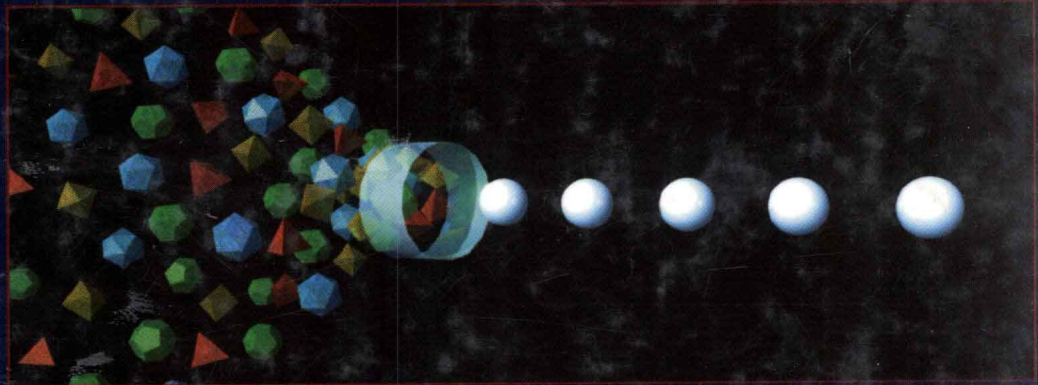


Bazley, Nikolai and Grove



*f*INANCIAL ACCOUNTING

Concepts and Uses Third Edition



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Concepts and Uses Third Edition

JOHN D. BAZLEY
Professor, School of Accountancy
University of Denver

江苏工业学院图书馆
藏书章

LOREN A. NIKOLAI
Ernst & Young Professor, School of Accountancy
University of Missouri – Columbia

HUGH D. GROVE
Professor, School of Accountancy
University of Denver



SOUTH-WESTERN College Publishing
An International Thomson Publishing Company

Acquisitions Editor: Elizabeth Bowers
Developmental Editor: Sara Bates
Production Editor: Marci Dechter
Internal Design: Craig LaGesse Ramsdell
Production House: The Cowans
Marketing Manager: Sharon Oblinger

A067CA

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Cincinnati, Ohio

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1 2 3 4 5 6 7 8 9 D1 0 9 8 7 6 5 4 3 2 1

Printed in the United States of America

Library of Congress Cataloging-in-Publication Data

Bazley, John D.

Financial Accounting: concepts and uses / John D. Bazley,
Loren A. Nikolai, Hugh D. Grove. — 3rd ed.

p. cm.

Includes index.

ISBN 0-538-83922-8

1. Accounting. I. Nikolai, Loren A. II. Grove, Hugh D.

III. Title.

HF5635.B35 1995

657'.3—dc20

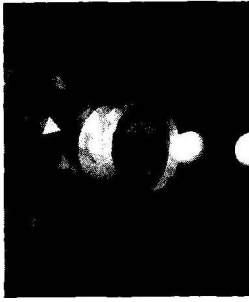
94-12586

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Preface

PURPOSE

Financial accounting is a growing and dynamic discipline. Similarly, the financial statements prepared by companies are becoming more complex as the business environment and transactions become more complex and disclosure requirements increase. The subject matter can be made more relevant and understandable by a book that contains (1) clear, direct discussion that anticipates the student's learning process, (2) up-to-date treatment of accounting principles, (3) the frequent use of examples, (4) illustrations taken from financial statements of real companies, and (5) plentiful and varied assignment materials. We feel that we have incorporated these teaching and learning tools into this book.

Our goal is to provide students with a comprehensive yet readable book, one that will enable the reader to develop a sound understanding of the principles underlying the accounting information included in financial statements and the uses to which that information is put. The book is intended for students who wish to develop a thorough understanding of the meaning of accounting information, whether they are undergraduate or graduate students, business or accounting majors or other interested students. We believe that an understanding of the content of, and principles underlying, financial statements is valuable for the students' future careers as bankers, managers, investors, accountants, or owners of their own businesses.

