

Intermediate Accounting



Stice & Stice

Intermediate Accounting^{19e}

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Australia • Brazil • Japan • Korea • Mexico • Singapore • Spain • United Kingdom • United States

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1 2 3 4 5 6 7 17 16 15 14 13

Currency + Context = Motivation

Motivation

From the smallest mom-and-pop retailer to the largest multinational corporation, businesses of all sizes are recognizing that accounting professionals are no longer simply “number crunchers” but, rather, essential partners in achieving the fundamental goals of their organization. When people understand accounting’s critical role in managing a business and making business decisions, they are **motivated** to learn accounting. That is why *Intermediate Accounting, 19e* provides a powerful connection between accounting and business today with:

- **Business strategy cases** at the start of each chapter that describe how a real-world firm such as MicroStrategy struggled with revenue recognition and the pressures on management to interpret revenue as positively as possible.
- **Coverage of high-interest and current topics** such as **earnings management**, **fair value**, and **International Financial Reporting Standards (IFRS)** as well as other issues that are driving accounting in today’s business environment.
- **FASB codification activities** that link FASB research with real business situations and help readers understand how to research and use authoritative guidance as well as why that guidance is important.
- **Real-world end-of-chapter case activities** that use the financial results of companies such as The Walt Disney Company, The Boston Celtics, Hewlett-Packard, and Dell to help readers connect accounting to business.

CURRENCY—Current and Relevant Coverage

One look at the business pages of any newspaper shows how illusory long-term success can be. Yesterday’s runaway successes can quickly find themselves derailed by the new realities of today’s business world. This is the first text to provide a real-world perspective that links accounting functions to the activities of business.



I F R S

International Financial Reporting Standards topics, indicated by this symbol throughout the text, help students understand how accounting practices differ from country to country and reflect the increasingly global nature of business.

The international environment of business is dramatically changing the landscape of accounting. The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) are working together to develop one set of accounting standards to be used by companies in countries around the world. No longer is the United States making the rules for the rest of the world to follow. Instead, the FASB and the IASB are working hand-in-hand as financial accounting standards converge at a pace that was not dreamed of even five years ago.

The international environment has greatly affected this textbook. Every chapter discusses relevant accounting standards and developments from both a U.S. and a global perspective. Each chapter begins with a discussion of the accounting standards and procedures used by companies complying with U.S. GAAP. Then those areas where U.S. GAAP and international accounting standards are significantly different are discussed so that the reader can understand how accounting standards around the world are similar and how they are different. A chapter on **Accounting in a Global Market** further emphasizes the role of International Financial Reporting Standards.

The objective of this approach is to develop in students the ability to see beyond the borders of the United States and understand that the global business environment is leading to global accounting standards. Users of this text will understand that they are not just learning U.S. GAAP. Instead, they are being prepared to be active participants in a global accounting environment with the ability to understand and apply international accounting standards as well as U.S. accounting standards.

Fair Value Accounting is another major topic affecting the accounting environment. The credit crisis of 2008 is blamed by some on the inappropriate use of fair value accounting. A module details the *why, when, where, and how* for using fair values in financial statements. Because this concept of fair value accounting is so important and affects so many of the principles and topics discussed later in the text, it has been placed near the front of the text following the discussion of the financial statements.

A Chapter on Earnings Management in Part 1 establishes a framework for the remainder of the course. Students come to understand the importance and ramifications of earnings management through current, real-world examples, extracts from SEC enforcement actions, business press analysis, and the extensive use of academic research findings.

FASB Codification feature presents a relevant issue and related question in order to assist students in understanding how to use the FASB's codification in research. This feature is found in each chapter and includes a description of the issue at hand, a specific question pertaining to that given issue, and suggestions for "Searching the Codification" in order to guide students in the right direction for research. Each feature includes an answer section at the end of the chapter, so that students can check their research and adjust their technique as needed. References throughout the textbook reflect the FASB ASC (Accounting Standards Codification).



FASB CODIFICATION

The Issue: You are the accountant for a company in the carpet cleaning business. Because of your company's innovative cleaning system (no harsh detergents, no damaging brushes, and extremely small carbon footprint), you have been very successful and have begun to drive your competitors out of business. In fact, just today your company's CEO has decided to start buying a number of your competitors. As you walked out the door at the end of the day, she said: "You had better learn how to account for a bargain purchase."

The Question: What is a bargain purchase, and why is a bargain purchase likely to arise in this situation?

