



Sixth Edition

ADVANCED ACCOUNTING

Concepts
and
Practice

Arnold J. Pahler
Joseph E. Mori

Sixth Edition

ADVANCED ACCOUNTING

Concepts and Practice

Arnold J. Pahler

San Jose State University

Joseph E. Mori

San Jose State University



THE DRYDEN PRESS
HARCOURT BRACE COLLEGE PUBLISHERS

FORT WORTH PHILADELPHIA SAN DIEGO NEW YORK AUSTIN ORLANDO SAN ANTONIO
TORONTO MONTREAL LONDON SYDNEY TOKYO

EXECUTIVE EDITOR

Mike Reynolds

ACQUISITIONS EDITOR

Sara Tenney

DEVELOPMENTAL EDITOR

Van Strength

PROJECT EDITOR

Michele Tomiak

ART DIRECTOR

Linda Wooton

PRODUCTION MANAGER

Carlyn Hauser

PERMISSIONS EDITOR

Annette Coolidge

PRODUCT MANAGER

Craig Johnson

COPY EDITOR

JaNoel Lowe

COMPOSITOR

ETP Harrison

TEXT TYPE

10/12 Palatino

Cover photo © David Sharpe, Inc.

Copyright © 1997, 1994, 1991, 1988, 1985, 1981 by Harcourt Brace & Company

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopy, recording, or any information storage and retrieval system, without permission in writing from the publisher.

Requests for permission to make copies of any part of the work should be mailed to: Permissions Department, Harcourt Brace & Company, 6277 Sea Harbor Drive, Orlando, Florida 32887-6777.

Address for Editorial Correspondence

The Dryden Press, 301 Commerce Street, Suite 3700, Fort Worth, TX 76102

Address for Orders

The Dryden Press, 6277 Sea Harbor Drive, Orlando, FL 32887-6777

1-800-782-4479, or 1-800-433-0001 in Florida

ISBN: 0-03-018612-9

Library of Congress Catalog Card Number: 96-85081

Publications of the AICPA quoted herein are copyright © by the American Institute of Certified Public Accountants. Reprinted by permission. Page 1153 constitutes a continuation of this copyright page.

IBM® is a registered trademark of International Business Machines Corporation.
Lotus® and 1-2-3® are registered trademarks of Lotus Development Corporation.
Excel® is a registered trademark of Microsoft Corporation.

Printed in the United States of America

7 8 9 0 1 2 3 4 5 039 9 8 7 6 5 4 3 2

The Dryden Press

Harcourt Brace College Publishers

THE DRYDEN PRESS SERIES IN ACCOUNTING

INTRODUCTORY

Bischoff
Introduction to College Accounting
Third Edition

COMPUTERIZED

Wanlass
Computer Resource Guide: Principles of Accounting
Fourth Edition

FINANCIAL

Hanson and Hamre
Financial Accounting
Eighth Edition

Porter and Norton
Financial Accounting: The Impact on Decision Makers

Porter and Norton
Financial Accounting: The Impact on Decision Makers
Alternate Edition

Stickney and Weil
Financial Accounting: An Introduction to Concepts, Methods, and Uses
Eighth Edition

MANAGERIAL

Maher, Stickney, and Weil
Managerial Accounting: An Introduction to Concepts, Methods, and Uses
Sixth Edition

INTERMEDIATE

Williams, Stanga, and Holder
Intermediate Accounting
Fifth Edition

ADVANCED

Pahler and Mori
Advanced Accounting
Sixth Edition

FINANCIAL STATEMENT ANALYSIS

Stickney
Financial Reporting and Statement Analysis: A Strategic Perspective
Third Edition

AUDITING

Guy, Alderman, and Winters
Auditing
Fourth Edition

Rittenberg and Schwieger
Auditing: Concepts for a Changing Environment
Second Edition

THEORY

Bloom and Elgers
Foundations of Accounting Theory and Policy: A Reader

Bloom and Elgers
Issues in Accounting Policy: A Reader

REFERENCE

Bailey
Miller Comprehensive GAAS Guide
College Edition

Williams
Miller Comprehensive GAAP Guide
College Edition

GOVERNMENTAL AND NOT-FOR-PROFIT

Douglas
Governmental and Nonprofit Accounting: Theory and Practice
Second Edition

PREFACE

The sixth edition of *Advanced Accounting: Concepts and Practice* has been substantially revised in the following ways.

