

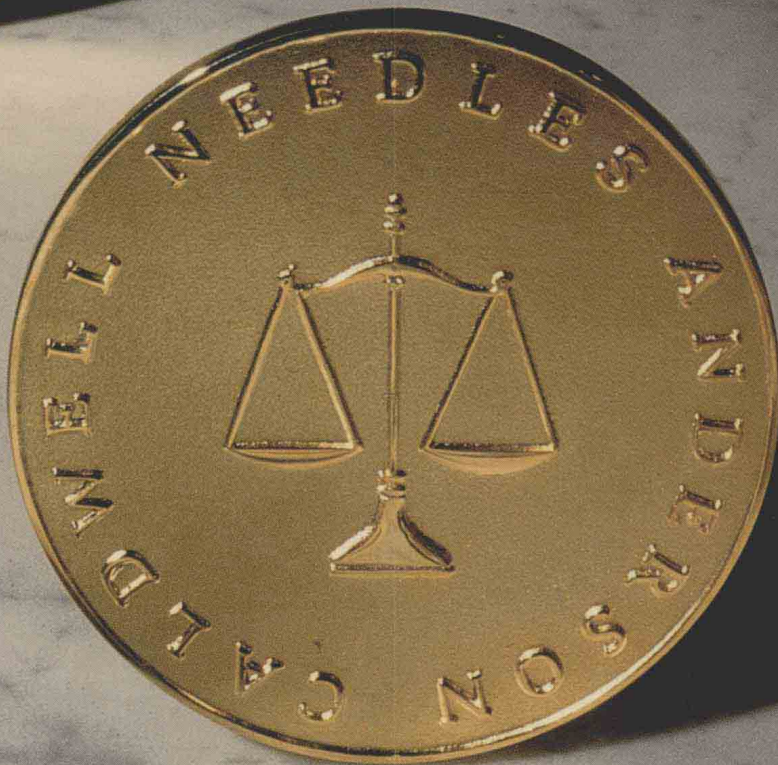
PRINCIPLES OF ACCOUNTING

NEEDLES

ANDERSON

CALDWELL

FOURTH EDITION



PRINCIPLES OF ACCOUNTING

FOURTH EDITION

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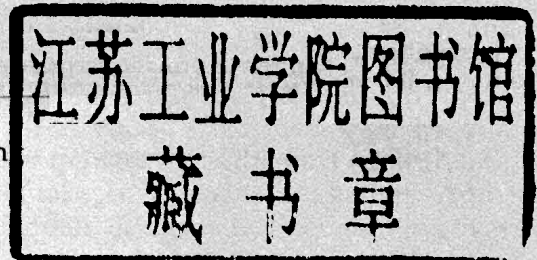
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To Marian Needles, and to Jennifer, Jeff, and Annabelle

To Sue Anderson, and to Deborah and Gregor Shewman, and to Howard, Christine,
and Nichole Anderson, and to Randy Anderson and Hugh Anderson

To Bonnie Caldwell, and to Stephanie, Susan, and Sharon

This book is written to provide accurate and authoritative information concerning the
covered topics. It is not meant to take the place of professional advice.

Cover photograph by Ralph Mercer.

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PRINCIPLES OF ACCOUNTING

TO THE STUDENT: HOW TO STUDY ACCOUNTING SUCCESSFULLY

Success in your accounting class depends first on your desire to learn and your willingness to work hard. But it also depends on your understanding of how the text complements the way your instructor teaches and the way you learn. An understanding of how this text is structured will help you to study more efficiently, make better use of classroom time, and improve your performance on exams.

