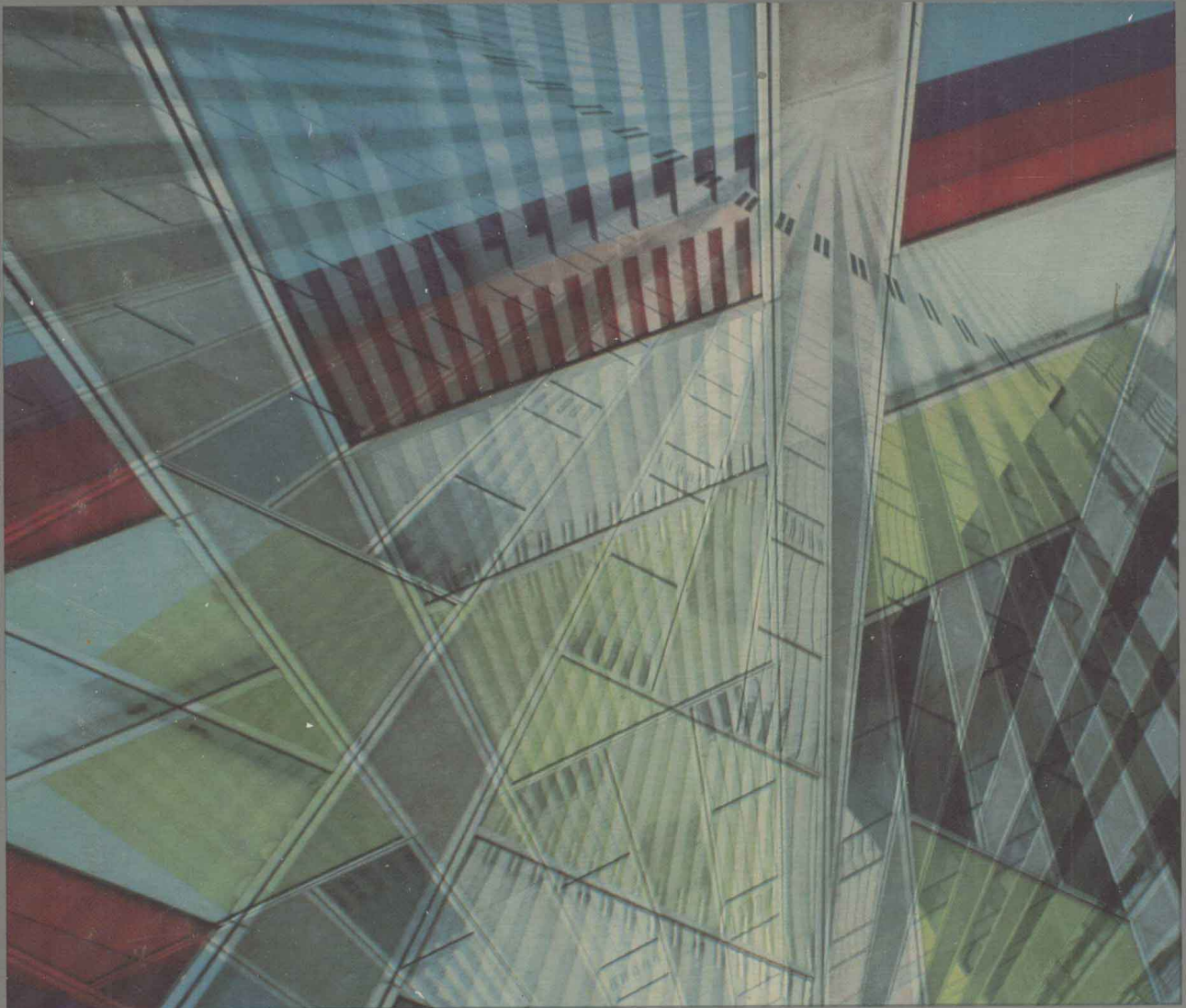


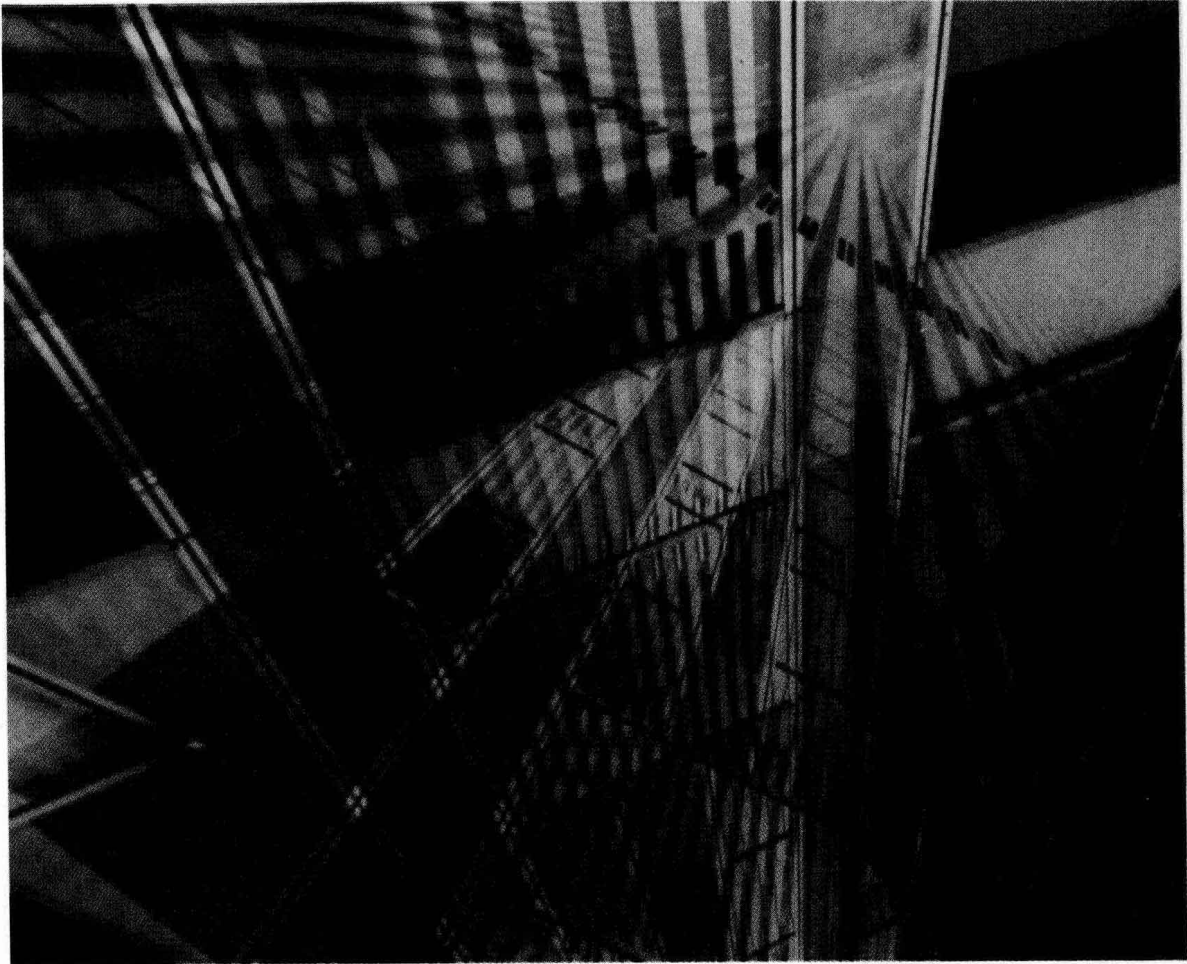
FINANCIAL ACCOUNTING



Walter B. Meigs and Robert F. Meigs

FOURTH EDITION

FINANCIAL ACCOUNTING



FOURTH EDITION

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FINANCIAL ACCOUNTING

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PREFACE

The environment of accounting is changing fast, and these environmental changes, such as continued inflation and the critical financial problems of many cities, affect the goals and the content of an introductory text in accounting. In order to function intelligently as a citizen as well as in a business of any size or type, every individual needs more than ever before a clear understanding of basic accounting concepts. In this fourth edition, we have tried to reflect the impact of inflation on accounting measurements and to suggest the direction of needed changes in accounting concepts and methods. The importance of adequate disclosure in the system of financial reporting is stressed, and attention is drawn to the need for improved accounting controls in all sectors of society.

Our goal is to present accounting as an essential part of the decision-making process for the voter, the taxpayer, the government official, the business manager, and the investor. This edition, like the preceding one, is designed for the first college-level course in accounting. In this course, instructors often recognize three general groups of students: those who stand at the threshold of preparation for a career in accounting, students of business administration who need a good understanding of accounting as an important element of the total business information system, and students from a variety of other disciplines who will find the ability to use and interpret accounting information a valuable accomplishment. During the process of revision we have tried to keep in mind the needs and interests of all three groups.

