

## Chapter 2—A Review of the Accounting Cycle

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### MULTIPLE CHOICE

1. In an accrual accounting system,
  - a. all accounts have normal debit balances.
  - b. a debit entry is recorded on the left-hand side of an account.
  - c. liabilities, owner's capital, and dividends all have normal credit balances.
  - d. revenues are recorded only when cash is received.

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

2. A common business transaction that would *not* affect the amount of owners' equity is
  - a. signing a note payable to purchase equipment.
  - b. payment of property taxes.
  - c. billing of customers for services rendered.
  - d. payment of dividends.

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

3. Failure to record the expired amount of prepaid rent expense would *not*
  - a. understate expense.
  - b. overstate net income.
  - c. overstate owners' equity.
  - d. understate liabilities.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

4. On June 30, a company paid \$3,600 for insurance premiums for the current year and debited the amount to Prepaid Insurance. At December 31, the bookkeeper forgot to record the amount expired. The omission has the following effect on the financial statements prepared December 31:
  - a. overstates owners' equity.
  - b. overstates assets.
  - c. understates net income.
  - d. overstates both owners' equity and assets.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

5. A chart of accounts is a
  - a. subsidiary ledger.
  - b. listing of all account titles.
  - c. general ledger.
  - d. general journal.

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

6. Which of the following criteria must be met before an event should be recorded for accounting purposes?
  - a. The event must be an arm's-length transaction.

- b. The event must be repeatable in a future period.
- c. The event must be measurable in financial terms.
- d. The event must be disclosed in the reported footnotes.

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
 TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

7. Adjusting entries normally involve
- a. real accounts only.
  - b. nominal accounts only.
  - c. real and nominal accounts.
  - d. liability accounts only.

ANS: C                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

8. Which of the following is an item that is reportable in the financial records of an enterprise?
- a. The value of goodwill earned through business operations
  - b. The value of human resources
  - c. Changes in personnel
  - d. Changes in inventory costing methods

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 1  
 TOP: AICPA FN-Reporting                      MSC: AACSB Reflective Thinking

9. The balance in a deferred revenue account represents an amount that is

	<u>Earned</u>	<u>Collected</u>
a.	Yes	Yes
b.	Yes	No
c.	No	Yes
d.	No	No

ANS: C                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

10. The debit and credit analysis of a transaction normally takes place when the
- a. entry is posted to a subsidiary ledger.
  - b. entry is recorded in a journal.
  - c. trial balance is prepared.
  - d. financial statements are prepared.

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
 TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

11. A trial balance is useful because it indicates that
- a. owners' equity is correct.
  - b. net income is correct.
  - c. all entries were made correctly.
  - d. total debits equal total credits.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

12. Which of the following would typically be considered a source document?
- a. Chart of accounts

- b. General ledger
- c. General journal
- d. Invoice received from seller

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
 TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

13. Which of the following is *not* among the first five steps in the accounting cycle?
- a. Record transactions in journals.
  - b. Record closing entries.
  - c. Adjust the general ledger accounts.
  - d. Post entries to general ledger accounts.

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 1  
 TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

14. A routine collection on a customer's account was recorded and posted as a debit to Cash and a credit to Sales Revenue. The journal entry to correct this error would be
- a. a debit to Sales Revenue and a credit to Accounts Receivable.
  - b. a debit to Sales Revenue and a credit to Unearned Revenue.
  - c. a debit to Cash and a credit to Accounts Receivable.
  - d. a debit to Accounts Receivable and a credit to Sales Revenue.