GENERAL OVERVIEW

Financial Accounting: Concepts and Uses, third edition, has been developed for an introductory course, or courses, in financial accounting. It is written with the same care and thought as our book *Intermediate Accounting*, (sixth edition by Nikolai and Bazley) published by South-Western Publishing Company. Our goal is to include the most educationally effective blend to facilitate an understanding of the usefulness and limitations of accounting principles, the concepts underlying those principles, and the practical implementation of those principles in the financial statements. The book is organized in a fairly traditional manner because we do not believe that rearranging the order of coverage, just for the sake of being different, is sound pedagogy. On the other hand, we have chosen to expand the coverage of some topics (e.g., postemployment benefits, earnings per share, and investments) that are important to an understanding of the financial statements, and to reduce that of other topics (e.g., discounts, exchanges, and LIFO perpetual inventory) that are unlikely to affect the financial statements materially. We believe that this blend of topics will provide a more relevant introduction to financial reporting.

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 PEDAGOGY

Although the first exposure to accounting principles is sometimes difficult for students, we believe that these principles can be made more understandable and interesting by using a clear, direct, building block discussion that anticipates a student's learning process and that is written at the student's reading level. Numerous real-world examples are used to provide an understanding of the way in which the principles actually are implemented. Each chapter begins with a set of learning objectives—what the student should understand after reading this chapter—and an introduction that presents the topics to be covered. Each topic is discussed in a logical order. Generally, each topic is introduced by a brief practical and conceptual overview, followed by a discussion of the related accounting principles and their implementation in the financial statements. This discussion often includes the use of visuals: diagrams, sets of steps designed to facilitate the student's understanding, and real-world examples. At the appropriate place in the discussion, an example is presented to reinforce the student's learning process. Each example is straightforward, is fully explained, and avoids quantum leaps that might confuse the student. Illustrations of the effects on the accounting equation and the financial statements as well as the notes and supporting schedules are abundant and meaningful. Any issues regarding the interpretation of those principles in the financial statements are discussed. Only after the current principles and practices have been thoroughly explained are the usefulness and limitations of those principles discussed, and any alternative principles explained and evaluated.

Within each chapter, headings separate the material into logically ordered, understandable portions for the student. Key concepts are **boldfaced**; *italics* are used for emphasis. The entire financial section of the 1993 annual report of Nike, Inc., is in various chapters throughout the book. The entire financial section of the 1993 annual report of Ford Motor Company is included in Appendix A.



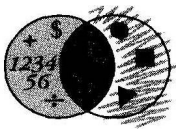
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 COVERAGE

The book consists of 14 chapters divided into three parts: The Fundamentals of Financial Reporting; Assets, Liabilities, and Stockholders' Equity; and Additional Financial Reporting Topics. Because of the complexity of accounting principles and the economic transactions that occur in today's business environment, the book may include more topics than an instructor wishes to cover in a single class. The book is written so that the instructor may select topics without detracting from the ability of the student to understand those topics. For example, postretirement benefits, primary and fully diluted earning per share, alternative methods of revenue recognition, and consolidations are self contained topics that may be omitted. *Our philosophy is not to exclude items that are relevant to an understanding of most companies' published financial statements, but to allow the instructor to select the appropriate coverage. Therefore, the book will also be a valuable resource to the student after the class when topics omitted from the class are encountered, whether in another academic class or in a working environment.* Suggestions regarding the selection of topics are included in the *Instructor's Manual*.

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 SPECIFIC
 FEATURES

In our combined 70 years of teaching experience we have identified many aspects of sound pedagogy; these have been incorporated into the book. Some of the major features are summarized:

1. *Nontechnical GAAP.* The book introduces and explains generally accepted accounting principles (GAAP) in understandable nontechnical language without repeatedly quoting formal pronouncements.
2. *Revenues and expenses.* Discussion of revenues and expenses is deferred until Chapter 2, after a clear discussion of assets, liabilities, and stockholders' equity in Chapter 1, causing less confusion for the students.
3. *Corporations.* The book focuses on the corporate form of entity because that is the most likely entity that the student will encounter. Other types of entities are discussed briefly.
4. *Mechanics of accounting.* The book eliminates the emphasis on debits and credits by focusing on the accounting equation and the financial statements when transactions are being analyzed and discussed.
5. *Making decisions.* Sections entitled "Making Decisions" are included in each chapter (new in this edition). The primary purpose of these sections is to help students appreciate the relevance of the chapter discussion to real-world decisions. While some issues relate directly to the chapter discussion, others deal with issues that are beyond the *specific* chapter coverage. These are intended to stimulate students' thinking about broader issues. All the questions may be used for class, or group, discussions.
6. *Characteristics of accounting information and audit reports.* Chapter 4 contains an extensive discussion of the characteristics of accounting information, such as relevance and reliability, as well as the purpose and types of audit reports. The purpose of this discussion is to give the student a perspective for understanding the realities of financial reporting. Instructors may prefer to assign some of this material earlier, for example, as the first chapter.
7. *Uses of accounting information.* Chapter 5 contains a discussion of the analysis of financial information, including ratios, so that those topics can be integrated throughout the book.
8. *Real-world understanding.* Frequently, once a topic has been explained, the impact on the financial statements is discussed. Examples include the impacts of LIFO, LIFO liquidation, conversion from LIFO to FIFO, the recognition or nonrecognition of contingencies, the appropriateness of the 40-year period for amortizing intangibles, the selection of purchase or pooling, and the selection of rates used for postemployment benefits. Each of these sections is designated by a logo.
9. *Receivables and liabilities.* Accounts receivable are discussed in Chapter 6, while liabilities are discussed in Chapters 9 and 10. This arrangement lessens the confusion often found in many texts that discuss the accounting for receivables and payables in the same chapter.
10. *Income tax issues integrated.* Rather than devoting an entire chapter to the specifics of income taxes, the discussion of income taxes is integrated in each chapter where it applies to specific topics (e.g., inventory, depreciation, deferred income taxes, and operating loss carrybacks and carryforwards). This organization allows the student to understand the general relationship of accounting principles and income taxes while leaving the detailed discussion of specifics to a separate tax course.
11. *Effective interest method.* The discussion of bonds focuses on bonds issued at par, while the effective interest method is applied to mortgages, notes, (zero coupon bonds) and leases. The effective interest method applied to bonds (as well as the straight-line method) is explained in an Appendix to Chapter 9.



12. *Consolidated financial statements.* Because of the importance of acquisitions in the business world, the basic characteristics of purchase and pooling are discussed, as well as the preparation of a balance sheet on the date of acquisition. The discussion of disaggregated information (segment reporting) follows the discussion of consolidation.
13. *International accounting.* Because of the increasing importance of international transactions and subsidiaries, both topics are discussed. The conversion of foreign financial statements, when a foreign currency is the functional currency and when the U.S. dollar is the functional currency, is discussed.
14. *An abundance of end-of-chapter assignment materials is included.* A bold-faced note preceding each assignment indicates the subject at issue, *without* providing a hint as to the appropriate solution. The assignment materials are divided into three separate classifications, questions, problems and cases, and annual report problems. The first group includes questions that address key concepts and terms and may be most useful for class discussion or for the student to review the key items in the chapter. The second group includes problems and cases that typically require numerical solutions or narrative answers; generally they are organized in order of difficulty and follow the order of the topics in the chapter. The third group includes assignments that focus on financial statements and financial reporting issues involving real-world companies. These assignments require the student to apply the concepts developed in the chapter to the financial statements of actual companies. Therefore, they may require an ability by the student to understand the use of different terminology, to apply the principles to alternative situations, and to integrate topics from different chapters. (If the assignment requires knowledge of a topic not yet discussed in the sequential order of the chapters, a note is included in the *Instructor's Manual*.)

