

INTERMEDIATE ACCOUNTING

WILLIAMS STANGA HOLDER



FIFTH EDITION

INTERMEDIATE ACCOUNTING

FIFTH EDITION

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INTERMEDIATE ACCOUNTING

FIFTH EDITION



We dedicate this work to

Our wives:

Elaine Williams Josie Stanga Carolyn Holder

*and our families
in appreciation of their support*

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Preface

The decade of the 1990s will be remembered as the decade of change in accounting education. Never before has the discipline placed so much emphasis on changing the education model for preparing students to enter the accounting profession.

The need for change in accounting education has resulted from several factors. The body of knowledge that students entering the profession must master is growing at an unprecedented rate. At the same time, the skills required for success in accounting practice—whether in public accounting, industry, government, or education—are expanding. No longer is it enough for students to only have a mastery of technical accounting material. Today they are expected to develop a broad background in areas such as computer science, economics, and finance, while at the same time developing high-level interpersonal skills, particularly the ability to communicate well and work in teams.

In addition to authoring *Intermediate Accounting*, we have been participants at the forefront of recent changes in accounting education. Jan Williams is currently Director of Education of the American Accounting Association and represents that organization as a member of the Accounting Education Change Commission (AECC). The AECC, an organization funded by the Big Six accounting firms, is intended to be a catalyst for change in accounting education. Jan has also been actively involved in the AICPA's program to change accounting education via the 150-hour education requirement. Keith Stanga has been involved in accounting education change through his role as an administrator of an accounting program. Keith currently serves as Head of the Department of Accounting and Business Law at The University of Tennessee. He and his faculty colleagues are working together in several specific areas to continuously improve the educational experience of accounting students at The University of Tennessee. William Holder has been deeply involved in the comprehensive curriculum revision project at the University of Southern California for the past five years. His efforts have been focused directly on the subject matter of this text as it relates to the redesigned curriculum. In addition, Bill's involvement with standard setting and his consulting experience with accounting litigation is reflected where appropriate to help put the student's mind on these aspects of financial accounting practice. We all teach intermediate accounting on a regular basis and are well aware of the importance of presenting high-level technical material in an interesting and challenging way.

From the first edition, the objective in writing this textbook was to provide the market with a book that maintains a unique balance between explanation of applied accounting practice and the conceptual framework on which practice is based. This objective, established in 1984, remains consistent with current trends in accounting education. With the help of users, reviewers, students, colleagues, and our publisher, we have sought to continuously improve our presentation with new material and proven pedagogical techniques.

The need for change in accounting education does not mean that traditional approaches to teaching and learning have no merit. We are sensitive to traditional needs of many faculty and students. Our goal has always been to blend the best of tradition in intermediate accounting with the innovations of the present and future. We believe the fifth edition of *Intermediate Accounting* accomplishes this goal.

FEATURES OF THE FIFTH EDITION

Retained Unique Approach in Early Chapters

We have retained the three early chapters that lay the foundation of balance between theory and practice for students.

- In Chapter 2, we present the broad accounting principles that underlie specific procedures currently used in the preparation of financial statements. We highlight these principles

throughout the book in marginal heads as their application to specific reporting practices are illustrated.

- In Chapter 3, we introduce the student to the nature and measurement of the elements of financial statements, emphasizing alternatives to current practice at a level understandable to students at this point in their study of financial accounting.
- Chapter 4 reviews the four basic financial statements and emphasizes the important feature of articulation.

Learning Enhancements

We retained a unique feature we have had since the first edition—*noting accounting principles throughout the textbook in the margins*. Instructors have consistently said this feature helps students identify and understand the overall impact of the principles on accounting concepts and practice.

Boxed articles extend the subject of the chapter to show students actual business applications, often from perspectives outside the accounting profession such as those of investors and creditors. We have continued to *improve our flowcharts, diagrams, and other graphics* that summarize text material and enhance students' learning. As a part of this effort to provide greater visual appeal and permit more alternatives for emphasis, we have published this edition in a *new four-color format*.