I

NEW PRONOUNCEMENT-RELATED CHANGES

The text reflects the latest FASB, GASB, and AICPA pronouncements and exposure drafts pertinent to the topics covered:

SFAS No. 124, "Accounting for Certain Investments Held by Not-for-Profit Organizations" (November 1995).

SFAS No. 119, "Disclosure About Derivative Financial Instruments and Fair Value of Financial Instruments" (October 1994).

Proposed SFAS, "Consolidated Financial Statements: Policy and Procedures" (October 1995). In May 1996, the FASB revised its position on certain proposals in this document.

Proposed SFAS, "Accounting for Derivative and Similar Financial Instruments and for Hedging Activities" (June 1996).

Proposed SFAS, "Reporting Comprehensive Income" (June 1996).

Proposed SFAS, "Reporting Disaggregated Information about a Business Enterprise" (January 1996).

Proposed SGAS, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools" (March 1996).

AICPA Audit and Accounting Guide, "Not-for-Profit Organizations" (June 1996).

AICPA Audit and Accounting Guide, "Health Care Organizations" (June 1996).

PROPOSED NEW STANDARD ON CONSOLIDATION POLICY AND PROCEDURES (CHAPTERS 1, 3, 6, AND 13)

In October 1995, the FASB issued the exposure draft "Consolidated Financial Statements: Consolidation Policy and Procedures." When finalized, this new FASB standard will supersede both (1) *Accounting Research Bulletin No. 51, "Consolidated Financial Statements"* (issued in 1951), and (2) *Statement of Financial Accounting Standard No. 94, "Consolidation of All Majority-owned Subsidiaries"* (a 1987 amendment to ARB No. 51). The major changes proposed in this exposure draft would

- Broaden the existing consolidation rules to conform to those of the Securities and Exchange Commission so that consolidation is required whether control exists by *legal means* (owning a majority voting interest) or *nonlegal means* (having financial arrangements that effectively achieve control). (This issue is contained to portions of Chapters 1 and 3 in this text.)
- Require use of the *economic unit concept* rather than the *parent company concept*, an issue that exists only for less than 100%-owned *acquired* subsidiaries. (This issue is contained to portions of Chapters 3, 6, and 13 of this text.)

In May 1996, the FASB slightly modified its position on certain issues in the October 1995 exposure draft in response to concerns raised by respondents and

participants at the public hearings held in February 1996. **The only substantive May 1996 change was to require the imputing of goodwill to a noncontrolling interest to prevent possible "gaming" abuses.** (This issue is contained to only a portion of Chapter 6 and all of Chapter 13 of this text.)

Because the FASB could finalize its consolidation policy and procedures rules in early 1997, **the consolidation rules we present and discuss in this text are the ones set forth in the FASB's May 1996 working draft document.** (As this book goes to print, the FASB is deliberating between going to a final statement or a *revised* exposure draft.)

PROPOSED NEW STANDARD ON DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING (CHAPTER 17)

In June 1996, after ten years of intensive research and study, the FASB published for public comment an exposure draft titled "Accounting for Derivative and Similar Financial Instruments and for Hedging Activities." This proposed statement would (1) **amend SFAS No. 52 and SFAS No. 107** and (2) **supersede SFAS No. 80, SFAS No. 105, and SFAS No. 119.** (The FASB's timetable is to issue this standard in the second quarter of 1997.)

Because of extensive participation by industry and practitioners prior to the issuance of this exposure draft, the FASB has indicated that it expects this proposed standard to be enacted largely intact. The proposed standard would become effective for fiscal years beginning after December 15, 1997.

Of the three categories of foreign exchange (FX) exposures we discuss in Chapter 17, "Using Derivatives to Manage Foreign Exchange Exposures," substantive rule changes are proposed only for the *hedges of forecasted transactions* category. Accordingly, **our discussion of the treatment of FX gains and losses on *hedges of forecasted transactions* is based on this proposed standard.**

REVISED AICPA ACCOUNTING AND AUDIT GUIDES FOR NOT-FOR-PROFIT ORGANIZATIONS AND HEALTH-CARE ORGANIZATIONS (CHAPTERS 26 AND 27)

These new guides were issued in mid-1996, and we discuss them fully in Chapters 26 and 27. Of significance is that the new Health Care Organizations (HCOs) guide (1) applies to both *private* and *public* HCOs and (2) requires that financial reporting for both *private* and *public* HCOs be on an *aggregated basis*, which is consistent with SFAS No. 117, "Financial Statements of Not-for-Profit Organizations" (before, reporting could be on an *aggregated* or *disaggregated* basis).