Searching the Codification: Bargain purchases are covered in this chapter, but you would like to show your boss that you can find accounting standards for yourself in the authoritative literature. The best place to start is in Topic 805 (Business Combinations), which is in the "Broad Transactions" collection of topics.

The Answer: The authoritative accounting standards relative to bargain purchases are described on page 10-41.

Up-to-Date *Intermediate Accounting, 19e* has been **completely updated** to reflect the latest changes in accounting standards, practices, and techniques. The real company information has been revised to account for recent changes in financial statements and other company reports.

Exhibit 16-6 | ExxonMobil—Disclosure for Provision for Income Taxes

18. Income, Sales-Based and Other Taxes (Millions of dollars)	2011			2010			2009		
	U.S.	Non-U.S.	Total	U.S.	Non-U.S.	Total	U.S.	Non-U.S.	Total
Income taxes									
Federal and non-U.S.									
Current	\$ 1,547	\$28,849	\$ 30,396	\$1,224	\$21,093	\$ 22,317	\$ (838)	\$15,830	\$14,992
Deferred—net	1,577	(1,417)	160	49	(1,191)	(1,142)	650	(665)	(15)
U.S. tax on non-U.S. operations	15	—	15	46	—	46	32	—	32
Total federal and non-U.S.	3,139	27,432	30,571	1,319	19,902	21,221	(156)	15,165	15,009
State	480	—	480	340	—	340	110	—	110
Total income taxes	3,619	27,432	31,051	1,659	19,902	21,561	(46)	15,165	15,119
Sales-based taxes	5,652	27,851	33,503	6,182	22,365	28,547	6,271	19,665	25,936
All other taxes and duties									
Other taxes and duties	1,539	38,434	39,973	776	35,342	36,118	581	34,238	34,819
Included in production and manufacturing expenses	1,342	1,425	2,767	1,001	1,237	2,238	699	1,318	2,017
Included in SG&A expenses	181	623	804	201	570	771	197	538	735
Total other taxes and duties	3,062	40,482	43,544	1,978	37,149	39,127	1,477	36,094	37,571
Total	\$12,333	\$95,765	\$108,098	\$9,819	\$79,416	\$89,235	\$7,702	\$70,924	\$78,626

ExxonMobil, 2011, 10K Report

CONTEXT—Business Activities Emphasized in Organization

No other text works harder to demonstrate accounting's integral importance to an organization's decision-making capabilities. This book is organized as much as possible around the essential interrelationship between accounting procedures and the activities of business to provide students with the context behind the accounting that is discussed. The innovative structure is unsurpassed in preparing students to serve as trusted advisors on the front lines of business.

In an effort to streamline the sequence of chapters in the text, the table of contents accounts for a more traditional balance sheet order of topics while still maintaining the structure of covering topics as they relate to business activities. The investing chapters fall before the financing chapters, which results in a more familiar order of presentation for instructors and students.

Part 1—Foundations of Financial Accounting provides students with the fundamentals of financial accounting, including a full chapter on Earnings Management, and concludes with a module that covers the Time Value of Money as well as a module on Fair Value.

Part 2—Routine Activities of a Business gets down to business, integrating accounting into management by exploring operating and investing activities.

Part 3—Additional Activities of a Business examines financing activities, leases, income taxes, and employee compensation.

Part 4—Other Dimensions of Financial Reporting rounds out the comprehensive coverage with earnings per share; derivatives, contingencies, business segments, and interim reports; accounting changes; and financial statement analysis; as well as extended coverage of IFRS, which is found in the separate chapter, Accounting in a Global Market.

Why and How Framework follows each learning objective, as the authors provide additional reinforcement of the critical concepts by highlighting both the procedural aspects (the “how”) as well as the context (or “why”) for which they are applied. As they move through the chapter, students gain a greater understanding of both elements and can rationalize why businesses account for things the way they do. By exposing students to the “why” behind each concept, students are being trained to realize the business implications of various decisions made by companies and can take their careers head-on.

Supporting this framework are a number of critical-thinking elements that allow students to stretch their minds into the analysis of the relevant topics, a skill that will also be crucial as they move on in their studies and careers.

WHY *SAB 101* was released to curtail specific abuses in revenue recognition practices. The guiding principle behind *SAB 101* is that companies should not be granted the flexibility to decide to accelerate or delay the recognition of revenue. Instead, the economic characteristics of the transaction itself should determine when the revenue is to be recognized.