A new edition provides authors with an opportunity to add new material, to condense the coverage of topics that have declined in relative importance, to reorganize portions of the book to improve instructional efficiency, and to refine and polish the treatment of basic subject matter. We have tried to do all these things in this fourth edition.

New features of this edition

Among the many new features of this edition are:

- 1 Illustrative cases—brief descriptions of interesting business situations which tie important concepts in the textbook to events in the “real world.”
- 2 Learning objectives for each chapter, designed to focus students’ attention upon the most important topics and concepts.
- 3 Increased flexibility through the use of optional appendixes (with separate problem material) to cover the specialized topics of present value computations and consolidated financial statements.
- 4 New, open text design to enhance readability, with an increased number of diagrams to present concepts visually.
- 5 An Instructor’s Guide (separate from the Solutions Manual), with topical outlines of each chapter, an assignment guide indicating topics covered in each exercise and problem, and personal comments and observations by the authors on specific aspects of the text and of the introductory accounting course. Also included are solutions to the two parallel sets of Achievement Tests and Comprehensive Examinations.
- 6 Both printed and computer-based test banks with examination material arranged chapter-by-chapter for the entire text.
- 7 An increased number of single-concept problems and decision-oriented problems.
- 8 Thorough review of all problem material to assure emphasis of key topics and to eliminate unnecessary mathematical complexity.
- 9 A new appendix following Chapter 13 summarizing in one location the various applications of present value and demonstrating the use of present value tables.
- 10 A new appendix following Chapter 14 presenting an introductory level discussion of the basic concepts of consolidated financial statements.
- 11 Coverage of the accelerated cost recovery system (ACRS) now used to depreciate newly acquired assets for income tax purposes.
- 12 A discussion of the nature and purpose of reversing entries.
- 13 Perspective—careful effort throughout the text and problems to utilize current and realistic prices, interest rates, and profit levels.

Features carried forward from prior editions

Special qualities that are carried forward from prior editions include:

- 1 Depth of coverage. Topics are covered in a depth which will qualify the student for subsequent course work in accounting.
- 2 A reputation for accuracy in all problem material and solutions. All problems, solutions, and supplementary materials developed and tested first-hand by the authors in their own classes for introductory accounting students. This personal attention to accuracy is supplemented by independent testing by other accounting faculty.

- 3 People-oriented problems which depict the hard decisions that must be made by men and women acting as managers, investors, and in other roles.
- 4 For each chapter, a demonstration problem, a business decision problem, and a glossary of key terms introduced or emphasized in the chapter.
- 5 Emphasis on the impact of inflation upon accounting information.
- 6 The concept of present value, presented in clear and understandable terms, integrated into the discussions of the valuation of assets and liabilities.
- 7 Emphasis on internal control—how a business of any size can strengthen its system of internal control.
- 8 Evaluation of corporate profits. Are they adequate? Are they reasonable? What are the appropriate yardsticks?
- 9 Careful integration into the text and problems of the latest pronouncements of the Financial Accounting Standards Board.
- 10 The most comprehensive package of supplementary materials of any financial accounting textbook.

New topics and extensively revised chapters

Many new topics are discussed in this fourth edition. For example Chapter 4, entitled Completion of the Accounting Cycle, now includes coverage of reversing entries. Among the new topics in Chapter 5 on merchandising transactions are the net method of recording purchases, sales tax and corporate income tax accruals, and the distinction between the single-step and multiple-step formats of the income statement. In addition, this chapter has been carefully revised and reorganized. In its new form, the chapter is shorter, yet more clearly presents the basic topics of merchandising transactions and internal control.

Chapter 10 includes up-to-date coverage of the Accelerated Cost Recovery System (ACRS) and revised discussions of depreciation methods and accounting for natural resources. Two new appendixes cover the topics of accounting applications of present value and consolidated financial statements. Chapter 14, dealing with the effects of inflation, covers the constant dollar and current cost disclosure requirements of *FASB Statement No. 33*, with emphasis on the interpretation of this information by users of financial statements. Chapter 17, on income taxes, has been thoroughly revised to reflect the many recent changes in tax laws. Included are the important implications of the Economic Recovery Tax Act, the recent reductions in tax rates, the “marriage penalty,” and the proposals for future indexing of tax brackets.

