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2013

# ACCOUNTING DESK BOOK

The Accountant's  
Everyday Instant  
Answer Book

22<sup>nd</sup>  
Edition!

LOIS RUFFNER PLANK  
DONALD MORRIS  
BRYAN R. PLANK  
CHRISTIE PLANK CIRAULO



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## 2013 Accounting Desk Book

by Lois Ruffner Plank, Donald Morris, Bryan R. Plank, and Christie Plank Ciraulo

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### Highlights

The 2013 Accounting Desk Book is a practical working tool that provides quick, authoritative, and up-to-date answers for CPAs and Financial Services Professionals applying relevant accounting principles and standards as well as tax rules. It contains all of the important pronouncements from the FASB, GASB, PCAOB, and IASB; financial reporting presentation requirements; required and recommended disclosures; and specialized accounting topics needed to field a client's questions, brush up on the proper treatment of a transaction, or consider an engagement in a new area of practice.

Guidelines, illustrations, and step-by-step instructions simplify complex accounting issues and give public and private accountants quick answers to accounting application questions.

### 2013 Edition

- **The 22nd edition's "Governmental Accounting" update covers four new standards.** To ensure that Government Accounting Standards continue to be of high quality and are in line with the continuously evolving government environment, the GASB periodically reexamines its standards. Reexamination typically takes place after a Statement has been in place and fully implemented for at least five years. Research on the GASB's pension standards, for example, indicated opportunities for significant improvement as well as for other important practice issues of state and local governments. In June 2012, the Board approved two standards that improve the accounting and financial reporting of public employee pensions. *Statement No.*

68, *Accounting and Financial Reporting for Pensions*, revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. *Statement No. 67, Financial Reporting for Pension Plans*, revises existing guidance for the financial reports of most pension plans. On April 2, 2012, the GASB issued two Statements addressing important practice issues for state and local governments. *Statement No. 66, Technical Corrections—2012*, enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. *Statement No. 65, Items Previously Reported as Assets and Liabilities*, clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting.

- **The Federal Insurance Office (FIO) is making strides in getting organized in several areas, as reviewed in “Insurance Accounting.”** Committees have been formed, are being formed, and the FIO is joining others. The Director, who has been busy explaining the activities and accomplishments of this new government agency to Congressional committees and insurance organizations, also is accumulating a professional staff. Although FIO has myriad responsibilities, the immediate predominant focus is on international issues, involving key bilateral relationships and critical international initiatives. FIO provides the United States with a sophisticated and authoritative voice on international insurance matters. Given the current fast-paced development of international insurance supervisory standards, and the explosive growth of premium volume in emerging markets, FIO’s participation and engagement arrives at an opportune moment for U.S.-based insurance consumers and the industry.
- **A central question of accounting is whether certain costs must be capitalized or whether they may be expensed.** At what point in a building’s roof repair, for example, are the costs considered a normal repair and expensed, or the costs are extensive enough that they must be added to the cost of the building and depreciated? “*Asset Valuation for Tax Purposes*” presents a summary of new IRS guidance on this question. The IRS has issued temporary regulations that took effect on January 1, 2012 and expire on December 23, 2014 (unless made permanent). While the general rules have not changed, the IRS tries to give clarity to some of the terms used in describing the type of costs that should be capitalized, including betterment, restoration, rehabilitation, and improvement. For costs that may be expensed, the IRS gives examples of repairs and routine maintenance.

- **“Appendix K” describes the Whistleblower Program and the first cash award given.** In August 2012, the SEC issued its first monetary award from the program, when a whistleblower, who helped stop a multi-million dollar securities fraud, received nearly \$50,000. In just its first year, the whistleblower program already has proven to be a valuable tool in helping ferret out financial fraud. When insiders provide the SEC with high-quality road maps of fraudulent wrongdoing, it reduces the length of time spent investigating and saves the agency substantial resources.
- **“Recent Tax Changes” highlights the numerous Bush-era tax cuts and other measures that were set to expire at the end of 2010 but were extended through 2012, one part of the so called fiscal cliff.** Among the many changes that will occur when the Bush tax changes sun-set—pending last-minute action by Congress—are the increase in the long-term capital gains rate to 20 percent from 15 percent, the return of the itemized deduction phase-out and the dependency exemption phase-out for higher income taxpayers. Also included are the tax rate changes that will impact higher-income individuals and the end of the 15 percent tax rate on qualified dividends. The chapter on Depreciation describes the new limits for bonus depreciation and section 179 expensing.
- **“Plain Language for Government” reviews the first Plain Writing Act Report Card, released July 2012, a year from the date when the first requirement of the Plain Writing Act went into effect.** The report card was issued by the Center for Plain Language, a non-profit organization dedicated to clear communication in government, business, non-profits, and universities.
- **“Saving for a Higher Education,” has been revised and renamed. It is now called “The Finances of a Higher Education” to better reflect the majority of the content.** Although the maximum Federal Pell Grant award for the 2012–2013 Award Year remains the same at \$5,550, beginning in 2013–14 the maximum Pell Grant amount will increase each year according to the Consumer Price Index + one percent. The spending on Pell Grants has doubled and some of the changes for the 2012–2013 academic year include eligibility now being limited to 12 semesters (or 600%), regardless of when or where a student received his or her first Pell Grant.

