

# Financial Accounting

with International Financial Reporting Standards

**Fourth Edition**

**JERRY J. WEYGANDT PhD, CPA**

University of Wisconsin—Madison  
Madison, Wisconsin

**PAUL D. KIMMEL PhD, CPA**

University of Wisconsin—Milwaukee  
Milwaukee, Wisconsin

**DONALD E. KIESO PhD, CPA**

Northern Illinois University  
DeKalb, Illinois

**WILEY**

# Contents

## 1 Accounting in Action 1-1

---

- Knowing the Numbers* 1-1
- Accounting Activities and Users** 1-3
  - Three Activities 1-3
  - Who Uses Accounting Data 1-4
- The Building Blocks of Accounting** 1-6
  - Ethics in Financial Reporting 1-6
  - Accounting Standards 1-7
  - Measurement Principles 1-8
  - Assumptions 1-8
- The Accounting Equation** 1-10
  - Assets 1-11
  - Liabilities 1-11
  - Equity 1-11
- Analyzing Business Transactions** 1-13
  - Accounting Transactions 1-13
  - Transaction Analysis 1-14
  - Summary of Transactions 1-19
- Financial Statements** 1-20
  - Income Statement 1-22
  - Retained Earnings Statement 1-22
  - Statement of Financial Position 1-22
  - Statement of Cash Flows 1-23
  - Comprehensive Income Statement 1-23
- Appendix 1A: Career Opportunities in Accounting** 1-25
  - Public Accounting 1-25
  - Private Accounting 1-26
  - Governmental Accounting 1-26
  - Forensic Accounting 1-26
  - A Look at U.S. GAAP* 1-46

## 2 The Recording Process 2-1

---

- Accidents Happen: Bank of Taiwan* 2-1
- Accounts, Debits, and Credits** 2-2
  - The Account 2-2
  - Debits and Credits 2-3
  - Equity Relationships 2-6
  - Summary of Debit/Credit Rules 2-6
- The Journal** 2-7
  - The Recording Process 2-7
  - The Journal 2-8
- The Ledger and Posting** 2-10
  - The Ledger 2-10
  - Posting 2-12
  - Chart of Accounts 2-13
  - The Recording Process Illustrated 2-13

- Summary Illustration of Journalizing and Posting 2-19
- The Trial Balance** 2-21
  - Limitations of a Trial Balance 2-22
  - Locating Errors 2-22
  - Currency Signs and Underlining 2-22
  - A Look at U.S. GAAP* 2-46

## 3 Adjusting the Accounts 3-1

---

- What Was Your Profit?: Cadbury* 3-1
- Accrual-Basis Accounting and Adjusting Entries** 3-2
  - Fiscal and Calendar Years 3-3
  - Accrual- versus Cash-Basis Accounting 3-3
  - Recognizing Revenues and Expenses 3-3
  - The Need for Adjusting Entries 3-5
  - Types of Adjusting Entries 3-5
- Adjusting Entries for Deferrals** 3-6
  - Prepaid Expenses 3-6
  - Unearned Revenues 3-10
- Adjusting Entries for Accruals** 3-13
  - Accrued Revenues 3-13
  - Accrued Expenses 3-14
  - Summary of Basic Relationships 3-17
- Adjusted Trial Balance and Financial Statements** 3-20
  - Preparing the Adjusted Trial Balance 3-21
  - Preparing Financial Statements 3-21
- Appendix 3A: Alternative Treatment of Deferrals** 3-24
  - Prepaid Expenses 3-25
  - Unearned Revenues 3-26
  - Summary of Additional Adjustment Relationships 3-27
- Appendix 3B: Financial Reporting Concepts** 3-28
  - Qualities of Useful Information 3-28
  - Assumptions in Financial Reporting 3-28
  - Principles in Financial Reporting 3-29
  - Cost Constraint 3-30
  - A Look at U.S. GAAP* 3-56

## 4 Completing the Accounting Cycle 4-1

---

- Speaking the Same Language: IASB* 4-1
- The Worksheet** 4-3
  - Steps in Preparing a Worksheet 4-3
  - Preparing Financial Statements from a Worksheet 4-10
  - Preparing Adjusting Entries from a Worksheet 4-11
- Closing the Books** 4-11
  - Preparing Closing Entries 4-12

Posting Closing Entries	4-14
Preparing a Post-Closing Trial Balance	4-16
<b>The Accounting Cycle and Correcting Entries</b>	<b>4-19</b>
Summary of the Accounting Cycle	4-19
Reversing Entries—An Optional Step	4-19
Correcting Entries—An Avoidable Step	4-19
<b>Classified Statement of Financial Position</b>	<b>4-23</b>
Intangible Assets	4-24
Property, Plant, and Equipment	4-25
Long-Term Investments	4-25
Current Assets	4-25
Equity	4-26
Non-Current Liabilities	4-27
Current Liabilities	4-27
<b>Appendix 4A: Reversing Entries</b>	<b>4-29</b>
Reversing Entries Example	4-29
<i>A Look at U.S. GAAP</i>	4-57