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MAJOR
CHANGES

To improve the pedagogy and to reflect significant changes in accounting principles, numerous changes have been made in this third edition. The major changes are summarized as follows:

1. *Simplification of discussion.* The entire book has been thoroughly reviewed and, wherever possible, simplified to make the text more "student friendly." Particular emphasis has been placed on making the first 5 chapters easier to read and understand.
2. *Rearrangement of coverage.* The topics from Chapter 14 have been simplified and moved to Chapter 5, so that the first 5 chapters form a unified introduction to the content and uses of financial reporting. The discussion of present value principles has been moved to Appendix B of the book so that it may be introduced into the course at the instructor's discretion.
3. *Modification and expansion of visual aids.* Exhibits 1-1 (capital markets), 4-1 (groups influential in establishing GAAP), 9-4 (characteristics of bonds), and 14-1 (pension relationships) are examples of visual aids that have been added to enhance student understanding.
4. *Addition of discussion of differences in international accounting principles.* In Chapter 5, a discussion of international accounting differences and international accounting principles has been added. In subsequent chapters, an explanation of major differences in international accounting standards has been added. Discussion of international topics is designated by the use of a logo.



5. *Integration of the annual report of Nike.* A reference list included in Appendix A shows the integration throughout the book of the Nike annual report.
6. *Ford Motor Company's annual report.* Ford's financial statements (in Appendix A) have been included because they are separated into automotive and financial services segments so that instructors and students have "two statements for the price of one."
7. *Analysis of transactions and events using the accounting equation.* Transactions and events are explained in terms of the accounting equation with related text discussion emphasizing the effects on the financial statements. Journal entries and ledger accounts are not used.
8. *Usefulness and limitations of financial statements.* Sections on the usefulness and limitations of the balance sheet, income statement, and cash flow statement have been added to Chapters 1 and 2.
9. *Discussion of agency theory.* A brief discussion of agency theory has been added to Chapter 5.
10. *Expansion of cash flow discussion.* The discussion of the cash flow statement in Chapter 2 has been expanded so that instructors may discuss all subsequent topics in terms of their impacts on the cash flow statement. An explanation of those impacts has been added to the text of all subsequent chapters. Cash flow statements have been added to the Wells Company example in Chapter 2.
11. *Discussion of the accounting system.* Throughout the book, instructors may teach the impacts of transactions and events by reference only to the financial statements, and avoid the distraction of accounting procedures. However, the appendix to Chapter 3 may be used for an explanation of those procedures, if preferred.
12. *Changes to comprehensive review example.* In Chapter 3, Exhibit 3-3 has been added to make the example less procedural. Exhibits 3-4, 5, and 6 can be omitted to provide a more conceptual approach.
13. *Revision of homework assignments.* Homework has been updated and revised in all chapters. Also, virtually all the "annual report problems" have been revised and updated.
14. *Updating of hierarchy and sources of GAAP.* The hierarchy and sources of GAAP have been updated to reflect all current changes in the accounting standards.
15. *Addition of brief discussion of regulatory accounting principles (RAP).* A brief discussion of RAP has been added because companies in certain industries (e.g., banking) may follow those principles.
16. *Addition of a discussion of ethics.* A section on ethical issues in accounting has been added so that students understand that ethical issues arise in financial reporting, and to provide a framework for class discussion of ethical issues.
17. *Discussion of cash flow ratios.* A section discussing specific cash flow ratios has been added.
18. *Cash, accounts receivable, and revenue recognition.* The discussion of alternative revenue and expense recognition methods has been moved to the appendix of Chapter 6.
19. *Inventories and cost of goods sold.* The discussion of the periodic and perpetual inventory methods has been rewritten to emphasize the use of the perpetual method for control and the periodic method for financial reporting. Appendix 1 on purchases discounts has been simplified and Appendix 2 on the perpetual

LIFO method has not been included because its use is unlikely to have an effect on reported financial information.