As a result of the issuance of the SFAS No. 117, 116, and 124 and these audit guides, we were able to substantially simplify and streamline material in this edition (reducing the number of pages devoted to this material from 120 to 72, a 40% decrease).

II

ORGANIZATIONAL AND PEDAGOGICAL CHANGES

EQUAL PROMINENCE GIVEN TO THE COST METHOD (CHAPTERS 2, 3, 6, 9, 10, 11, AND 12)

Because of the continued extensive use in practice of both the *cost method* and the *equity method*, we now give equal prominence to both methods in Chapters 2 and 3 (the relatively simple situations involving *parent-created* subsidiaries), Chapter 6 (the more complex situation involving *acquired* subsidiaries), and Chapters 9–12

(intercompany transactions). Problems requiring consolidation worksheets now present consolidation data in a unique manner that allows students to use either the *cost method* or the *equity method* and readily see how the parent's financial statements differ under each method.

DISCUSSION OF PARTIALLY OWNED CREATED SUBSIDIARIES DISCUSSED SEPARATELY FROM ACQUIRED SUBSIDIARIES

To introduce major concepts on a full step-by-step basis, we now discuss noncontrolling interest situations first in the relatively simple situation in which the parent *creates* a partially owned subsidiary. Accordingly, Chapter 3 is a newly designed chapter that is a logical extension of Chapters 1 and 2, both of which deal with 100%-owned *created* subsidiaries. Noncontrolling interest situations involving *acquired* subsidiaries are discussed in Chapter 6, thus enabling the emphasis in that chapter to be entirely on the *change in basis of accounting* concept.

Chapter 3 also contains the more involved discussion of controlling a subsidiary by *nonlegal means* (financial arrangements); the simpler situation of control by *legal means* (owning a majority voting interest) is discussed in Chapter 1.

Accounting for *unconsolidated* subsidiaries (formerly in Chapter 2) was moved to Chapter 3 to balance more evenly the technical material in Chapters 2 and 3.

EXPANDED DISCUSSION OF INTRODUCTION TO INTERCOMPANY TRANSACTIONS PLACED IN A SEPARATE CHAPTER

To give students the biggest and broadest possible picture of intercompany transactions before immersing them in detailed intercompany transaction elimination entry procedures, we greatly expanded the material that describes the nature, types, and **operational importance** of these transactions. Formerly the first part of the intercompany inventory transfer chapter, this material is now in a self-contained chapter, Chapter 9.

MOVING THE INCOME TAXES, EARNINGS PER SHARE, AND CASH FLOWS TOPICS INTO APPENDICES

The discussion of these topics (Chapter 13 in the fifth edition) has been substantially simplified and streamlined as well as separated and moved to appendices of the chapters in which the related financial reporting topics are discussed (Chapters 3, 5, 6, 7, 8, and 19).

EXPANDED DISCUSSION OF USING DERIVATIVES TO MANAGE FOREIGN CURRENCY EXPOSURES (CHAPTER 17)

To make the material on translation of foreign currency *transactions* less intimidating to students, we placed the discussion of FX forwards and FX option contracts in a separate chapter, Chapter 17. We also standardized and simplified the account descriptions used to record FX forwards and FX option contracts.

More important, we added a **general discussion of derivative financial instruments** so that students obtain a broader understanding of (1) the unique *characteristics* and *features* of derivatives in general—not just FX forwards and FX options—and (2) the various types of exposures that can exist (*market risk*, *credit risk*, and *liquidity risk*). We also greatly expanded our discussion of the FASB-mandated disclosures required for FX derivatives.