The Teaching/Learning Cycle™

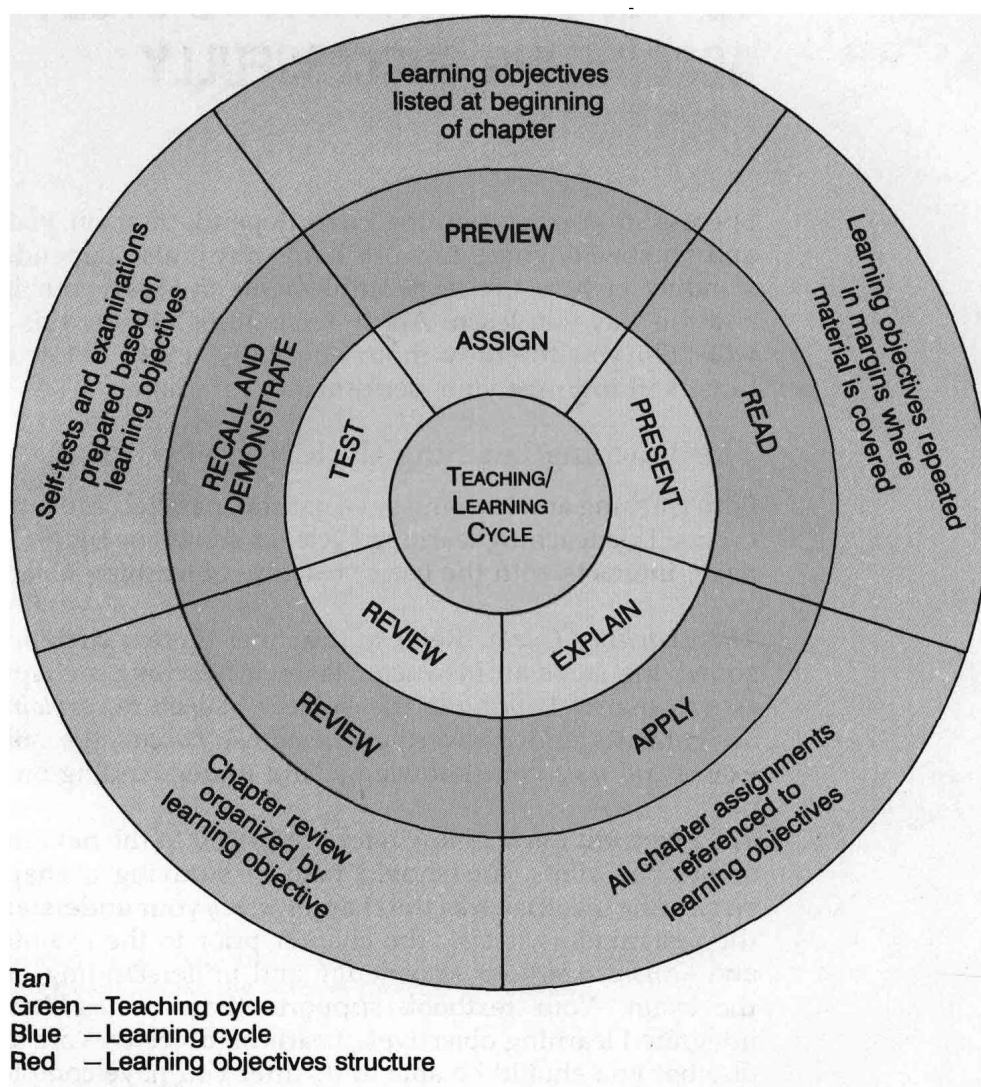
Both teaching and learning have natural, parallel, and mutually compatible cycles. This teaching/learning cycle, as shown in Figure 1 on the following page, interacts with the basic structure of learning objectives in this text.

The Teaching Cycle. Refer to the inner (green) circle in Figure 1, which shows the steps an instructor takes in teaching a chapter. Your teacher *assigns* material, *presents* the subject in lecture, *explains* by going over assignments and answering questions, *reviews* the subject prior to an exam, and *tests* your knowledge and understanding on the exam.

The Learning Cycle. Now refer in Figure 1 to the next circle (blue), which shows the steps you should take in studying a chapter. You should *preview* the material, *read* the chapter, *apply* your understanding by working the assignments, *review* the chapter prior to the examination, and *recall* and *demonstrate* your knowledge and understanding of the material on the exam. Your textbook supports these cycles through the use of integrated learning objectives. Learning objectives are simply statements of what you should be able to do after you have completed a chapter.