20. *Property, plant, and equipment, intangibles, natural resource assets and related expenses.* The discussion on impairments has been updated to reflect the most recent deliberations of the FASB. A section on the interpretation of the gain or loss in disposals has been added. The discussion of disposals has been simplified and the appendix on exchanges deleted because the method is unlikely to have an effect on reported financial information.
21. *Current liabilities, mortgages, notes, bonds, and interest expense.* A discussion of the impact of environmental liabilities has been added. A discussion of the impairment of loans has been added and the discussion of troubled debt restructuring has been updated for *FASB Statement No. 114*.
22. *Leases and income taxes.* The section on the evaluation of leases has been expanded. The discussion of deferred income taxes and operating losses has been updated for *FASB Statement No. 109*. The discussion of postemployment benefits has been moved to Chapter 14 to provide the instructor with greater flexibility of coverage.
23. *Stockholder's equity and components of the income statement.* The discussions of treasury stock, stock dividends, and appropriations of retained earnings have been simplified. A brief explanation of ESOPs has been added. The discussion of stock options has been simplified while the evaluation section has been expanded to provide a better user orientation. A brief discussion of the FASB's proposed rules has been added.
24. *Investments and acquisitions of other companies.* The discussion has been updated for *FASB Statement No. 115*, and the discussion of segment reporting has been included in this chapter because of its relationship to consolidations.
25. *Postemployment benefits, international operations, and changing prices.* The examples of accounting for pensions have been simplified, and a section on the evaluation of pension disclosures has been added. The section on OPEBs has been updated to reflect *FASB Statement No. 106*. The evaluation of accounting for changing prices has been modified to emphasize the impacts on financial statements of not reporting the effects of changing prices. The discussion of the supplementary disclosure of the effects of changing prices has been deleted. The conclusions to the book have been updated for the report of the AICPA Committee on Financial Reporting.

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SUPPLEMENTARY MATERIALS

In addition to the book, an *Instructor's Manual* is available. It includes a suggested solution for each assignment and helpful notes to the instructor. Also included at the beginning of each chapter are teaching notes for the instructor.

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ACKNOWLEDGMENTS

The authors wish to express their appreciation to the individuals who served as reviewers and who provided insightful comments and valuable suggestions in the development of the manuscript.

Vincent E. Brenner
Parveen P. Gupta
Herbert G. Hunt III

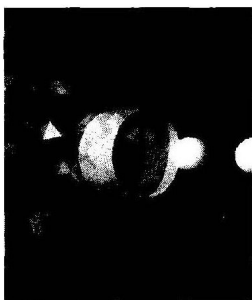
Louisiana State University
Lehigh University
University of Vermont

David Johnson
William L. Kimball
Richard Lau
E. James Meddaugh

University of St. Thomas
California State University, Northridge
California State University, Los Angeles
Ohio University

We wish to thank Anita Blanchar and our editorial and production staffs. We are grateful to our respective schools of accountancy for their support and to the American Institute of Certified Public Accountants, the Financial Accounting Standards Board, Nike, Inc., and Ford Motor Company for permission to quote from their respective pronouncements and financial statements. We are also grateful to our families and friends for their moral support and understanding during the entire manuscript production process.

John D. Bazley
Loren A. Nikolai
Hugh D. Grove



About the Authors

JOHN D. BAZLEY

John D. Bazley, Ph.D., CPA, is Professor of Accounting in the School of Accountancy at the University of Denver, where he has received the University's Distinguished Teaching Award, The Vernon Loomis Award for Excellence in Advising, the Alumni Award for Faculty Excellence, and the Jerome Kesselman Endowment Award for Excellence in Research. Dr. Bazley earned a B.A. from the University of Bristol in England and an M.S. and Ph.D. from the University of Minnesota. He has also taught at the University of North Carolina at Chapel Hill and holds a CPA certificate in the state of Colorado. He has taught national professional development classes for a major CPA firm and was a consultant for another CPA firm. Dr. Bazley is coauthor of *Intermediate Accounting* (sixth edition) (South-Western Publishing company). Dr. Bazley has published articles in professional journals, including *The Accounting Review*, *Management Accounting*, *Accounting Horizons*, *The International Journal of Accounting*, *The Journal of Managerial Issues*, *Petroleum Accounting and Financial Management Journal*, *Practical Accountant* and the *Academy of Management Journal*, and is a member of the Editorial Boards of *Issues in Accounting Education* and the *Journal of Managerial Issues*. He is also a coauthor of a monograph on Environmental Accounting published by the National Association of Accountants. Dr. Bazley has served on numerous committees of the Federation of Schools of Accountancy, including chair of the Student Lyceum Committee; the American Accounting Association; and the Colorado Society of CPAs, including the Continuing Professional Education Board. He is a member of the American Institute of Certified Public Accountants, the Colorado Society of Certified Public Accountants, and the American Accounting Association.