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

15. An accrued expense can be described as an amount
- a. paid and matched with earnings for the current period.
  - b. paid and not matched with earnings for the current period.
  - c. not paid and not matched with earnings for the current period.
  - d. not paid and matched with earnings for the current period.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

16. Which of the following errors will be detected when a trial balance is properly prepared?
- a. An amount that was entered in the wrong account
  - b. A transaction that was entered twice
  - c. A transaction that had been omitted
  - d. None of these

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

17. The premium on a two-year insurance policy expiring on June 30, 2015, was paid in total on July 1, 2013. The original payment was debited to the insurance expense account. The appropriate journal entry has been recorded on December 31, 2013. The balance in the prepaid asset account on December 31, 2013, should be
- a. the same as the original payment.
  - b. higher than if the original payment had been initially debited to an asset account.
  - c. lower than if the original payment had been initially debited to an asset account.
  - d. the same as it would have been if the original payment had been initially debited to an asset account.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

18. If an inventory account is understated at year end, the effect will be to overstate the
- net purchases.
  - gross margin.
  - cost of goods available for sale.
  - cost of goods sold.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

19. An adjusting entry will *not* take the format of which one of the following entries?
- A debit to an expense account and a credit to an asset account
  - A debit to an expense account and a credit to a revenue account
  - A debit to an asset account and a credit to a revenue account
  - A debit to a liability account and a credit to a revenue account

ANS: B                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

20. The last step in the accounting cycle is to
- prepare a post-closing trial balance.
  - journalize and post closing entries.
  - prepare financial statements.
  - journalize and post adjusting entries.

ANS: A                      PTS: 1                      DIF: Easy                      OBJ: LO 1  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

21. Which of the following is *not* presented in an income statement?
- Revenues
  - Expenses
  - Net income
  - Dividends

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Reporting                      MSC: AACSB Reflective Thinking

22. On March 1, 2012, Forest Co. borrowed cash and signed a 36-month, interest-bearing note on which both the principal and interest are payable on February 28, 2015. At December 31, 2014, the liability for accrued interest should be
- 10 months' interest.
  - 22 months' interest.
  - 34 months' interest.
  - 36 months' interest.

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

23. An example of an adjusting entry involving a deferred revenue is

- |                               |     |     |
|-------------------------------|-----|-----|
| Cash .....                    | xxx |     |
| Unearned Rental Revenue ..... |     | xxx |
- |                      |     |     |
|----------------------|-----|-----|
| Rental Revenue ..... | xxx |     |
| Cash .....           |     | xxx |
- |                               |     |     |
|-------------------------------|-----|-----|
| Unearned Rental Revenue ..... | xxx |     |
| Rental Revenue .....          |     | xxx |
- |                           |     |  |
|---------------------------|-----|--|
| Accounts Receivable ..... | xxx |  |
|---------------------------|-----|--|

Sales .....

xxx

ANS: C                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

24. The allowance for doubtful accounts is an example of a(n)
- expense account.
  - contra account.
  - adjunct account.
  - control account.

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

25. Iowa Cattle Company uses a periodic inventory system. Iowa purchased cattle from Big D Ranch at a cost of \$27,000 on credit. The entry to record the receipt of the cattle would be

a.	Purchases .....	27,000	
	Accounts Payable .....		27,000
b.	Inventory .....	27,000	
	Accounts Payable .....		27,000
c.	Purchases .....	27,000	
	Cash .....		27,000
d.	Inventory .....	27,000	
	Cash .....		27,000

ANS: A                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

26. Which of the following is presented in a balance sheet?
- Prepaid expenses
  - Revenues
  - Net income
  - Gains

ANS: A                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Reporting                      MSC: AACSB Reflective Thinking

27. If an expense has been incurred but not yet recorded, then the end-of-period adjusting entry would involve
- a liability account and an asset account.
  - a liability account and a revenue account.
  - a liability and an expense account.
  - a receivable account and a revenue account.

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

28. Failure to record depreciation expense at the end of an accounting period results in
- understated income.
  - understated assets.
  - overstated expenses.
  - overstated assets.

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

29. Iowa Cattle Company uses a perpetual inventory system. Iowa purchased cattle from Big D Ranch at a cost of \$19,500, payable at time of delivery. The entry to record the delivery would be

a.	Purchases .....	19,500	
	Accounts Payable .....		19,500
b.	Inventory .....	19,500	
	Accounts Payable .....		19,500
c.	Purchases .....	19,500	
	Cash .....		19,500
d.	Inventory .....	19,500	
	Cash .....		19,500

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

30. Beginning and ending Accounts Receivable balances were \$28,000 and \$24,000, respectively. If collections from clients during the period were \$80,000, then total services rendered on account were apparently
- \$76,000.
  - \$84,000.
  - \$104,000.
  - \$108,000.