## 5 Accounting for Merchandise Operations 5-1

<i>Who Doesn't Shop?: Carrefour</i>	5-1
<b>Merchandising Operations and Inventory Systems</b>	<b>5-3</b>
Operating Cycles	5-3
Flow of Costs	5-4
<b>Recording Purchases Under a Perpetual System</b>	<b>5-6</b>
Freight Costs	5-8
Purchase Returns and Allowances	5-9
Purchase Discounts	5-9
Summary of Purchasing Transactions	5-10
<b>Recording Sales Under a Perpetual System</b>	<b>5-11</b>
Sales Returns and Allowances	5-12
Sales Discounts	5-13
<b>The Accounting Cycle for a Merchandising Company</b>	<b>5-14</b>
Adjusting Entries	5-15
Closing Entries	5-15
Summary of Merchandising Entries	5-16
<b>Financial Statements for a Merchandiser</b>	<b>5-17</b>
Income Statement	5-17
Classified Statement of Financial Position	5-21
<b>Appendix 5A: Worksheet for a Merchandising Company</b>	<b>5-23</b>
Using a Worksheet	5-23
<b>Appendix 5B: Periodic Inventory System</b>	<b>5-24</b>
Determining Cost of Goods Sold Under a Periodic System	5-25
Recording Merchandise Transactions	5-25
Recording Purchases of Merchandise	5-26
Recording Sales of Merchandise	5-27
Journalizing and Posting Closing Entries	5-27
Using a Worksheet	5-29
<i>A Look at U.S. GAAP</i>	5-54

## 6 Inventories 6-1

<i>"Where Is That Spare Bulldozer Blade?": Komatsu</i>	6-1
<b>Classifying and Determining Inventory</b>	<b>6-2</b>
Classifying Inventory	6-2
Determining Inventory Quantities	6-4
<b>Inventory Methods and Financial Effects</b>	<b>6-6</b>
Specific Identification	6-7
Cost Flow Assumptions	6-7
Financial Statement and Tax Effects of Cost Flow Methods	6-11
Using Inventory Cost Flow Methods Consistently	6-12
<b>Effects of Inventory Errors</b>	<b>6-13</b>
Income Statement Effects	6-13
Statement of Financial Position Effects	6-14
<b>Inventory Statement Presentation and Analysis</b>	<b>6-15</b>
Presentation	6-15
Lower-of-Cost-or-Net Realizable Value	6-15
Analysis	6-16
<b>Appendix 6A: Inventory Cost Flow Methods in Perpetual Inventory Systems</b>	<b>6-18</b>
First-In, First-Out (FIFO)	6-18
Average-Cost	6-19
<b>Appendix 6B: Estimating Inventories</b>	<b>6-19</b>
Gross Profit Method	6-20
Retail Inventory Method	6-21
<b>Appendix 6C: LIFO Inventory Method</b>	<b>6-22</b>
<i>A Look at U.S. GAAP</i>	6-44

## 7 Fraud, Internal Control, and Cash 7-1

<i>Minding the Money at Nick's: Nick's Steakhouse and Pizza</i>	7-1
<b>Fraud and Internal Control</b>	<b>7-2</b>
Fraud	7-3
Internal Control	7-3
Principles of Internal Control Activities	7-4
Limitations of Internal Control	7-10
<b>Cash Controls</b>	<b>7-10</b>
Cash Receipts Controls	7-11
Cash Disbursements Controls	7-13
Petty Cash Fund	7-15
<b>Control Features of a Bank Account</b>	<b>7-18</b>
Making Bank Deposits	7-18
Writing Checks	7-19
Electronic Funds Transfer (EFT) System	7-20
Bank Statements	7-20
Reconciling the Bank Account	7-21
<b>Reporting Cash</b>	<b>7-26</b>

Cash Equivalents 7-26  
Restricted Cash 7-26  
*A Look at U.S. GAAP* 7-46

## 8 Accounting for Receivables 8-1

---

*Are You Going to Pay Me—or Not?: BNP Paribas* 8-1  
**Recognition of Accounts Receivable** 8-2  
Types of Receivables 8-3  
Recognizing Accounts Receivable 8-3  
**Valuation and Disposition of Accounts Receivable** 8-5  
Valuing Accounts Receivable 8-5  
Disposing of Accounts Receivable 8-11  
**Notes Receivable** 8-13  
Determining the Maturity Date 8-14  
Computing Interest 8-15  
Recognizing Notes Receivable 8-15  
Valuing Notes Receivable 8-16  
Disposing of Notes Receivable 8-16  
**Presentation and Analysis** 8-18  
Presentation 8-19  
Analysis 8-19  
*A Look at U.S. GAAP* 8-38