SIMPLER MANNER OF PRESENTING THE CURRENT RATE METHOD AND THE TEMPORAL METHOD (CHAPTERS 18 AND 19)

We substantially reorganized this material so that students learn on a step-by-step basis the two translation methods allowed under *SFAS No. 52*. Accordingly, the *current rate method* is discussed entirely in Chapter 18 (along with hedging a *net asset position*). The *temporal method* is discussed entirely in Chapter 19 (along with hedging a *net monetary position*). Tax reporting issues are discussed in an appendix to each chapter.

EXPANDED DISCUSSION OF THE SEC'S ENFORCEMENT POWERS (CHAPTER 22)

To make the rather technical material in Chapter 22 come alive as much as possible, we added an in-depth discussion of the procedures the SEC uses to exercise its enforcement powers (based on our discussions with SEC enforcement office personnel).

EXPANDED DISCUSSION OF GOVERNMENTAL MEASUREMENT FOCUS AND BASIS OF ACCOUNTING (CHAPTER 24)

We extensively revised and expanded our discussion in Chapter 24 of "what to measure" and "how to measure it" to better show that the so-called *operating statement* is *not* really a true operating statement. We also extensively revised this chapter's introductory material and streamlined the discussion of revenues and expenditures.

EXPANDED DISCUSSION OF THE GASB'S MAJOR CURRENT PROJECT INVOLVING A REEXAMINATION OF GOVERNMENTAL FINANCIAL REPORTING (CHAPTER 25)

In Chapter 25's appendix, we greatly expanded our discussion of the GASB's current ongoing efforts to reexamine governmental financial reporting. These efforts involve the following two broad areas:

- The Financial Reporting Model: *Dual-Perspective Reporting* versus *Single-Perspective Reporting*.
- Measurement Focus and Basis of Accounting (*SGAS No. 11*).

FULL DISCUSSION OF LIMITED LIABILITY PARTNERSHIPS (LLPs) ADDED (CHAPTER 28)

In Chapter 28, we have added a full discussion of *limited liability partnerships* in light of so many public accounting partnerships' (including all of the Big Six firms in 1994) changing to this new form of organization that burst on the scene in 1994 (largely as a result of the AICPA's efforts begun in 1992).

**ACCOUNTING EDUCATION TREND CHANGES**

Much of the change in accounting education in the past few years is along the following lines: (1) less emphasis on the traditional lecture and problem-solving mode of instruction in favor of making more use of assignments involving unstructured problem settings; (2) extensive use of group work in light of recent re-

search that documents the value of students learning from one another; (3) a shift in emphasis from memorizing existing GAAP to developing critical-thinking skills; and (4) teaching accounting courses with integrated coverage of related topics in economics, finance, managerial accounting, law, tax, international business, ethics, and interpersonal skills.

Building on changes begun in the fourth edition, we have expanded the number of end-of-chapter assignments that lend themselves to teaching in this manner. These assignments consist of (1) **cases**, (2) **financial analysis problems**, and (3) **personal situations** involving **ethics** or **interpersonal skills**. For convenience they are grouped together at the end of each chapter in a section entitled "Thinking Critically" that follows the regular assignment material.

THE FINANCIAL ANALYSIS PROBLEMS (FAPs)

The financial analysis problems (FAPs) are much longer than the cases and the personal situations. When we first started using the FAPs, we were apprehensive about students becoming frustrated at trying to perform financial analysis without having an explanation or illustration in the chapter for developing "their solution." In using the FAPs the past two editions, however, the one comment we repeatedly received from students is that even though the FAPs pushed them beyond what they thought they were capable of, they were grateful for having a unique accounting course that continually forced them to think on their own and use their creativity and imagination rather than merely receive assignments for which they continually referred to the text to see "how it is done" or how an approach should be developed. Furthermore, instructors have encouraged us to develop more of these types of assignments. Also, some instructors indicated to us that by their use of these types of assignments, their course serves as a highly desirable "capstone" financial accounting course (something we also believe occurs).

A consequence of using a substantial portion of these FAPs is that fewer chapters can be assigned. Thus a trade-off question arises as to the relative value of (1) obtaining a technical understanding of issues and accounting procedures versus (2) developing critical thinking skills. Our experience in using the FAPs leads us to believe that a balanced approach is possible and that students receive far more value from being assigned a fewer number of topics and using the FAPs than by being assigned a greater number of topics and not using the FAPs. Some suggestions are set forth in the *Instructor's Resource Manual* regarding ways to obtain the maximum benefit from the FAPs—certain approaches do *not* achieve the desired consequences.