HOW In order to report revenue reliably, a company must have a system of internal controls in place to govern the timing of revenue recognition. In a multiple-element transaction, the revenue associated with any specific component, or unit of accounting, can be recognized only if that component can be sold separately. Reporting the entire value of a transaction as “revenue” is inappropriate for a company that acts only as a broker or agent.

SAB 101

2 Discuss the revenue recognition issues, and abuses, underlying the examples used in *SAB 101*.

SAB 101 is a very interesting document. It is in a question-and-answer format. Most of the questions follow the pattern: “May a company recognize revenue in the following situation?” The answers given in *SAB 101* are invariably “No.” *SAB 101* arose in response to specific abuses seen by the SEC staff. As illustrated with the MicroStrategy scenario at the beginning of the chapter, these abuses were often driven by the desire of high-flying companies to maintain their aura of invincibility by continuing to report astronomical revenue growth each quarter.

Because *SAB 101* was released to curtail specific abuses, it should not be seen as a comprehensive treatise on the entire area of revenue recognition. Remember that the vast majority of companies apply the revenue recognition criteria in a very straightforward way with no questions from their auditor, the SEC, or investors. But it is precisely in the financial reporting of high-growth, start-up companies doing innovative transactions where reliable and transparent accounting practices add greatest value. Thus, the revenue recognition issues covered in *SAB 101* may not be comprehensive, but they are extremely important.

The release by the SEC of *SAB 101* caused quite a stir in the accounting community. *SAB 101* deals with a fundamental accounting topic (revenue recognition), is blunt in its provisions, and was released without the years of discussion and lobbying typically involved

Statement of Cash Flows “Revisited” in Chapter 21 provides coverage of the statement of cash flows in the second semester of the course. The book continues to provide a full chapter early in the text (Chapter 5) addressing the statement of cash flows and integrates this financial statement throughout the text, which results in the most comprehensive treatment of this important subject available.

Opening Scenario Questions are critical-thinking questions that follow the updated real company chapter openers. Solutions are provided at the end of each chapter so students can check their answers as they think about how they would approach accounting-related issues that businesses face.

1. Why do you think the price-to-sales ratio (as opposed to the price-earnings ratio) is often used in valuing the stocks of start-up technology companies, especially those related to the Internet?
2. On Monday, March 20, 2000, MicroStrategy issued a press release stating that revenues for the year 1999 were about \$155 million, not \$205 million as previously announced. This represented a drop of 24% in reported revenue. Why did a drop of just 24% in reported revenue result in a stock price drop of 62%? In other words, why wasn't the drop in stock price also 24%?
3. In early March 2000, MicroStrategy's board of directors received word that the company's auditor was requesting a revenue restatement. The board was reluctant to go forward with the restatement because of fears (justified, as it turns out) that the restatement would hurt the company's stock price. List and explain two or three arguments that you, as a member of the board, could have made in support of the restatement.



Answers to these questions can be found on pages 8-34–8-35.

Stop & Think

It would seem that the physical capital maintenance concept would provide the best theoretical measure of “well-offness.” However, use of the physical capital maintenance concept of measuring income involves many practical difficulties. Identify ONE of those practical difficulties from the list below.

- a) Difficulty in estimating depreciation lives
- b) Difficulty in implementing internal control procedures
- c) Difficulty in providing cash flow information
- d) Difficulty in obtaining fair market values of assets and liabilities

Stop & Think multiple-choice questions have been written by the authors to accompany the Stop & Think boxed features. These critical-thinking boxes, found in every chapter, allow students to test their knowledge and then consult the answers found at the end of the chapter.

FYI

Before 2002, all gains and losses resulting from the early extinguishment of debt were reported as extraordinary. This classification was ended with the release of pre-Codification *SFAS No. 145* (now in FASB ASC paragraph 470-50-45-1); these gains and losses are now considered ordinary, subject to the normal criteria for extraordinary items.

FYI margin boxes often provide additional context to an important topic by emphasizing additional points of interest.

Caution

The most common error when computing bad debt expense is to confuse the two methods—percentage of sales and percentage of receivables. Remember that when you are using the percentage-of-sales method, bad debt expense is computed and the balance in the allowance account is then determined. When you are using the percentage-of-receivables method, the balance in the allowance account is computed, and then the amount of bad debt expense for the period is determined.

Caution provide students with important points to consider when thinking about more complex concepts and topics.

REVERSE SOLVABLE

“Reverse Solvable” Problems at the end of chapters, identified by an icon, ask students to demonstrate mastery of relationships and accounting concepts by working with incomplete information and completing the missing information before completing the assignment.