In addition to covering new topics, we have revised many chapters to better target our discussions to the needs and backgrounds of introductory students. For example our coverage of corporate income statements and stockholders’ equity, formerly discussed in Chapters 7 and 8, has been moved to Chapters 11 and 12, where students are better prepared to deal with these topics. The discussions of discontinued operations, extraordinary items, and earnings per share have been revised to emphasize the interpretation of this information rather than the technical aspects of its presentation. Chapter 16, Analysis and

Interpretation of Financial Statements, includes real-world examples involving well-known corporations in order to acquaint students with realistic levels of business profits.

Supplementary materials

A full assortment of supplementary materials accompanies this text:

- 1 ***Solutions manual.*** A comprehensive manual containing answers to all review questions, exercises, problems, and Business Decision Problems contained in the text, along with a complete solution to the practice set.

In the development of problem material for this book, special attention has been given to the inclusion of problems of varying length and difficulty. By referring to the time estimates, difficulty ratings, and problem descriptions in the *Solutions Manual*, instructors can choose problems that best fit the level, scope, and emphasis of the course they are offering.

- 2 Two parallel sets of ***Achievement Tests*** and ***Comprehensive Examinations***. Each set consists of four Achievement Tests with each test covering three or four chapters; the Comprehensive Examination covers the entire text and may be used as a final examination.

- 3 ***An instructor's guide.*** This new separate manual includes the following three sections for each chapter of the textbook:

- a* A brief topical outline of the chapter listing in logical sequence the topics the authors like to discuss in class.

- b* An assignment guide correlating specific exercises and problems with various topics covered in the chapter.

- c* Comments and observations.

The "Comments and observations" sections indicate the authors' personal views as to relative importance of topics and identify topics with which some students have difficulty. Specific exercises and problems are recommended to demonstrate certain points. Many of these sections include "Asides," introducing real-world situations (not included in the text) that are useful in classroom discussions. Also included are solutions to the parallel sets of Achievement Tests and Comprehensive Examination.

- 4 ***An examination question manual.*** With an abundance of test questions and exercises arranged chapter by chapter for the entire text, this examination booklet will be a most useful source for instructors who prefer to assemble their own examinations. The questions in this book are printed in an 8½ × 11 format and can be torn out and copied to prepare individual examinations. All the questions and exercises in this manual are available on the EXAM-INNER system, a computerized test-generation system. Complete instructions for implementing the system are contained in the examination question manual.

- 5 ***A self-study guide.*** Written by the authors, the *Study Guide* enables students to measure their progress by immediate feedback. This self-study guide includes an outline of the most important points in each chapter, an abun-

dance of objective questions, and several short exercises for each chapter. In the back of the self-study guide are answers to questions and solutions to exercises to help students evaluate their understanding of the subject. The self-study guide will also be useful in classroom discussions and for review by students before examinations.

- 6 **Working papers.** A soft-cover book of *partially filled-in working papers* for the problem material is published separately from the text. On these work sheets, the problem headings and some preliminary data have been entered to save students much of the mechanical pencil-pushing inherent in problem assignments.
- 7 **Practice set.** The practice set available with the preceding edition has been completely revised. Designed for use after completing Chapter 6 of the text, the practice set is now bound in two separate books, making it easier for students to journalize transactions, post entries, and prepare financial statements.
- 8 **Checklist of key figures for problems.** This list appears on the front and back inside covers of this book. The purpose of the checklist is to aid students in verifying their problem solutions and in discovering their own errors.
- 9 **Transparencies of problem solutions.** This is a visual aid prepared by the publisher for the instructor who wishes to display in a classroom the complete solutions to any or all problems.
- 10 **Visual classroom displays.** Sixteen special transparencies have been produced for use in the classroom to illustrate such concepts as closing entries, the preparation of a work sheet, and the use of controlling accounts and subsidiary ledgers.

Contributions by others

We want to express our sincere thanks to the many users of preceding editions who offered helpful suggestions for this edition. Especially helpful was the advice received from Professor Sarah L. Adams, California State University, Chico; Professor Harold L. Cannon, State University of New York at Albany; Professor Joseph M. Conder, Indiana University Southeast; Professor Richard E. Czarnecki, The University of Michigan-Dearborn; Professor Howard Felt, Temple University; Professor Tom Hallinan, Portland Community College; Professor Orville R. Keister, The University of Akron; Professor Hans E. Klein, University of Massachusetts-Boston; Professor John A. Miller, Jr., St. Louis Community College at Florissant Valley; Professor Phyllis L. Mirchin, Monclair State College; Professor G. Kenneth Nelson, Penn State University; and Professor Jean Tillery, Emory University.

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Walter B. Meigs

Robert F. Meigs

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