IV

UNIQUE EMPHASIS ON CREATED SUBSIDIARIES RELATIVE TO ACQUIRED SUBSIDIARIES

Two of the findings of a major Institute of Management/Financial Executive Institute joint research project (completed in late 1994) were that (1) preparing consolidated financial statements is one of the more important of 15 accounting skill and knowledge areas deemed most important for corporate entry-level accountants and (2) accounting for *external expansion* (*purchase* and *pooling-of-interests* accounting) is *not* one of these 15 skills. The 15 skills were deemed "the essence of management."

In discussing the relative importance of these two areas with many corporate controllers in the electronics industry in the "Silicon Valley" region of California, the unanimous consensus was that preparing consolidated financial statements is far more important than accounting for external expansion, which typically is encountered infrequently.

These findings confirmed our belief that our decision in the fifth edition to separate the basic conceptual issues involving consolidated financial statements from the conceptual issues associated with business combinations better reflects practices and serves students.

Accordingly, the basic concept of preparing consolidated statements for *created* subsidiaries is discussed in Chapter 1. Accounting for a parent's investment in a *created* subsidiary is discussed in Chapter 2. Accounting for *created partially owned* subsidiaries is discussed in Chapter 3. Accounting for *acquired* subsidiaries is *not* discussed until Chapter 4. By focusing solely on parent-created subsidiaries for the first three chapters, we separate the basic concept of preparing consolidated statements from the much more involved concept of changing or not changing the basis of accounting for *acquired* subsidiaries. The separation of concepts results in a *step-by-step, building-block approach to the consolidation topic*.

BETTER REFLECTION OF ACTUAL BUSINESS EXPANSION PRACTICES

Aside from the pedagogical advantage, the initial emphasis on *created* subsidiaries better reflects actual business expansion practices. The vast majority of existing subsidiaries were *not acquired* but *created* by their parent companies. (Approximately 600 subsidiaries of U.S. parent companies were created in Ireland alone in the past 25 years.) Consequently, we treat *external expansion* as one facet of preparing consolidated statements—not as an integral part around which the consolidations area is structured.

GREATER INSTRUCTOR FLEXIBILITY IN DECIDING WHAT TO GIVE PRIMARY EMPHASIS

Two recent business trends suggest that this course give more emphasis to international transactions and operations and less emphasis to business combinations. The first trend is the extensive globalization of business that has occurred during the past 15 years. The second trend is the major decline in the 1990s of the number of business combinations relative to the preceding 35 years. An additional consideration is that accounting graduates in their entry-level positions will most likely not be exposed to business combination issues, which are usually handled only at the manager and partner level in public accounting firms.

By discussing *created* subsidiaries (*internal expansion*) separately from *acquired* subsidiaries (*external expansion*), instructors now have the option of either bypassing the business combinations material (Chapters 4–8) until later in the course or omitting it altogether. The advantage to this option is that in a one-semester course, the international topics (Chapters 16–20) can become the centerpiece of the course for those instructors desiring to give greater emphasis to this topic relative to the business combinations topic.

DISCUSSION OF INTERCOMPANY TRANSACTIONS USING CREATED SUBSIDIARIES (CHAPTERS 9, 10, 11, AND 12) INSTEAD OF ACQUIRED SUBSIDIARIES

Consistent with this emphasis on *created* subsidiaries in Chapters 1–3, the textual material and illustrations in Chapters 9–12 (intercompany transactions) are based on *created* subsidiaries instead of *acquired* subsidiaries. We believe intercompany transaction topics are difficult enough for students to initially learn without being burdened by the carryforward of the change- or no-change-in-basis-of-accounting

issue that arises with *external expansion*. Accordingly, the *purchase* versus *pooling* issue is largely contained in Chapters 4–7.

Furthermore, substantially all of the consolidation problems in Chapters 9–12 are based on *created* subsidiaries, enabling these chapters to be taught before the business combinations chapters if an instructor desires to do so. (A few of the problems, however, are labeled as “comprehensive” and involve the additional complexity of either *purchased* or *pooled* subsidiaries so that instructors have the flexibility of integrating these situations into the intercompany transactions topics if they desire.)

