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Leita Hart-Fanta, CPA



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This book is dedicated to my generous, supportive, and loving husband Jeff. You are the best, baby!

About the Author

Leita Hart-Fanta is a certified public accountant, certified government financial manager, and certified government audit professional. She is the author of a number of self-study courses for CPAs and auditors on auditing and accounting topics, including generating cash flow, basic audit skills, and government auditing standards. She also has taught over 1,000 day-long seminars and is a frequent keynote speaker at CPA conferences. To find out more about her, visit her Web sites at www.auditskills.com, www.happycashflow.com, www.leitahart.com, and www.yellowbook-cpe.com.

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Acknowledgments

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By watching the light bulb go on or the light bulb go out on the faces of my students, I could tell whether I was on the right track or not. I thank them for their eagerness to learn and their thoughtful questions. The questions and live feedback taught me what nonaccountants want to know about accounting—but more importantly what they do not want to know about accounting. Thank you!

I also want to thank Susan Allen who gave me my first shot as a writing teacher and writing coach and believed that I could pull it off. Those first classes were rough, but she didn't fire me!

And lastly I want to thank my friend Michele Carlquist, who once said that I had potential and encouraged me to stick to my plan to write and teach over and over and over.

Introduction

Why Is Accounting Important?

I was out of school and had my CPA (certified public accountant) license for several years before all the debit and credit microdetail the professors stuffed into my brain started to make real sense. And only after teaching the language of accounting and finance to others did it really become clear. An old Japanese proverb instructs: “Those who want to learn must teach.” Very true in my case.

When I was asked questions, I was forced to take all my technical, detailed knowledge and distill it so that I could answer the question in an understandable and clear way. And that is what this book is all about—answering your questions in an understandable and clear way.

I don’t know why the professors choose to start the first week with a discussion of debits and credits. I have a sneaking suspicion that, at my alma mater at least, it was a way to weed out tentative, unsure students. You had to be pretty darn sure you wanted to be a business major to sit through and memorize all that stuff.

I am not going to put you through that experience. You bought this book hoping that I’d make the subject easy, and I am going to do everything I can to make it painless. I find that many learners like to start with the big picture first. Many like to know why they need to know something before they just memorize a bunch of rules. So in [Part I](#), debits and credits are mentioned only once. The emphasis is on grasping the big picture.

In [Part II](#), I go into more detail. There I discuss debits and credits and inventory valuation and exciting stuff like that. But I am not going to discuss obscure transactions such as the repurchase of preferred stock under stock option plans. (It is scary to just write that sentence!) I imagine that would entail more detail than 99 percent of the readers of this book need. If you want that sort of detail, please consult accounting standards [through the Financial Accounting Standards Board (FASB) and/or the Governmental Accounting Standards Board (GASB)], an accounting professor, or an advanced accounting text.

In [Part III](#), I discuss how financial information is used in business and various business information systems. There I cover budgeting and cost accounting and how those systems differ from general ledger or financial accounting. I also talk about how governmental and not-for-profit accounting has its own special way of doing things.

And in the last part, I take everything from the first three parts and perform a high-level financial analysis of two competitors and raise some interesting questions about their performance.

So we go from the big picture, to detail, to practical application.

Why Should You Learn This Stuff?

Good question! It might seem easier to just leave all this technical stuff up to someone else so that you can focus on your job. Maybe you are in marketing, sales, product design, administration, quality—anywhere but the finance and accounting department! You have successfully avoided the topic so far, but it just keeps coming up in meetings

and conversations. It is like a nagging grandmother—always there, always hoping you will call.

Not understanding the language of business and leaving money decisions in the hands of accountants are bad ideas for several reasons:

- Accountants don't know your job, the real goings-on of the business, as well as you do. They shouldn't tell you how things should be.
- Accountants might make bad decisions. I don't know how many times I hear managers complain of how they are being victimized by a stringent and unreasonable budget created by the accountant. Big mistake! The accountant shouldn't have created the budget; the manager should have done it.
- You are ultimately responsible for results. When things go well or go badly, it is you that upper management looks to. Accountants don't make sales, do marketing, or design new products; often, all they do is compile and report data. You'd do well to keep informed of what is going on financially so that you can answer tough questions or consciously bask in the praise.
- You want your career to go somewhere. Maybe you have noticed that the farther you move up the chain of command in your organization, the more you hear talk about money. If you can't talk the talk, you won't be promoted to walk the walk.
- Accountants and other financially savvy members of your team might be snowing or manipulating you. You might have a sneaking suspicion that things are going on that you don't know about because you don't know what you don't know. In other words, how can you ask about something you know nothing about? Information is power.
- You would like to stay engaged during management meetings where financial results are discussed. When computer experts talk to me, they can quickly tell that they have surpassed my level of understanding when I start nodding and smiling in a glazed manner. This does nothing to enhance my credibility or stature with that computer expert. Not knowing what is going on in finance can be a detriment to your credibility with upper management. Wouldn't it be nice to be able to participate in a discussion about money?
- Business is about making money. You might think it is about the product or marketing or sales. But it's all about money. The reason that you have a product and market and sell it is to make money. And accounting is the language of money.
- Accounting really isn't all that hard. It is just a system and a language. Hey, if I can learn it, so can you!

Accounting Is Just a System and a Language

You see, accounting is one of the oldest systems around for tracking data. In business, someone has always wanted to know how much money was made or lost. For centuries, accountants have kindly kept track of the dollars that flow in and out of organizations of all types.

The systems that have been set up to track this information can be—and I

emphasize *can* be—difficult to use and interpret. The debit and credit stuff can get pretty confusing. With a little effort, though, I know that you will be able to extract some information that will help you to make decisions about what to do next in your business.

For example, most accounting systems will spit out data on how much it costs to create a product or provide a service. Now why do we care about this? Because we must price our product or service for more than we spent to create it. Selling something for more than you put into it is called a *business*. Selling something for less than you put into it is called a *hobby*!

You also might want to know how well your sales staff is doing at pushing your latest gizmo. Your accounting system should be able to tell you volume of sales per salesperson as well as the customers to whom your salespeople are selling the gizmos. This can be very useful data if you want to determine who to reward and who to send back to sales school.

Some Accounting Systems Are Real Time and Very Detailed

Any basic accounting system will tell you simple things such as how much cash you took in today and how much you paid out today. Accounting systems track all the money that goes in and out of the business and categorizes the ins and outs into useful groups so that you can judge where the money came from and what it was used for. Bottom line:

All accounting is *a counting*.

But some businesses believe that accounting can and should do more for them. For this extra bit of tracking, for this extra counting effort, if you will, they pay in both time and money.

One Fortune 500 company invested a huge amount of time and effort into creating a daily accounting report that told how many products it was selling, how it was selling the products (by phone, by Internet, or in stores), and what kind of profit each product generated. The company decided that it was worth it to get immediate feedback on whether the bells and whistles it was offering its customers were selling. If they weren't selling, the company changed its offerings immediately. The company didn't want to waste a week, a month, or a quarter hawking low-demand goods. The accounting system gave the company the power to make decisions quickly.

In most decisions in business, an evaluation has to be made as to whether the cost is worth the resulting benefit. The same must be said of accounting. What is the information worth to you?

But before you can even make that decision, you need to know what kind of information a basic accounting system can provide, and you need to understand the terminology behind it.

I hate to tell you this, but accountants are not working at changing their tunes—or their terminology—any time soon. Mohammed (that's you) is going to have to go to the mountain (that's accounting terminology, information, and accountants). I am glad you have decided to take this journey with me. I will make the mountains into little, tiny, bumpy hills for you.

Part I
The Big Picture