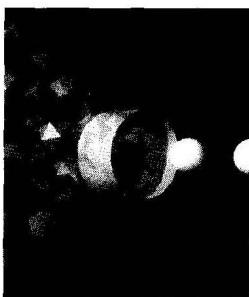
LOREN A. NIKOLAI

Loren A. Nikolai, Ph.D., CPA, is the Ernst & Young Professor in the School of Accountancy at the University of Missouri—Columbia (MU). He received his B.A. and M.B.A. from St. Cloud State University and his Ph.D. from the University of Minnesota. Professor Nikolai has taught at the University of Wisconsin at Platteville and at the University of North Carolina at Chapel Hill. He is the recipient of the MU College of Business and Public Administration 1994 Accounting Professor of the Year Award, Missouri Society of CPAs 1993 Outstanding Educator of the Year Award, the MU 1992 Kemper Fellowship for Teaching Excellence, the MU College of Business and Public Administration 1991 Faculty Member of the Year Award, and the Federation of Schools of Accountancy 1989

Faculty Award of Merit. Professor Nikolai was also the recipient of the 1990 Distinguished Alumni Award from St. Cloud State University. He holds a CPA certificate in the state of Missouri and previously worked for the 3M Company. Professor Nikolai is the lead author of *Intermediate Accounting* (sixth edition), (South-Western Publishing Company). He has published numerous articles in *The Accounting Review*, *Journal of Accounting Research*, *The Accounting Educator's Journal*, *Journal of Accounting Education*, *The CPA Journal*, *Management Accounting*, *Policy Analysis*, *Academy of Management Journal*, *Journal of Business Research*, and other professional journals. He was also lead author of a monograph published by the National Association of Accountants. He is a member of the American Accounting Association, the American Institute of Certified Public Accountants, and the Missouri Society of CPAs. He has chaired or served on several American Accounting Association committees, and was Director of Education from 1985–87. He has served on numerous Federation of Schools of Accountancy (FSA) committees and was President of the FSA in 1994.

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HUGH D.
GROVE

Hugh D. Grove, D.B.A., CPA, is Professor of Accounting in the School of Accountancy at the University of Denver. Dr. Grove earned a B.B.A. and an M.B.A. from the University of Michigan and a D.B.A. from the University of Southern California. He has also taught at California State Polytechnic University—Pomona and holds a CPA certificate in the state of Michigan. Dr. Grove has published articles in *The Accounting Review*, *Journal of Accounting Research*, *Accounting, Organizations and Society*, *Management Accounting*, *Advances in Accounting*, *Petroleum Accounting and Financial Management Journal*, *The International Journal of Accounting*, and other journals. He is the coauthor of *Measurement, Accounting and Organizational Information* and *Contemporary Issues in Cost and Managerial Accounting*. He has contributed chapters to *Corporate Financial Accounting: Text and Cases*, *Handbook of Accounting for Natural Resources*, *Evaluation of Human Service Programs*, *Sage Criminal Justice System Annuals* and other books. Dr. Grove was also the corecipient of a Peat, Marwick, Mitchell Foundation Research in Auditing Grant and is a member of the American Accounting Association, the American Institute of Certified Public Accountants, the Institute of Management Science, The American Society for Quality Control, the Institute of Management Accountants, and the Petroleum Accountants Society. He is currently the recipient of the Piccinati Endowed Professorship, the Distinguished Scholar Award, and the U.S. West Willemssen Research Professorship at the University of Denver.



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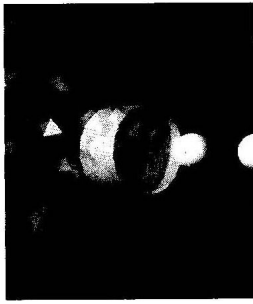
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