V

OTHER FEATURES

CURRENT ARTICLES

We have expanded to 13 the number of current articles from business magazines and newspapers as follows:

- Chapter 1 “AT&T Won’t Cover Eo’s Debts,” *San Jose Mercury News*
- Chapter 3 “Accountant Metcalf Knew Firsthand Give and Take of Taxes,” *The Wall Street Journal*
- Chapter 4 “Hostile Takeovers Are Revived, and Some Embrace ‘Bear Hug,’” *The Wall Street Journal*
- Chapter 7 “AT&T Pools with NCR—\$5.7 Billion of Goodwill Avoided,” *The Wall Street Journal*
- Chapter 9 “The Corporate Shell Game,” *Newsweek*
- Chapter 16 “Clashing Values,” *San Jose Mercury News*
- Chapter 16 “All Accountants May Speak the Same Language,” *The Wall Street Journal*
- Chapter 17 “Derivatives Could Hedge Career Growth,” *The Wall Street Journal*
- Chapter 22 “Votes Today, Taxes Tomorrow,” *Forbes*
- Chapter 26 “The Accounting Games Charities Play,” *Forbes*
- Chapter 26 “Unlikely Hero, a Persistent Accountant Brought New Era’s Problems to Light,” *The Wall Street Journal*
- Chapter 28 “Partnership Structure Is Called in Question as Liability Risk Rises,” *The Wall Street Journal*
- Chapter 30 “Behind the Fall of Laventhol,” *Forbes*

INTEGRATION OF INTERNATIONAL GAAP PERSPECTIVES

More brief capsules of international GAAP have been added for the consolidation and foreign currency topics so that students can place U.S. GAAP in perspective relative to GAAP around the world. The capsules are:

- Chapter 1 Foreign Consolidation Practices
- Chapter 2 Widespread Use of Parent-Company-Only Statements Overseas
- Chapter 3 Manner of Presenting Noncontrolling Interests in Foreign Countries
- Chapter 3 Basis of Control for Consolidation
- Chapter 4 Foreign Goodwill Accounting Practices
- Chapter 7 Pooling of Interests Practice Around the World
- Chapter 19 Worldwide Translation Practices

HISTORICAL DEVELOPMENT OF GAAP CAPSULES

The following historical development of GAAP capsules are included:

- Chapter 4 Goodwill
- Chapter 7 Pooling of Interests

INTEGRATION OF ETHICS

Numerous ethics cases, many of which relate to topics discussed, are included in the "Personal Situations" assignment material at the end of the chapters.

VI STUDENT-ORIENTED FEATURES

The following is a list of sixth edition features designed to heighten students' interest and make the text easy to read and use:

1. A list of **key learning objectives** to accompany the **topic outline** preceding each chapter.
2. A literary, anecdotal, or humorous **chapter-opening quotation** for each chapter.
3. A **chapter overview** introducing each chapter.
4. Inclusion of more **relevant articles** than ever before from *Forbes*, *Newsweek*, and *The Wall Street Journal* so that students can better relate the material to current events.
5. Use of **roman numerals** to distinguish major chapter sections so that students can more readily find topics.
6. Extensive use of **boldface type for key terms and key concepts**.
7. Convenient **vertical format for consolidation worksheets** that uses a plus-and-minus scheme consistent with Excel® and LOTUS 1-2-3® **spreadsheet software**.
8. Clearly marked **review points** for major illustrations.
9. **End-of-chapter review sections** for each chapter that include: (a) a **summary of key points**; (b) a **glossary of new terms**; (c) **demonstration problems and solutions** in key consolidation chapters (Chapters 5 and 6); and (d) **multiple-choice self-study questions**.
10. **Descriptive overviews** of all exercises, problems, cases, financial analysis problems, and personal situations.
11. Placement of **cases, financial analysis problems, and personal situations** in a readily identifiable section called "**Thinking Critically**."
12. Placement of **chapter appendix material** after *all* chapter assignment material.
13. **Checklist of key figures** for both exercises and problems on the inside covers for easy reference.
14. Use of a **marginal icon** to identify problems that can be worked on the computer using the spreadsheet software models provided to adopters.
15. **Display of dates** in the assignment material in a graphic manner (12/31/X1) rather than in a *nongraphic* manner (December 31, 19X1) for greater ease of use.