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## vi About the Authors

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# Preface

Accounting information is complex, mirroring the complexity of the business, government, and non-profit activities it measures. It is difficult for those practicing the profession to be specialists in more than a few limited areas, let alone understand it all. Overlaying this problem is the growing influence of the international accounting community and its pursuit of convergence of accounting standards, which could lead to uniform reporting around the world. In this complex and changing environment, it is essential that the accounting practitioner have at least a glancing knowledge of many areas.

In auditing in particular, but also in tax and other areas of accounting, the practitioner must understand the industry in which the client operates including the industry's specific regulatory environment. One of the goals of the *Accounting Desk Book* is to bring together in one source, changes and updates to areas of accounting and tax compliance from across the business spectrum. While it is difficult for anyone to be an expert in all areas of accounting, it is certainly possible to be aware of recent changes across a wide range of accounting and tax issues. From recent FASB pronouncements, to the implementation of Dodd-Frank, to significant recent tax legislation, this book provides information and guidance on what is occurring on the margins. It is not a textbook or a detailed reference on a niche within accounting. Rather, it spans traditional boundaries in accounting by providing current information on financial accounting, cost accounting, tax, non-profit, governmental, and international accounting as well as related information on investments, e-commerce, ethics, the Securities and Exchange Commission, insurance accounting and much more.

## xii Preface

Because of its breadth of coverage, this work serves to introduce and update many topics. Nevertheless, in the case of other topics, on which comprehensive information is not always available, such as the treatment of independent contractors and tip income, its coverage is substantial. For many practitioners, the book proves most useful by offering a quick background update on an unfamiliar topic or area in which they have not practiced for a number of years.

It is imperative that all accountants and auditors keep pace with new laws, regulations, official pronouncements and industry guidance affecting their practice. The *Accounting Desk Book* assists the accountant in his or her effort to understand and comply with both new and existing accounting rules and regulations. The importance of current information cannot be overemphasized. Coverage of topics, applications, examples, and definitions of terms is the goal of this volume. It avoids abstract theory, technical jargon, complex “legalese” and textbook-type prose, which can needlessly complicate discussion of the rules and procedures. All topics are covered in straightforward, plain English. Discussions throughout the *Accounting Desk Book* are mostly self-contained. A review of the topics does not require reference to other sources. The table of contents clearly sets forth the subjects discussed and the index helps locate needed information rapidly.

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# Chapter 1

## Principles of Financial Statements, Disclosure, Analysis, and Interpretation

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## ¶1000 OVERVIEW

The general objective of financial reporting is to provide reliable information on resources, obligations and progress. The information should be useful for comparability, completeness and understandability. The basic features involved in financial accounting are the individual accounting entity, the use of approximation and the preparation of fundamentally related financial statements.

The financial statements—balance sheet, income statement, change in stockholders' equity and statement of cash flows, as well as segment reports and interim reports—will summarize a firm's operations and ending financial position. Analysts, investors, creditors and potential investors and creditors will analyze these documents in their decision-making processes.

## ¶1001 FAIR PRESENTATION IN CONFORMITY WITH GAAP

When a business is audited, the CPA's audit report attests to the fact that the financial statements are presented in conformity with GAAP. This means a number of things, but high in importance is the use of accrual basis accounting as opposed to cash basis, tax basis or some other comprehensive basis of accounting. As the day approaches when what constitutes generally accepted accounting principles in the U.S. (U.S. GAAP) gives way to International Financial Reporting Standards (IFRS), it is important to understand what has really changed and what has remained the same. The process of bringing U.S. GAAP and IFRS together, called convergence, means that when the transition to IFRS finally takes place, the two sets of standards, while not identical, will closely resemble each other in most major respects. This is expected to minimize the difficulty of the transition and to buffer the shock to the financial markets.

Fair presentation in conformity with GAAP requires that the following four criteria be met:

1. GAAP applicable in the circumstances have been applied in accumulating and processing the accounting information.
2. Changes from period to period in GAAP have been properly disclosed.
3. The information in the *underlying* records is properly *reflected* and *described* in the financial statements in conformity with GAAP.
4. A proper balance has been achieved between the conflicting needs to:
  - a. Disclose the important aspects of financial position and results of operation in conformity with conventional concepts, and



- b. Summarize the voluminous underlying data with a limited number of financial statement captions and supporting notes.

These criteria are fundamentally the same for U.S. GAAP and IFRS.

## ¶1003 12 PRINCIPLES OF FINANCIAL STATEMENT PRESENTATION

1. *Basic Financial Statements.* At minimum, these statements must include:
  - a. Balance Sheet
  - b. Statement of Income
  - c. Statement of Changes in Stockholders' Equity
  - d. Statement of Cash Flows
  - e. Disclosure of Accounting Policies
  - f. Full Disclosure in Related Notes

Information is usually presented for two or more periods. Other information also may be presented, and in some cases required, as supplemental information (e.g., price-level statements, information about operations in different industries, foreign operations and export sales, and major customers (segment reporting)).

2. *The Balance Sheet.* A complete balance sheet must include:
  - a. All assets
  - b. All liabilities
  - c. All classes of stockholders' equity
3. *The Income Statement.* A complete income statement must include:
  - a. All revenues
  - b. All expenses
4. *The Statement of Cash Flow.* A complete statement of cash flow includes and describes all important aspects of the company's operating, financing and investing activities.
5. *Accounting Period.* The basic time period is one year. An interim statement is for less than one year.
6. *Consolidated Financial Statements.* In the context of a parent company and its subsidiaries statements are presumed to be more meaningful than separate statements of the component legal entities. They are usually necessary when one of the group owns (directly or indirectly) over 50 percent of the outstanding voting stock. The information is presented as if it were a single enterprise.