Chapter Updates and Enhancements

Chapter 1

- Update on the standard-setting process
- New discussion of the revised Conceptual Framework
- Further explanation of the convergence of U.S. GAAP and IASB standards
- Extended coverage of U.S. GAAP and IFRS similarities and differences

Chapter 2

- New feature “Using the FASB’s Codification”

Chapter 3

- Updated and revised opening case on Coca-Cola
- New feature “Using the FASB’s Codification”
- Analysis of the proposed new balance sheet format

Chapter 4

- Updated exhibits
- New feature “Using the FASB’s Codification”
- Analysis of the proposed new income statement format

Chapter 5

- New feature “Using the FASB’s Codification”
- Revised FASB-IFRS-Codification Summary

Chapter 6

- Updated exhibits
- Revised to reflect economic and housing crises

Time Value of Money Module

- Revised end-of-chapter material to reflect recent updates

Fair Value Module

- New FASB ASC references

Chapter 7

- Updated chapter-opening vignette to reflect global economic crisis
- New FASB ASC references
- New feature “Using the FASB’s Codification”
- Updated exhibits

Chapter 8

- Revised Learning Objectives
- Updated and expanded discussion of the asset-and-liability approach to revenue recognition that is currently being developed as a joint effort of the FASB and the IASB
- New feature “Using the FASB’s Codification”
- Updated data and exhibits

Chapter 9

- New feature “Using the FASB’s Codification”
- Updated data and exhibits

Chapter 10

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Updated data and exhibits

Chapter 11

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- New discussion of a qualitative assessment as part of goodwill impairment
- Updated data and exhibits

Chapter 12

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Updated data and exhibits
- Updated discussion on the use of the fair value option for the reporting of financial assets and liabilities

Chapter 13

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Updated discussion of the reporting of comprehensive income
- Updated data and exhibits

Chapter 14

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Updated data and exhibits
- Updated discussion on the classification of investment securities according to IFRS and U.S. GAAP
- Updated discussion on the use of the fair value option with equity method securities

Chapter 15

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Updated discussion of the possibility that a future standard may require capital lease accounting for most leases
- Updated data and exhibits

Chapter 16

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Expanded discussion of accounting for uncertain tax provisions

Chapter 17

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- New coverage of pension accounting under IFRS
- Updated information regarding GM and the effects of the company’s bankruptcy on its pension and other post-retirement plans

Chapter 18

- New chapter-opening vignette focusing on China’s position in the global economic world
- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”

Chapter 19

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- New discussion of an abandoned FASB proposal to increase loss contingency disclosures

Chapter 20

- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”
- Updated exhibits and data

Chapter 21

- New discussion of the FASB–IASB project on financial statement presentation
- Updated exhibits and data
- Updated references to FASB ASC throughout

Chapter 22

- Revised information on the IASB
- Updated key differences between U.S. GAAP and IFRS
- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”

Chapter 23

- Updated illustration of the use of accounting data in equity valuation
- Updated references to FASB ASC throughout
- New feature “Using the FASB’s Codification”

Reinforce Student Understanding

Unmatched End-of-Chapter Material

Widely regarded as providing the most varied and expansive set of problem assignments available, *Intermediate Accounting, 19e* continues to raise the bar to new heights. Only

Intermediate Accounting features such a diverse set of traditional exercises, problems, and cases:

- 15–25 Questions per chapter to help assimilate chapter content
- More than 400 Practice Exercises written by the authors
- Discussion Cases for homework or class discussion
- Exercises to reinforce key concepts or applications
- Problems that integrate several concepts or techniques
- Sample CPA Exam Questions written to provide students with similar problems commonly found on the CPA exam

REVERSE SOLVABLE

“Reverse Solvable” Problems at the end of chapters, identified by an icon, ask students to demonstrate mastery of relationships and accounting concepts by working with incomplete information to determine the data that is missing from the exercise, before completing the assignment.

Case Materials have been designed to help accelerate the development of essential skills in critical thinking, communication, research, and teamwork. Retention and application of key concepts build as future accountants and business professionals take advantage of a wide range of tools found in this innovative section. These cases satisfy the skills-based curriculum endorsed by the AICPA’s Core Competency Framework and the recommendations of the Accounting Education Change Commission (AECC).

Deciphering Actual Financial Statements Cases enable students to analyze financial data from recent annual reports from companies such as The Walt Disney Company, Coca-Cola, and the Boston Celtics.

