14.7 Corporate governance	380
14.8 Developing issues: 'Present fairly' and 'true and fair view'	381
14.9 Measurement of value	384
14.10 Developing issues: How valid is the stakeholder model	387
14.11 Summary	387
Questions	389
A Test your understanding	389
B Application	390
C Problem solving and evaluation	390
Activities for study groups	390
Notes and references	391
Chapter 15 Reporting cash flows	393
Real World Case	393
Learning outcomes	394
15.1 Introduction	394
15.2 Cash and cash equivalents	395
15.3 The direct method and the indirect method	395
15.4 Preparing a cash flow statement: the indirect method	399
15.5 Preparing a cash flow statement: the direct method	407

15.6 Interpretation of cash flow information	408
15.7 Illustration	408
15.8 Summary	413
Further reading	413
Questions	413
A Test your understanding	414
B Application	414
C Problem solving and evaluation	415
Notes and references	417

MANAGEMENT ACCOUNTING

Part 5 Setting the scene and defining the basic tools of management accounting

Chapter 16 Functions of management accounting	422
Real World Case	422
Learning outcomes	423
16.1 Introduction	424
16.2 Meeting the needs of internal users	426
16.3 Management functions	427
16.4 Role of management accounting	432
16.5 Judgements and decisions: case study illustrations	435
16.6 The language of management accounting	440
16.7 Summary	441
Further reading	441
Questions	441
A Test your understanding	441
B Application	442
C Problem solving and evaluation	443
Cases for study groups	446
Notes and references	446
Chapter 17 Classification of costs	447
Real World Case	447
Learning outcomes	448
17.1 Definition of a cost	448
17.2 The need for cost classification	449
17.3 The meaning of 'activity' and 'output'	449
17.4 Variable costs and fixed costs	450
17.5 Direct costs and indirect costs	454
17.6 Product costs and period costs	456
17.7 Cost classification for planning, decision making and control	458
17.8 Cost coding	461
17.9 Cost selection and reporting	462
17.10 Summary	463
Further reading	464

Questions	464
A Test your understanding	464
B Application	465
C Problem solving and evaluation	467
Cases for study groups	467

Chapter 18 Product costs: materials, labour and overheads 469

Real World Case	469
Learning outcomes	470
18.1 Introduction	471
18.2 Accounting for materials costs	472
18.3 Accounting for labour costs	476
18.4 Production overheads: traditional approach	478
18.5 Activity-based costing (ABC) for production overheads	488
18.6 Comparing traditional approach and ABC	496
18.7 Summary	498
Further reading	499
Questions	499
A Test your understanding	499
B Application	500
C Problem solving and evaluation	502
Cases for study groups	503
Notes and references	503

Part 6 Job costs and stock valuation

Chapter 19 Job costing 506

Real World Case	506
Learning outcomes	507
19.1 Introduction	507
19.2 Job cost records: an illustration	509
19.3 Job costing: applying the accounting equation to transactions	512
19.4 Absorption costing and marginal costing	517
19.5 Moving forward	521
19.6 Summary	522
Questions	523
A Test your understanding	524
B Application	524
C Problem solving and evaluation	526
Cases for study groups	527

Part 7 Decision making

Chapter 20 Breakeven analysis and short-term decision making 530

Real World Case	530
Learning outcomes	531

20.1	Introduction	532
20.2	Cost behaviour: fixed and variable costs	532
20.3	Breakeven analysis	537
20.4	Using breakeven analysis	540
20.5	Limitations of breakeven analysis	543
20.6	Applications of cost-volume-profit analysis	543
20.7	Cases in short-term decision making	545
20.8	Pricing decisions	550
20.9	Summary	552
	Questions	553
A	Test your understanding	553
B	Application	554
C	Problem solving and evaluation	555
	Cases for study groups	556

Part 8 Planning and control

Chapter 21	Preparing a budget	560
	Real World Case	560
	Learning outcomes	561
21.1	Introduction	562
21.2	Purpose and nature of a budget system	562
21.3	Administration of the budgetary process	565
21.4	The benefits of budgeting	569
21.5	Behavioural aspects of budgeting	572
21.6	Approaches to budgeting	575
21.7	Practical example – development of a budget	577
21.8	Shorter budget periods	587
21.9	Summary	590
	Questions	591
A	Test your understanding	591
B	Application	592
C	Problem solving and evaluation	594
	Cases for study groups	597
Chapter 22	Standard costs	598
	Real World Case	598
	Learning outcomes	599
22.1	Introduction	600
22.2	Purpose of using standard costs	600
22.3	The level of output to be used in setting standards	601
22.4	The control process	602
22.5	Direct materials cost variance	603
22.6	Direct labour cost variance	605
22.7	Variable overhead cost variance	606
22.8	Fixed overhead expenditure variance	607
22.9	Case study: Allerdale Ltd	607

22.10	Investigating variances	612
22.11	Flexible budgets and variance analysis	613
22.12	Case study: Brackendale Ltd	614
22.13	Is variance analysis, based on standard costs, a useful exercise?	618
22.14	A broader view of applications of variance analysis	619
22.15	Summary	620
	Questions	620
A	Test your understanding	621
B	Application	621
C	Problem solving and evaluation	624
	Cases for study groups	626
	Notes and references	627

Chapter 23 Performance evaluation and feedback reporting 628

	Real World Case	628
	Learning outcomes	629
23.1	Introduction	629
23.2	Preparing performance reports	631
23.3	Performance evaluation	632
23.4	Benchmarking	637
23.5	Non-financial performance measures	638
23.6	The balanced scorecard	640
23.7	Management use of performance measurement	642
23.8	Summary	644
	Further reading	645
	Questions	645
A	Test your understanding	645
B	Application	646
C	Problem solving and evaluation	646
	Cases for study groups	649

Part 9 Capital investment appraisal and business strategy

Chapter 24 Capital investment appraisal 652

	Real World Case	652
	Learning outcomes	653
24.1	Purpose of capital investment appraisal	654
24.2	Payback method	656
24.3	Accounting rate of return	658
24.4	Net present value method	660
24.5	Internal rate of return	665
24.6	Mutually exclusive projects	668
24.7	Which methods are used in practice?	670
24.8	Control of investment projects: authorisation and review	671
24.9	Advanced manufacturing technologies	672
24.10	Summary	673
	Further reading	674

Questions	674
A Test your understanding	674
B Application	675
C Problem solving and evaluation	676
Cases for study groups	679
Supplement: Table of discount factors	680
Chapter 25 Business strategy and management accounting	682
Real World Case	682
Learning outcomes	683
25.1 Introduction	683
25.2 Strategic management accounting	684
25.3 The just-in-time approach	685
25.4 Value chain analysis	686
25.5 Total quality management and cost of quality	687
25.6 Business process re-engineering	688
25.7 E-business and e-commerce	689
25.8 Summary	692
Further reading	692
Questions	693
A Test your understanding	693
B Application	693
C Problem solving and evaluation	694
Cases for study groups	694
Note and reference	694
Financial accounting terms defined	G1
Management accounting terms defined	G11
Appendices	
I Information extracted from annual report of Safe and Sure Group plc, used throughout Financial Accounting	A1
II Solutions to numerical and technical questions in Financial Accounting	A15
III Solutions to numerical and technical questions in Management Accounting	A39
Index	11