Integrated Learning Objectives. In Figure 1, the outside (red) circle shows how learning objectives are integrated into your text and other study aids and how they interact with the teaching/learning cycle.

1. Learning objectives appear at the beginning of the chapter, as an aid to your teacher in making assignments and as a preview of the chapter for you.
2. Each learning objective is repeated in the text at the point where that subject is covered to assist your teacher in presenting the material and to help you in reading the material.
3. Every exercise, problem, and case in the chapter assignments shows the applicable learning objective(s) so that you can refer to the text if you need help.
4. A summary of the key points for each learning objective, a list of new concepts and terms referenced by learning objectives, and a review

Figure 1. Teaching/Learning Cycles with Learning Objectives

problem covering key learning objectives assist you in reviewing each chapter. Your Study Guide, also organized by learning objectives, provides for additional review.

5. Finally, a self-test in each chapter review helps you prepare for the examination that your teacher will give based on the learning objectives assigned and covered in class. The questions, exercises, and problems in the Study Guide also help you prepare for examinations.

Why Students Succeed. Students succeed in their accounting course when their personal learning cycle is in phase with their instructor's cycle. Students who do a good job of previewing their assignments, reading the chapters before the instructor is ready to present them, preparing homework assignments before they are to be gone over in

class, and reviewing carefully will ultimately achieve their potential on exams. Those who get out of phase with their instructor, for whatever reason, will do poorly or fail. To ensure that you are in phase with your instructor, check your study habits against these suggestions.

Previewing The Chapter

1. Read the learning objectives at the beginning of the chapter. These learning objectives are specific action statements of what you should be able to do after completing the chapter.
2. Study your syllabus. Know where you are in the course and where you are going. Know the rules of the course.
3. Studying accounting is not like studying history or political science. Each assignment builds on previous ones. If you do poorly in Chapter 1, you may have difficulty in Chapter 2, and be lost in Chapter 3.

Reading The Chapter

1. As you read each chapter, be aware of the learning objectives in the margins. They will tell you why the material is relevant.
2. Allow yourself plenty of time to read the text. Accounting is a technical subject. Accounting books are condensed and almost every sentence is important.
3. Strive to be able to say "I understand why they do that." Accounting is logical and requires reasoning. If you understand why something is done in accounting, there is little need to memorize.
4. Relate each new topic to its learning objective and be able to explain it in your own words.
5. Be aware of colors as you read. They are designed to help you understand the text. (See the chart on page xxxiv of the preface.)

Red All learning objectives and references to them are in red, as well as all key terms. Make sure you know their meanings. Remember, they are listed with definitions in the chapter reviews and a comprehensive glossary is located at the end of the book. In addition to learning objectives and key terms, source documents are shown in red.

Green All accounting forms and working papers are shown in green.

Blue All financial statements, the final product of the accounting process, are shown in blue. In addition, blue is used to emphasize the major headings in each chapter.

Beige Selected tables and illustrations use beige to heighten contrasts and aid student understanding. This color is also used in the part openers and comprehensive problems.

6. If there is something you do not understand, prepare specific questions for your instructor. Pinpoint the topic or concept that confuses you. Some students keep a notebook of points with which they have difficulty.

Applying The Chapter

1. In addition to understanding “why they do that,” you must also be able to do it yourself by working exercises, problems, and cases. Accounting is a “do-it-yourself” course.
2. Read assignments and the instructions carefully. The wording is precise, and a clear understanding of it will save time and improve your performance.
3. Try to work exercises, problems, and cases without flipping back to the chapter. If you cannot work the assignment without looking in the chapter, you will not be able to work a similar problem on an exam. After you have tried on your own, refer to the chapter (based on the learning objective reference) and check your answer. Try to understand any mistakes you may have made.
4. Be neat and orderly. Sloppy calculations, messy papers, and general carelessness cause most errors on accounting assignments.
5. Allow plenty of time to work the chapter assignments. Assignments are harder to work and more errors occur when prepared under time pressure.
6. Keep up with your class. Check your answer against the solution presented in class. Find your mistakes. Be sure you understand the correct solution.
7. Note the part of an exercise, problem, or case with which you have difficulty so that you can ask for help.
8. Attend class. Most instructors design class to help you and to answer your questions. Absence from even one class can have a negative effect on your performance.