## 9 Plant Assets, Natural Resources, and Intangible Assets 9-1

---

*How Much for a Ride to the Beach?: Rent-A-Wreck* 9-1  
**Plant Asset Expenditures** 9-2  
Determining the Cost of Plant Assets 9-3  
Expenditures During Useful Life 9-5  
**Depreciation Methods** 9-7  
Factors in Computing Depreciation 9-8  
Depreciation Methods 9-8  
Component Depreciation 9-13  
Depreciation and Income Taxes 9-13  
Revaluation of Plant Assets 9-13  
Revising Periodic Depreciation 9-14  
**Plant Asset Disposals** 9-15  
Retirement of Plant Assets 9-16  
Sale of Plant Assets 9-16  
**Natural Resources and Intangible Assets** 9-18  
Natural Resources and Depletion 9-18  
Intangible Assets 9-20  
**Statement Presentation and Analysis** 9-23  
Presentation 9-23  
Analysis 9-24  
**Appendix 9A: Exchange of Plant Assets** 9-24  
Loss Treatment 9-25  
Gain Treatment 9-25  
*A Look at U.S. GAAP* 9-47

## 10 Current Liabilities 10-1

---

*Financing His Dreams: Wilbert Murdock* 10-1  
**Accounting for Current Liabilities** 10-2  
What Is a Current Liability? 10-2  
Notes Payable 10-3  
Value-Added and Sales Taxes Payable 10-4  
Unearned Revenues 10-5  
Salaries and Wages 10-5  
Current Maturities of Long-Term Debt 10-7  
**Reporting and Analyzing Current Liabilities** 10-8  
Reporting Uncertainty 10-8  
Reporting of Current Liabilities 10-9  
Analysis of Current Liabilities 10-10  
*A Look at U.S. GAAP* 10-26

## 11 Non-Current Liabilities 11-1

---

*Are We Living on Borrowed Time?* 11-1  
**Overview of Bonds** 11-2  
Types of Bonds 11-3  
Issuing Procedures 11-3  
Bond Trading 11-3  
Determining the Market Price of a Bond 11-4  
**Bond Transactions** 11-6  
Issuing Bonds at Face Value 11-6  
Discount or Premium on Bonds 11-7  
Issuing Bonds at a Discount 11-8  
Issuing Bonds at a Premium 11-9  
Redeeming Bonds 11-10  
**Accounting for Non-Current Liabilities** 11-11  
Long-Term Notes Payable 11-11  
Lease Liabilities 11-13  
**Reporting and Analyzing Non-Current Liabilities** 11-14  
Presentation 11-14  
Analysis 11-14  
Debt and Equity Financing 11-15  
**Appendix 11A: Effective-Interest Method of Bond Amortization** 11-17  
Amortizing Bond Discount 11-17  
Amortizing Bond Premium 11-19  
**Appendix 11B: Straight-Line Amortization** 11-20  
Amortizing Bond Discount 11-20  
Amortizing Bond Premium 11-21  
*A Look at U.S. GAAP* 11-38

## 12 Corporations: Organization, Share Transactions, and Equity 12-1

---

*To the Victor Go the Spoils: adidas* 12-1  
**The Corporate Form of Organization** 12-2  
Characteristics of a Corporation 12-3

Forming a Corporation	12-5
Shareholder Rights	12-5
Share Issue Considerations	12-7
Corporate Capital	12-9
<b>Accounting for Share Transactions</b>	<b>12-10</b>
Accounting for Ordinary Shares	12-10
Accounting for Preference Shares	12-12
Accounting for Treasury Shares	12-13
<b>Dividends and Splits</b>	<b>12-16</b>
Accounting for Cash Dividends	12-17
Dividend Preferences	12-18
Accounting for Share Dividends	12-21
Accounting for Share Splits	12-23
<b>Reporting and Analyzing Equity</b>	<b>12-24</b>
Retained Earnings	12-24
Presentation of Statement of Financial Position	12-26
Analysis	12-27
<b>Appendix 12A: Statement of Changes in Equity</b>	<b>12-28</b>
<b>Appendix 12B: Book Value—Another per Share Amount</b>	<b>12-29</b>
Book Value per Share	12-29
Book Value versus Market Price	12-30
<i>A Look at U.S. GAAP</i>	12-55