VII**ANCILLARIES**

The following updated ancillaries, all written and revised by the authors, are available with this edition:

SOLUTIONS MANUAL To assist instructors in evaluating and selecting assignment materials, the *Solutions Manual* contains a description of each exercise, problem, case, financial analysis problem, and personal situation. The **relative difficulty** and **estimated time for completion** of the assignment materials are also included.

INSTRUCTOR'S RESOURCE MANUAL AND TESTBOOK The manual is divided into five parts:

- Part I consists of **course coverage considerations**.
- Part II contains a master list of both **teaching transparencies** for lectures and **problem solution transparencies** that accompany the text.
- Part III is an **instructor's introduction to the spreadsheet software models** that are provided free to instructors and students.
- Part IV contains **teaching-related materials for each individual chapter**. The materials consist of (1) teaching suggestions (including additional items of current interest to students), (2) descriptions of assignment material (including level of difficulty and estimated times), (3) a list of selected readings, and (4) a list of transparencies provided.
- Part V is a **test bank** for each chapter of the text. The test bank is highly accessible as a result of grouping items by subtopics and is also available on EXAMaster software, which is easy to install and use.

TRANSPARENCIES OF SELECTED PROBLEM SOLUTIONS For nearly all problems involving consolidation or foreign currency translation worksheets, a solutions transparency is available of that worksheet. In addition, selected solutions transparencies are provided for certain other chapters.

TRANSPARENCIES FOR TEACHING Teaching transparencies for use in lecturing on chapter material are available for selected chapters.

WORKING PAPERS Working papers are provided for selected problems in Chapters 2, 3, 5–7, 9–13, 18, 19, and 28.

STUDY GUIDE The *Study Guide* contains approximately 65 study items per chapter, grouped into (1) chapter highlights, (2) completion statements, (3) true-or-false statements, (4) *conceptual* multiple-choice questions, (5) *application* multiple-choice questions, and (6) problems (for Chapters 5–7 only).

SPREADSHEET SOFTWARE MODELS A master diskette is available free to adopting instructors. The models on the diskette are designed for use on IBM® personal computers and compatibles with Excel (version 4.0 or higher) or LOTUS 1-2-3 (version 2.0 or higher) software. **Excel users must instruct Excel to read all files.** Approximately 60 problems from the text can be worked on the computer using this software, in 15 class-tested models for 15 chapters. No computer experience is required; each model has its own on-screen instructions that are displayed above the worksheet area. Each problem that can be worked using one of the models is identified with a spreadsheet icon in the margin of the book.

To give students the opportunity to design a template of their own, program some macros for this model, and create logic functions for this model, an assignment containing detailed instructions is provided in Chapter 2 (Problem 2–8). We

also have included an assignment in Chapter 10 containing detailed instructions (Problem 10-7) on how to automate the entire consolidation process when inter-company transactions exist.

The Dryden Press may provide complimentary instructional aids and supplements or supplement packages to those adopters qualified under our adoption policy. Please contact your sales representative for more information. If as an adopter or potential user you receive supplements you do not need, please return them to your sales representative or send them to:

Attn: Returns Department
Troy Warehouse
465 South Lincoln Drive
Troy, MO 63379

VIII

ACKNOWLEDGMENTS

We are indebted to the following individuals who gave generously of their time and provided many fine suggestions in reviewing material for the sixth edition before publication:

Orapin Duangploy	University of Houston, Downtown
Francene Feldbrugge	San Jose State University
George J. Haytko	San Jose, California
Stuart S. Karlinsky	San Jose State University
Stanley Martens	DePaul University
Mallory L. McWilliams	San Jose State University
Michael E. Solt	San Jose State University
Frederic M. Stiner	University of Delaware
Charles A. Tritschler	Purdue University
Charles F. Vincent	San Jose State University (Emeritus)
Larry M. Walther	University of Texas, Arlington

We are grateful to Charlie Tritschler of Purdue University, who, in addition to having reviewed many of the substantially revised consolidation and foreign currency chapters, effectively served as a consulting technical editor. He gave us considerable guidance in reorganizing the sequence of the various consolidation and foreign currency topics and in developing new material that discusses derivative financial instruments in a broad context (Chapter 17). We consider ourselves extremely fortunate to have been able to draw and learn from his extensive teaching experience, remarkable insights, and unequalled expertise in foreign currency translation and derivative financial instruments. He spent so many hours with us discussing technical matters and pedagogical approaches that it seems he ran not only an extra lap but an extra race as well. Charlie, you are a true professional in the highest sense of the word and an absolute gem of a person. To the extent that these chapters have been improved, great credit goes to you. We, the authors, of course, assume full responsibility for any shortcomings in these areas.