Reviewing The Chapter

1. Read the summary of learning objectives in the chapter review. Be sure you know all the words in the review of concepts and terminology.
2. Take the chapter self-test and review the learning objective for any question you answered incorrectly.
3. Review all assigned exercises, problems, and cases. Know them “cold!” Be sure you can work these assignments without the aid of the book.
4. Determine the learning objectives for which most of the problems were assigned. These are the topics that your instructor is most likely to emphasize on an exam. Scan the text for these learning objectives and pay particular attention to the examples and illustrations.
5. Look for and scan other similar assignments that cover the same learning objectives. These may be helpful on an exam.
6. Review quizzes. These questions are often similar to longer exams.
7. Attend any labs or visit any tutors your school provides, or see your instructor during office hours to get assistance. Be sure to have specific questions ready.

Taking The Exam

1. Arrive to class early so you can get the feel of the room and make a last minute review of your notes.

2. Have plenty of sharp pencils and your calculator (if allowed) ready.
3. Review the exam quickly when it is handed out to get an overview of your task. Start with a part you know. It will give you confidence and save time.
4. Allocate your time to the various parts of the exam, and stick to your schedule. Every exam has an element of speed. You need to move ahead and make sure you attempt all parts of the exam.
5. Read the questions carefully. Some may not be exactly like a homework assignment. They may approach the material from a slightly different angle to test your understanding and ability to reason, rather than your ability to memorize.
6. Be neat, use good form, and show calculations. These techniques prevent errors.
7. Relax. If you have followed the above guidelines, your effort will be rewarded.

PREFACE

PRINCIPLES OF ACCOUNTING, Fourth Edition, is a comprehensive first course in accounting for students with no previous training in accounting or business. It is intended for use in the traditional two-semester or two- and three-quarter sequence. Designed for both majors and nonmajors, the textbook is part of a well-integrated package for students and instructors that includes many manual and computer ancillaries not found in previous editions.

Goals of the Fourth Edition

We wrote this book believing that integrated learning objectives can significantly improve the teaching and learning of accounting. This system of learning by objective enhances the role of the overall package, and particularly that of the textbook, in achieving good communication between the instructor and the student.

The success of the first three editions of this book has justified our confidence in the principle of learning by integrated objectives. At the same time, several goals guided us in developing and writing **PRINCIPLES OF ACCOUNTING**, Fourth Edition. Those goals were: (1) to write for the student's first exposure to accounting; (2) to extend learning by objectives to the entire package; (3) to make the content authoritative, practical, and contemporary; (4) to emphasize the role of accounting in decision making; (5) to adhere to a strict system of quality control; and (6) to develop the most complete and flexible package available.

The Student's First Exposure to Accounting

When organizing the text, we specifically focused on the needs of the intended audience, the freshman and sophomore student. First, we carefully paced new concepts and techniques to ensure that students would grasp and retain the material. Second, we limited the number of difficult concepts or practices in each chapter, particularly in the early part of the book. Third, we rigorously provided a clear presentation, a consistent reading level, and a uniform use of terminology throughout the text. Fourth, we focused on understanding, not memorization, believing that concepts acquire meaning when applied and practices become most easily understood when related to those concepts. Fifth, we emphasized concepts and practices useful to students throughout their careers, whether in accounting or not.