## 13 Investments 13-1

---

<i>Playing for Fun and Profit: Sony</i>	13-1
<b>Debt Investments</b>	<b>13-2</b>
Why Companies Invest	13-2
Accounting for Debt Investments	13-4
<b>Share Investments</b>	<b>13-6</b>
Holdings of Less than 20%	13-6
Holdings Between 20% and 50%	13-7
Holdings of More than 50%	13-8
<b>Valuing and Reporting Investments</b>	<b>13-10</b>
Categories of Securities	13-10
Statement of Financial Position Presentation	13-16
Presentation of Realized and Unrealized Gain or Loss	13-17
Classified Statement of Financial Position	13-17
<b>Appendix 13A: Preparing Consolidated Financial Statements</b>	<b>13-19</b>
Consolidated Statement of Financial Position	13-19
Consolidated Income Statement	13-23
<i>A Look at U.S. GAAP</i>	13-40

## 14 Statement of Cash Flows 14-1

---

<i>What Should We Do with This Cash?: Keyence</i>	14-1
<b>Statement of Cash Flows: Usefulness and Format</b>	<b>14-3</b>
Usefulness of the Statement of Cash Flows	14-3
Classification of Cash Flows	14-3

Significant Non-Cash Activities	14-5
Format of the Statement of Cash Flows	14-5
<b>Preparing the Statement of Cash Flows—Indirect Method</b>	<b>14-7</b>
Indirect and Direct Methods	14-8
Indirect Method—Computer Services	14-8
International	14-8
Step 1: Operating Activities	14-9
Summary of Conversion to Net Cash Provided by Operating Activities—Indirect Method	14-12
Step 2: Investing and Financing Activities	14-13
Step 3: Net Change in Cash	14-14
<b>Using Cash Flows to Evaluate a Company</b>	<b>14-17</b>
Free Cash Flow	14-17
<b>Appendix 14A: Statement of Cash Flows—Direct Method</b>	<b>14-19</b>
Step 1: Operating Activities	14-21
Step 2: Investing and Financing Activities	14-25
Step 3: Net Change in Cash	14-26
<b>Appendix 14B: Statement of Cash Flows—T-Account Approach</b>	<b>14-26</b>
<i>A Look at U.S. GAAP</i>	14-50

## 15 Financial Analysis: The Big Picture 15-1

---

<i>Making Money the Old-Fashioned Way: Li Ka-shing</i>	15-1
<b>Basics of Financial Statement Analysis</b>	<b>15-2</b>
Need for Comparative Analysis	15-3
Tools of Analysis	15-3
Horizontal Analysis	15-3
Vertical Analysis	15-6
<b>Ratio Analysis</b>	<b>15-9</b>
Liquidity Ratios	15-9
Profitability Ratios	15-13
Solvency Ratios	15-16
Summary of Ratios	15-18
<b>Sustainable Income</b>	<b>15-20</b>
Discontinued Operations	15-21
Changes in Accounting Principle	15-22
Comprehensive Income	15-22
<i>A Look at U.S. GAAP</i>	15-48

<b>Appendix A Specimen Financial Statements: Taiwan Semiconductor Manufacturing Company, Limited</b>	<b>A-1</b>
--	------------

---

**Appendix B Specimen Financial Statements:**  
Nestlé SA **B-1**

---

**Appendix C Specimen Financial Statements: Delfi Limited** **C-1**

---

**Appendix D Specimen Financial Statements:**  
Apple Inc. **D-1**

---

**Appendix E Time Value of Money** **E-1**

---

**Interest and Future Values** **E-1**

Nature of Interest E-1

Future Value of a Single Amount E-3

Future Value of an Annuity E-5

**Present Value Concepts** **E-7**

Present Value Variables E-7

Present Value of a Single Amount E-7

Present Value of an Annuity E-9

Time Periods and Discounting E-11

Present Value of a Long-Term Note or Bond E-11

**Using Financial Calculators** **E-14**

Present Value of a Single Sum E-14

Present Value of an Annuity E-15

Useful Applications of the Financial Calculator E-16

**Appendix F Accounting for Partnerships** **F-1**

---

**Forming a Partnership** **F-2**

Characteristics of Partnerships F-2

Organizations with Partnership Characteristics F-3

Advantages and Disadvantages of Partnerships F-4

The Partnership Agreement F-5

Accounting for a Partnership Formation F-5

**Accounting for Net Income or Net Loss** **F-6**

Dividing Net Income or Net Loss F-6

Partnership Financial Statements F-9

**Liquidation of a Partnership** **F-10**

No Capital Deficiency F-11

Capital Deficiency F-12

**Admissions and Withdrawals of Partners** **F-15**

Admission of a Partner F-15

Withdrawal of a Partner F-18

**Appendix G Subsidiary Ledgers and Special Journals** **G-1**

---

**Subsidiary Ledgers** **G-1**

Subsidiary Ledger Example G-2

Advantages of Subsidiary Ledgers G-3

**Special Journals** **G-4**

Sales Journal G-4

Cash Receipts Journal G-7

Purchases Journal G-10

Cash Payments Journal G-13

Effects of Special Journals on the General Journal G-15

Cybersecurity: A Final Comment G-16

**Company Index** **I-1**

**Subject Index** **I-3**