We express appreciation to the American Institute of Certified Public Accountants, the Financial Accounting Standards Board, the Governmental Accounting Standards Board, and the Government Finance Officers Association for their permission to quote material from their pronouncements and various other publications. We also thank the American Institute of Certified Public Accountants for their permission to use and adapt material from the CPA examinations.

We also express our appreciation to many partners and managers of the Big 6 international accounting firms to whom we made numerous inquiries concerning current accounting issues and practices.

Finally, we express our appreciation to Mike Reynolds, acquisitions editor; Van Strength, our dedicated and conscientious developmental editor; JaNoel Lowe, our in-a-class-by-herself copy editor; Linda Wooton, our talented art and design director; Michele Tomiak, our delightful project editor; Carlyn Hauser, our energetic production manager; and Annette Coolidge, our thorough permissions editor. Their commitment and professionalism were greatly appreciated.

We encourage and welcome all comments from users of the sixth edition.

Arnold J. Pahler

Joseph E. Mori

BRIEF CONTENTS

PART I	CONSOLIDATED FINANCIAL STATEMENTS: INTERNAL EXPANSION ISSUES	1
	1 Wholly Owned Subsidiaries: At Date of Creation	1
	2 Wholly Owned Subsidiaries: Postcreation Periods	31
	3 Partially Owned Subsidiaries and Unconsolidated Subsidiaries	75

PART II	CONSOLIDATED FINANCIAL STATEMENTS: EXTERNAL EXPANSION ISSUES	107
	4 Introduction to Business Combinations	107
	5 The Purchase Method: At Date of Acquisition—100% Ownership	155
	6 The Purchase Method: Postacquisition Periods and Partial Ownerships	199
	7 The Pooling of Interests Method	247
	8 New Basis of Accounting	291

PART III	CONSOLIDATED FINANCIAL STATEMENTS: INTERCOMPANY TRANSACTIONS	313
	9 Introduction to Intercompany Transactions	313
	10 Intercompany Inventory Transfers	341
	11 Intercompany Fixed Asset Transfers	391
	12 Intercompany Bond Holdings	423

PART IV	CONSOLIDATED FINANCIAL STATEMENTS: OTHER TOPICS	453
	13 Changes in a Parent's Ownership Interest	453
	14 Indirect and Reciprocal Holdings	477
	15 Reporting Disaggregated Information	497

PART V FOREIGN TRANSACTIONS AND FOREIGN OPERATIONS 529

16	Translating Foreign Currency Transactions	529
17	Using Derivatives to Manage Foreign Currency Exposures	563
18	Translating Foreign Statements: The Current Rate Method	615
19	Translating Foreign Statements: The Temporal Method and the Functional Currency Concept	661
20	Translating Foreign Statements: Evaluating the Validity of the Functional Currency Concept	699

PART VI MISCELLANEOUS CORPORATE REPORTING TOPICS 725

21	Interim Reporting	725
22	Securities and Exchange Commission Reporting	745
23	Troubled Debt Restructurings, Bankruptcy Reorganizations, and Liquidations	779

PART VII GOVERNMENTAL AND NONPROFIT ORGANIZATIONS 827

24	Governmental Accounting: Basic Principles and the General Fund	827
25	Governmental Accounting: Special-Purpose Funds and Account Groups ...	885
26	Not-for-Profit Organizations: Introduction & <i>Private</i> NPOs	945
27	Not-for-Profit Organizations: <i>Public</i> NPOs	979

PART VIII PARTNERSHIPS AND ESTATES AND TRUSTS 1023

28	Partnerships: Formation and Operation	1023
29	Partnerships: Changes in Ownership	1061
30	Partnerships: Liquidations	1089
31	Estates and Trusts	1125