Integrated Learning by Objectives

We took a definite pedagogical approach to writing *PRINCIPLES OF ACCOUNTING*, Fourth Edition. We extensively used learning objectives and learning theory. Learning objectives were integrated throughout the text and package from the chapter previews and presentations to the chapter reviews, assignments, study aids, and testing and evaluation material.

Authoritative, Practical, and Contemporary

This book presents accounting as it is practiced and carefully explains the theory underlying those practices. Accounting terms and concepts are defined according to pronouncements of the AICPA, APB, FASB, and CASB. The Statements of Financial Accounting Concepts of the FASB's Conceptual Framework Study form the theoretical underpinning of the book and are used to assess various accounting situations and controversies. In addition, steps were taken to ensure that, to the extent possible within the framework of introductory accounting, the material realistically reflects the way accounting is practiced today.

The topics covered are up to date and correspond with current trends in business and accounting. Ethical considerations in accounting are integrated at appropriate points throughout the book. They are included in the discussions of the auditor's professional responsibilities, financial reporting, managerial accounting, and in a general business context. New appendices have been added on not-for-profit accounting and the just-in-time philosophy in managerial accounting. Complete coverage of the new statement of cash flows is contained in Chapter 18. International accounting is now the primary focus of Chapter 21.

Decision-Making Emphasis

Another of our goals was to present the contemporary business world and the real-life complexities of accounting in a clear, concise, easy-to-understand manner. Accounting is treated as an information system that helps managers, investors, and creditors make economic decisions. In addition to questions, exercises, and problems, the chapter assignments include two decision-oriented features: an "Interpreting Accounting Information" exercise and either a "Financial Decision Case" or a "Management Decision Case." In each situation, the student must extract quantitative information from the exercise or case and make an interpretation or a decision.

Quality Control

Together with our publisher, we developed a system of quality control for all parts of the package to ensure the most technically and conceptually accurate program possible. This system, which utilizes an innovative computer database technology, involved many steps, including thorough reviews by users, visits to and discussions with users by the authors, extensive in-house editorial review, accuracy checking by over forty

introductory accounting teachers, class testing, and finally an audit for technical and conceptual accuracy by the international accounting firm, Ernst & Young.

Complete and Flexible Learning System

We believe that *PRINCIPLES OF ACCOUNTING*, Fourth Edition, represents the most complete and flexible package available for a first course in accounting. All parts of the package fit within the exclusive pedagogical system of integrated learning by objectives established by the authors. This system fits within the framework of the Teaching/Learning Cycle, which is described in detail in the To the Student section at the beginning of this text and in the following sections.

Organization of the Fourth Edition

The book is organized into seven parts so it may be used by schools on either a semester or quarter sequence. Those using the two-semester or two-quarter sequence may cover three parts during the first term and four parts during the second. Those using the three-quarter sequence may cover two parts in each of the first two quarters and three parts in the last quarter. If a shorter course is required, all or parts of chapters 4, 6, 13, 19, 20, 21, and 24 may be omitted or covered briefly without hindering comprehension of the later chapters. For instructors wanting to introduce students to the present and future value of money, individual income taxes, not-for-profit accounting, or the just-in-time philosophy, appendices on these subjects along with examples and assignments are provided at the end of the text.

Focus on Ethics and Communication Skills

There is a recognized need in our society for accounting and business students to be exposed in all their courses to ethical considerations and to be better prepared in writing and communication skills. As authors, we feel an obligation to help students achieve these goals. First, we introduce ethical concerns, throughout the text, not only as they apply to auditors but also as they apply to financial and managerial accountants and to business professionals. Second, we have provided ample assignments to enhance student communication skills. All sections of the end-of-chapter material now contain written assignments. The Discussion Questions and Writing Assignments focus on this objective as do the Interpreting Accounting Information and Financial and Management Decision Cases. In addition, selected classroom exercises and A and B problems in each chapter contain writing components. We have found the Interpreting Accounting Information and Financial and Management Decision Cases to be excellent vehicles for the improvement of commu-

nication skills through small group discussion and oral reports. Appropriately structured, these activities take far less time than might be thought and are valuable to the students.