Emphasis on Contemporary Issues

We stress contemporary financial reporting issues throughout the book in several ways. We provide students with *Kellogg's Financial Statements* as an appendix to the book and as the primary company referenced throughout the book, replacing Strawbridge & Clothier from the previous edition. In the fifth edition, we have *expanded references to international accounting*, pointing out varying reporting practices in different parts of the world. Where appropriate, we emphasize *how current financial reporting standards provide information that is useful in predicting future cash flows*, a primary objective of financial reporting as indicated in the FASB's conceptual framework. The emphasis on *current research*, which has characterized earlier editions, has been strengthened. Many items in the assignment materials include written requirements, and many of the *judgment cases have ethical considerations* similar to those students are likely to confront early in their professional careers. All of these features are intended to emphasize contemporary issues that are important for the preparation of future professionals.

Increased Emphasis on Real-World Applications

Each chapter opens with a carefully selected vignette and photo to interest students and to emphasize the importance of chapter concepts. Throughout the book, we use extensive examples, drawn from published financial statements of well-known companies. Realistic cases and material have been prepared that model the accounting practice.

New Financial Reporting Cases

Appearing at the end of Chapters 7 through 26, these cases are characterized by excerpts from published financial statements of actual companies. The questions following the cases require students to respond to the kinds of problems they are likely to face in practice, which require interpretation and have possible judgment implications.

Text Reorganized into Six Major Sections from Five

Intermediate accounting includes many procedures. We chose to organize the book into six major parts, or sections, to provide students with a framework to organize the material—a roadmap of sorts. The fifth edition is organized as follows:

- Part I—Theoretical Foundation for Financial Reporting (Chapters 1–4)
- Part II—Tools of Accounting (Chapters 5–6)
- Part III—Asset Accounting (Chapters 7–13)
- Part IV—Liability and Stockholders' Equity Accounting (Chapters 14–18)
- Part V—Reporting Operations and Cash Flows (Chapters 19–22)
- Part VI—Advanced Measurement and Disclosure Issues (Chapters 23–26)

A newly organized Part V includes discussion of issues related to reporting operations and cash flows. Of particular interest is Chapter 21, which covers the theoretical construct underlying revenue recognition and illustrates the application of that theory in the preparation of income statements in complex situations.

In response to users and reviewers, we added a sixth section, titled Advanced Measurement and Disclosure Issues. Chapters in this section, used in conjunction with the 1993 financial statements of Kellogg Company presented in an appendix to the book, are particularly useful to help students understand many of the most complex accounting and disclosure issues confronting the profession today.

Moved Forward Earnings per Share Coverage (Chapter 18)

Based on market feedback, we brought this coverage forward to strengthen the tie between EPS figures and debt and equity instruments that are discussed in Chapters 14–17, which directly precede it.

Extensively Updated

In the text, examples, illustrations, and assignment and test material, we have taken care to provide students and instructors with current material.

Of particular importance is the revision of Chapter 10 on the subject of investments. It reflects recent changes by the FASB to incorporate current value information in the financial statements. The broader implications of this development for financial reporting, as well as the specific application for investment accounting, are explored in Chapter 10.

In Chapter 21, we review many topics related to income presentation of a comprehensive income statement, which includes all of the irregular income items that the students will have studied.

Emphasis on Professional Judgment

In today's complex business environment, professional judgment by accountants is particularly important. Throughout the text, we refer to the importance of professional judgment. Each chapter ends with a brief discussion of the judgment implications of the subject of the chapter and is supported by judgment cases in the problem material. These features provide the instructor with an opportunity to remind students that professional accountants are constantly confronted with the need to apply carefully reasoned judgment as they carry out their responsibilities in the financial reporting process.

SUPPORTING PACKAGE MATERIAL

For the Student

- *Working Papers*
- *Checklist of Key Figures*
- *Improved! Spreadsheet Templates for Selected Assignment Problems*
- *Improved! Study Guide with Lotus 1-2-3 Applications Manual* In response to primary research with intermediate students, this edition of the study guide now includes several new features. The manual is prepared by James Rothwell, Ouachita Baptist University, and James Reeve, University of Tennessee.

- *Practice Set, Classic Toys and Trains* This practice set allows the student to explore transactions of a small corporate merchandising company. It includes special journals and direct and indirect statements of cash flows. The practice set is available in manual or computerized versions and is prepared by Sandra Pelfrey and Gadis J. Dillon.