ANS: A                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

31. For a given year, beginning and ending total liabilities were \$8,400 and \$10,000, respectively. At year-end, owners' equity was \$26,000 and total assets were \$2,000 larger than at the beginning of the year. If new capital stock issued exceeded dividends by \$2,400, net income (loss) for the year was apparently
- (\$2,800).
  - (\$2,000).
  - \$400.
  - \$2,800.

ANS: B                      PTS: 1                      DIF: Challenging                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

32. The Supplies on Hand account balance at the beginning of the period was \$6,600. Supplies totaling \$12,825 were purchased during the period and debited to Supplies on Hand. A physical count shows \$3,825 of Supplies on Hand at the end of the period. The proper journal entry at the end of the period
- debits Supplies on Hand and credits Supplies Expense for \$9,000.
  - debits Supplies Expense and credits Supplies on Hand for \$12,825.
  - debits Supplies on Hand and credits Supplies Expense for \$15,600.
  - debits Supplies Expense and credits Supplies on Hand for \$15,600.

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

33. Arid Company paid \$1,704 on June 1, 2013, for a two-year insurance policy and recorded the entire amount as Insurance Expense. The December 31, 2013, adjusting entry is
- debit Prepaid Insurance and credit Insurance Expense, \$497.
  - debit Insurance Expense and credit Prepaid Insurance, \$497.
  - debit Insurance Expense and credit Prepaid Insurance, \$1,207.
  - debit Prepaid Insurance and credit Insurance Expense, \$1,207.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

34. Moon Company purchased equipment on November 1, 2013, by giving its supplier a 12-month, 9 percent note with a face value of \$48,000. The December 31, 2013, adjusting entry is
- debit Interest Expense and credit Cash, \$720.
  - debit Interest Expense and credit Interest Payable, \$720.
  - debit Interest Expense and credit Interest Payable, \$1,080.
  - debit Interest Expense and credit Interest Payable, \$4,320.

ANS: B

PTS: 1

DIF: Medium

OBJ: LO 3

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

35. In November and December 2013, Bee Company, a newly organized newspaper publisher, received \$72,000 for 1,000 three-year subscriptions at \$24 per year, starting with the January 2, 2014, issue of the newspaper. How much should Bee report in its 2013 income statement for subscription revenue?
- \$0
  - \$12,000
  - \$24,000
  - \$72,000

ANS: A

PTS: 1

DIF: Easy

OBJ: LO 3

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

36. On December 31 of the current year, Holmgren Company's bookkeeper made an entry debiting Supplies Expense and crediting Supplies on Hand for \$12,600. The Supplies on Hand account had a \$15,300 debit balance on January 1. The December 31 balance sheet showed Supplies on Hand of \$11,400. Only one purchase of supplies was made during the month, on account. The entry for that purchase was
- debit Supplies on Hand, \$8,700 and credit Cash, \$8,700.
  - debit Supplies Expense, \$8,700 and credit Accounts Payable, \$8,700.
  - debit Supplies on Hand, \$8,700 and credit Accounts Payable, \$8,700.
  - debit Supplies on Hand, \$16,500 and credit Accounts Payable, \$16,500.

ANS: C

PTS: 1

DIF: Medium

OBJ: LO 2

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

37. The following errors were made in preparing a trial balance: the \$1,350 balance of Inventory was omitted; the \$450 balance of Prepaid Insurance was listed as a credit; and the \$300 balance of Salaries Expense was listed as Utilities Expense. The debit and credit totals of the trial balance would differ by
- \$1,350.
  - \$1,800.
  - \$2,100.
  - \$2,250.

ANS: D

PTS: 1

DIF: Challenging

OBJ: LO 3

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

38. Crescent Corporation's interest revenue for 2013 was \$13,100. Accrued interest receivable on December 31, 2013, was \$2,275 and \$1,875 on December 31, 2012. The cash received for interest during 2013 was
- \$1,350.
  - \$10,825.
  - \$12,700.
  - \$13,100.