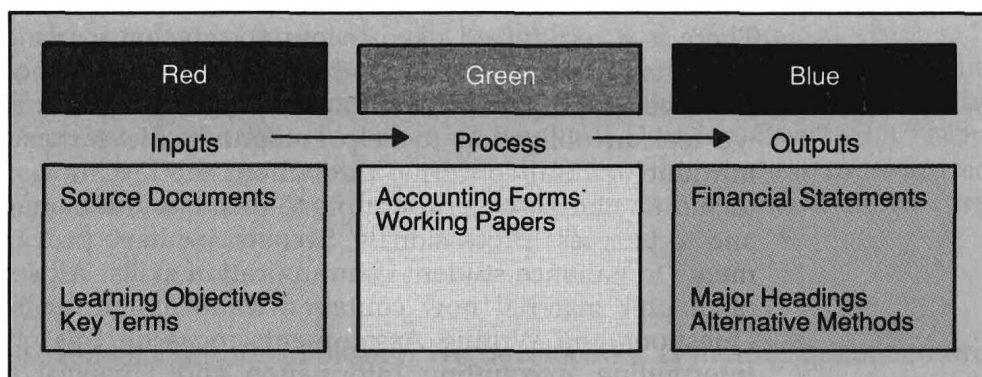
Textbook Features

Pedagogical Use of Color

The text uses a five-color design consistently throughout the illustrations to enhance students' understanding of the accounting process. The chart below displays the value of this pedagogical approach to color. First, pedagogical features such as learning objectives, key terms, and emphasized material in the text are printed in red, as are all source documents. Second, green is used to represent accounting forms and working papers, which are part of the ongoing process of accounting. Third, blue is used to emphasize the major headings in the chapter and to highlight the actual financial statements, the final product of the accounting process. Blue is also used to indicate alternative methods that are presented in the text. Beige is used in selected tables and illustrations to heighten the contrasts and aid student understanding. In addition, it helps students locate the three new comprehensive problems.

Integrated Learning Objectives

Action-oriented objectives at the beginning of each chapter indicate in precise terms what students should be able to do when they complete the chapter. The learning objective is restated in the margin beside pertinent text. All end-of-chapter components—Review of Learning Objectives, Review of Concepts and Terminology, Self-Test, and Review Problem—are clearly referenced to learning objectives, and end-of-chapter assignments are keyed to specific objectives.



Real-World Applications

Many chapters include graphs or tables illustrating how the actual business practices relate to chapter topics. Most Interpreting Accounting Information exercises are based on the published financial reports of real companies.

Key Terms and Glossary

Throughout the book, key accounting terms are emphasized in bold, red type and are clearly defined in context. These terms are listed alphabetically with definitions and learning objective references in each Chapter Review; they are also assembled in a comprehensive glossary at the end of the book.

Transaction Index

A new feature of the Fourth Edition, the index of transactions, appears inside the front cover of the text. This unique index allows students to look up any transaction and find the page number on which it is discussed and illustrated. The transaction index is especially useful to students when solving homework assignments.

Guide to Accounting Formats and Financial Statements

Inside the back cover of the text, another new student aid is provided. This guide illustrates the proper formats for financial statements and references pages on which common accounting forms and financial statements can be found.

Chapter Review

A unique feature of each chapter is a special review section. The Review of Learning Objectives summarizes the chapter's main points in relation to the objectives. The Review of Concepts and Terminology presents all key terms from the chapter with definitions and learning objective references. The Review Problem with a complete solution demonstrates the chapter's major procedures before students work the exercises and problems. Self-Tests, now in every chapter, review the basic concepts and are referenced to learning objectives. The Answers to Self-Test section provides immediate feedback to students and is located after each chapter's assignments.

Discussion Questions and Writing Assignments

Review questions at the end of each chapter focus on major concepts and terms and provide thought-provoking questions for writing assignments.