For the Instructor

- *New! Annotated Instructor's Edition*
- *Improved! Instructor's Manual and Instructor's Manual on disk* For those instructors who wish to modify this material for their class notes, the instructor's manual is available on 3.5-inch disk. The instructor's manual is written by Jane Campbell of Kennesaw State College.
- *Solutions Manual*
- *Teaching Transparencies*
- *Improved! Solutions Transparencies* In this edition, these transparencies have been enlarged and redesigned.
- *Improved! Test Bank* Written by Larry A. Deppe, Westminster College, the test bank has hundreds of new questions. Many require critical thinking skills.
- *Computerized Test Bank* Available in 3.5-inch, 5.25-inch Mac and Windows versions. This software offers four ways to select questions, a range of formatting options, and the option to easily add questions.

Special Packaging and Innovative Computerized Learning Materials

As with previous editions, we have a special packaging option for the textbook and *Miller GAAP Guide: College Edition*, by Jan Williams. A new computerized version of the *GAAP Guide* will allow students who like to study with a computer to research pronouncements by topic on this new version of the *GAAP Guide*.

ACKNOWLEDGMENTS

The fifth edition of *Intermediate Accounting* would not have been successfully completed without the help of many people. We would like to recognize those who have contributed to the writing, review, revision, and publication of *Intermediate Accounting*.

One of the most useful forms of input concerning a textbook is the expert evaluation of educators who invest time and effort in reviewing the manuscript at the request of the publisher. We received many thought-provoking reviews of our first four editions and gave careful consideration to all suggestions made. We gratefully acknowledge the contributions of the following individuals who were willing to assist us as we sought to improve the overall quality of this text in the fifth edition: Alex B. Ampadu, SUNY at Buffalo; Jack Armitage, University of Nebraska at Omaha; Ronald Campbell, North Carolina A&T State; Larry Deppe, Westminster College; Larry Falcetto, Emporia State University; Lucille Genduso, Nova University; Oscar J. Holzmman, University of Miami; Kenneth R. Lambert, University of Memphis; Martha Loudder, Texas A&M University; George Mead, Michigan State University; Lucille Montondon, Southwest Texas State University; Daniel J. O'Mara, Villanova University; and Larry Walther, University of Texas at Arlington. We also wish to thank the users of the fourth edition who responded to detailed questionnaires or otherwise offered suggestions.

We must thank our student and faculty colleagues at the University of Tennessee and the University of Southern California for their advice and counsel. Many useful suggestions from these individuals have been incorporated into this revision. The direct input from those studying the text and those teaching from it is invaluable to us.

We would like to express a special thanks to those individuals who assisted in the development of our improved supplements package this edition. First, we appreciate the efforts extended by Jane Campbell (Kennesaw State College) on the instructor's manual; James

Rothwell (Ouachita Baptist University) and James Reeve (University of Tennessee) for contributions to this and previous editions of the study guide, respectively. Also, we are grateful to Larry Deppe for the significant revision to the test bank.

We also appreciate the assistance and dedication of other supplement authors and contributors. They include Sandra Bitenc, Kent Finkle, Gadis Johnson, Sandra Pelfrey, Suzanne Pinac-Ward, Chandra Schrog, and Lyn Suberly.

Throughout the text, we cite authoritative accounting literature published by the American Institute of Certified Public Accountants (AICPA) and the Financial Accounting Standards Board (FASB). We are grateful for the work done by these organizations. We also acknowledge and thank the AICPA and The Institute of Management Accounting for allowing us to adapt material from past CPA and CMA examinations.

Our text includes many financial reporting examples taken from the published financial statements of U.S. corporations. We have also included several articles from business publications. We appreciate the willingness of these organizations to allow us to use this material, which greatly enhances the learning experiences of serious students of this book.

The people at The Dryden Press have provided guidance and motivation to this revision. Those on the editorial staff—Lyn Hastert, editor-in-chief; Elizabeth Storey, acquisitions editor; Van Strength, developmental editor—have shown great personal interest in the project, and their understanding of our lives outside of writing the book has made this edition possible. We are thankful for the skill of the production team: Cheryl Hauser has been meticulous in keeping us posted of the many deadlines and changes, and we appreciate the hard work of our designer, Jeanette Barber, our production manager, Erin Gregg, and our permissions editor Shirley Webster. Finally, the sales and marketing group of Dryden deserves our thanks for the success of the book to date, and we wholly support their effort in the fifth edition under the direction of Annie Todd, product manager for accounting.

A special acknowledgment goes to our families. Much of the credit for this book rightfully belongs to them.

Jan R. Williams
Keith G. Stanga
William W. Holder

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