Ethical Dilemma Assignments help develop the critical-thinking skills students will need as they wrestle with the business world’s many “gray” issues.

Case 7-74

Ethical Dilemma

You recently graduated from college with your accounting degree. Your father’s best friend is the director of the accounting department of a small manufacturing firm in the area, and you accepted a position on his staff. After a month on the job, you have noticed several deficiencies in the cash controls for the company. For example, the individual making the daily deposits at the bank is also in charge of updating accounts receivable. You also notice that the petty cash fund is under general control of everyone in the office (that means that no one person has ultimate responsibility) and that vouchers are seldom completed when cash is removed from the fund. You bring your concerns to the attention of your boss, your father’s friend, and he comments:

“I appreciate your concerns. I knew when we hired you that you were sharp, but you need to understand that not everything is done by the book here. We trust our employees. If we were to enforce rigid controls on cash, it would create a nontrusting work environment. We don’t want that. Sure, a little money may turn up missing now and then, but it is a small price to pay. Now, don’t you worry about it anymore.”

What do you do now? Would you be comfortable working in an environment where there is a lack of control on cash? If a significant sum of money were to turn up missing and the control system was unable to determine who was responsible, what would that do to the trusting work environment? And remember, big sums of money never turned up missing until you came to work at the company.

The Cumulative Spreadsheet Analysis Case builds upon the lessons of each chapter to give students the opportunity to demonstrate and reinforce their understanding. Found at the end of Chapters 2–5, 7–20, and 23, each exercise requires students to create a spreadsheet that allows for numerous variables to be modified and their effects to be monitored. By the end of the course, students have constructed a spreadsheet that enables them to forecast operating cash flows for five years in the future, adjust forecasts for the most reasonable operating parameters, and analyze the impact of a variety of accounting assumptions based on the reported numbers.

Case 2-53**Cumulative Spreadsheet Analysis**

Beginning with Chapter 2, each chapter in this text will include a spreadsheet assignment based on the financial information of a fictitious company named Skywalker Enterprises. The assignments start out simple—in this chapter you are not asked to do much more than set up financial statement formats and input some numbers. In succeeding chapters, the spreadsheets will get more complex so that by the end of the course you will have constructed a spreadsheet that allows you to forecast operating cash flows for five years in the future, adjust your forecast depending on the operating parameters that you think are most reasonable, and analyze the impact of a variety of accounting assumptions on the reported numbers.

So, let's get started with the first spreadsheet assignment.

Bonus Content

Web-Based Chapter Enhancements

In response to instructor requests, subject-enhancing material from previous editions of the text is available on the companion Web site. The result is a streamlined, easier-to-use text that provides ample supplement material for important topics.

CHAPTER	WEB MATERIAL
2	Illustration of Special Journals and Subsidiary Ledgers
5	Statement of Cash Flows—Indirect Method
7	Petty Cash Fund
8	Deposit Method: Franchising Industry
10	Complexities in Accounting for Capitalized Interest
13	Quasi-Reorganizations Complexities in Accounting for Stock-Based Compensation
14	Changes in Classification Involving the Equity Method
15	Real Estate Leases
16	Intraperiod Tax Allocation
17	Details of Accounting for Postretirement Benefits Other Than Pensions Detailed Pension Present Value Calculations
22	Foreign Currency
23	Impact of Changing Prices on Financial Statements

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Solutions Manual This manual is prepared by James D. Stice and Earl K. Stice, Brigham Young University, and is available online. It contains independently verified answers to all end-of-chapter questions, cases, exercises, and problems, written by the authors.

Test Bank The test bank is available online in both Word files and computerized Exam-View versions. Test items include multiple-choice questions and short examination problems for each chapter, along with solutions. Analysis problems are included to coincide with the emphasis on decision making in the text.

Instructor's PowerPoint® Slides Hundreds of slides in PowerPoint format can be used in onscreen lecture presentations or printed out and used as traditional overheads. Additionally, they can be printed and distributed to students, allowing students to concentrate on the professor instead of rushing to copy down information. These slides are available electronically on the companion Web site.

For Students

Excel Enhanced Spreadsheet Templates Excel templates with validations are provided on the Web site for solving selected end-of-chapter exercises and problems.

Robust Product Support Web Site A robust Web site provides a wealth of resources for you and your students in *Intermediate Accounting* at no additional cost! With a multitude of chapter-enhancing features and study aids, these resources will allow students to excel in class and save you time in planning.

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