Classroom Exercises

Classroom exercises provide practice in applying concepts and procedures taught in the chapter and are effective in illustrating lecture points. Each

exercise is keyed to one or more learning objectives. There are 25 percent new exercises in this edition. In addition, solution transparencies are available for all exercise solutions.

Interpreting Accounting Information

This feature asks the student to interpret published financial information in Chapters 1–21 and internal management reports in Chapters 22–28. Such reports and information are based on excerpts from actual reports or on published articles about well-known corporations and organizations. Among the companies included are K mart, Sears, U.S. Steel, Marathon Oil, Chrysler, and Lockheed. Each exercise requires students to analyze published information by extracting data and making computations and interpretations.

A and B Problems

We have included two sets of problems to provide maximum flexibility in homework assignments. Generally, the problems are arranged in order of difficulty, with problems A-1 and B-1 for each chapter being the simplest. A and B problems have been matched by topic, thus A-1 and B-1 are equivalent in content and level of difficulty. In addition, all problems are keyed to the learning objectives. For each problem, ratings of difficulty, time estimates, and solutions are available to the instructor as are transparencies of all solutions. Additional assignment material is provided in the Demonstration Problems Book.

Financial and Management Decision Cases

Each chapter contains a case emphasizing the usefulness of accounting information in decision making. The business background and financial information for each case are presented in the context of the decision. The decision maker may be a manager, an investor, an analyst, or a creditor. In the role of decision maker, the student is asked to extract relevant data from the case, make computations as necessary, and arrive at a decision.

Comprehensive Problems

Comprehensive Problems covering several chapters have been added to the Fourth Edition. After Chapter 4, the first Comprehensive Problem covers the accounting cycle for a service company. The cycle is the second month of operations for Joan Miller Advertising Agency, the same company which was used to introduce the accounting cycle in Chapters 2 through 4. After Chapter 6, the accounting cycle for a merchandising concern using special journals is the subject of the Comprehensive Problem. The company, Fenwick Fashions, is the same company as used to introduce merchandising in Chapter 5. After Chapter 16, comprehensive stockholders' equity transactions for Sundial Corporation are recorded and a statement of stockholders' equity is prepared.

Supplementary Learning Ancillaries

The supplementary learning aids provide a variety of useful items for students and instructors. A complete description is contained in the Instructor's Handbook. Briefly, they consist of the following:

- Study Guide with Selected Readings, also available in a Spanish edition
- Working Papers, four sets, plus a set of Blank Working Papers
- Demonstration Problems Book
- Traditional Practice Sets, including
 - Micro-Tec, Third Edition
 - A Merchandising Sole Proprietorship Practice Set, in narrative and working-papers formats
 - College Words and Sounds Store, Third Edition
 - A Sole Proprietorship Merchandising Business with Payroll Practice Set
 - The Windham Company, Second Edition
 - A Managerial Accounting Practice Set
- Practice Analysis Cases, including
 - Richland Home Centers, Inc. Annual Report, Second Edition
 - A Practice Case in Financial Analysis
 - Heartland Airways, Inc. Annual Report, Second Edition
 - A Practice Case in Financial Analysis
 - McHenry Hotels, Inc.
 - A Practice Case in Managerial Accounting
- Computer-Assisted Practice Sets
 - Parks Computer Company
 - Matthew Sports Company
 - Cooks Solar Energy Systems, Second Edition
 - Sounds Abound
- Other Computerized Study Materials
 - Lotus® Problems for Accounting: A Working Papers Approach
 - Correlation Chart to Accompany PRINCIPLES OF ACCOUNTING, Fourth Edition
 - Rags to Riches®: General Ledger Software and Workbook
 - The Accounting Transaction Tutor
 - Computerized Diagnostic Tests
- Check List of Key Figures
- Student Resource Videos

Instructor's Aids

Print-Based Materials

- Instructor's Handbook
- Instructor's Solutions Manual, Volume 1: Chapters 1–14
- Instructor's Solutions Manual, Volume 2: Chapters 15–28 and Appendices