ANS: C                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium              OBJ: LO 2  
MSC: AACSB Analytic

39. Sky Corporation's salaries expense for 2012 was \$136,000. Accrued salaries payable on December 31, 2013, was \$17,800 and \$8,400 on December 31, 2012. The cash paid for salaries during 2013 was
- \$126,600.
  - \$127,600.
  - \$145,400.
  - \$153,800.

ANS: A                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Easy                      OBJ: LO 2  
MSC: AACSB Analytic

40. Winston Company sells magazine subscriptions for one- to three-year subscription periods. Cash receipts from subscribers are credited to Magazine Subscriptions Collected in Advance, and this account had a balance of \$9,600,000 at December 31, 2013, before year-end adjustment. Outstanding subscriptions at December 31, 2013, expire as follows:

During 2014 .....	\$2,600,000
During 2015 .....	3,200,000
During 2016 .....	1,800,000

In its December 31, 2013, balance sheet, what amount should Winston report as the balance for magazine subscriptions collected in advance?

- \$2,000,000
- \$3,800,000
- \$7,600,000
- \$9,600,000

ANS: C                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Challenging              OBJ: LO 3  
MSC: AACSB Analytic

41. L. Lane received \$12,000 from a tenant on December 1 for four months' rent of an office. This rent was for December, January, February, and March. If Lane debited Cash and credited Unearned Rental Income for \$12,000 on December 1, what necessary adjustment would be made on December 31?

a. Unearned Rental Income .....	3,000	
Rental Income .....		3,000
b. Rental Income .....	3,000	
Unearned Rental Income .....		3,000
c. Unearned Rental Income .....	9,000	
Rental Income .....		9,000
d. Rental Income .....	9,000	
Unearned Rental Income .....		9,000

ANS: A                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium                      OBJ: LO 3  
MSC: AACSB Analytic

42. Ingle Company paid \$12,960 for a four-year insurance policy on September 1 and recorded the \$12,960 as a debit to Prepaid Insurance and a credit to Cash. What adjusting entry should Ingle make on December 31, the end of the accounting period?

a. Prepaid Insurance .....	810	
Insurance Expense .....		810
b. Insurance Expense .....	1,080	
Prepaid Insurance .....		1,080
c. Insurance Expense .....	3,240	
Prepaid Insurance .....		3,240



d. Prepaid Insurance .....	11,880	
Insurance Expense .....		11,880

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

43. Bannister Inc.'s fiscal year ended on November 30, 2013. The accounts had not been adjusted for the fiscal year ending November 30, 2013. The balance in the prepaid insurance account as of November 30, 2013, was \$35,200 (before adjustment at Nov. 30, 2013) and consisted of the following policies:

Policy <u>Number</u>	Date of <u>Purchase</u>	Date of <u>Expiration</u>	Balance in <u>Account</u>
279248	7/1/2013	6/30/2014	\$14,400
694421	12/1/2011	11/30/2013	9,600
800616	4/1/2012	3/31/2014	<u>11,200</u>
			<u>\$35,200</u>

The adjusting entry required on November 30, 2013, would be

a. Insurance Expense .....	24,000	
Prepaid Insurance .....		24,000
b. Insurance Expense .....	9,600	
Prepaid Insurance .....		9,600
c. Insurance Expense .....	11,200	
Prepaid Insurance .....		11,200
d. Insurance Expense .....	16,400	
Prepaid Insurance .....		16,400

ANS: A

#279248:

\$14,400 balance represents twelve months of coverage left since no adjustment has been made at Nov. 30, 2013.  $\$14,400/12 = \$1,200/\text{month}$ . Policy was purchased on 7/1/13, so five months have expired, or  $\$1,200 \times 5 \text{ mos.} = \text{\$6,000 that should be expensed for year ending 11/30/2013.}$

#694421:

**The entire balance of \$9,600 should be expensed for the year ending 11/30/2013** since the policy expired on Nov. 30, 2013, and the \$9,600 balance represents the final year of prepaid insurance remaining to be expensed, assuming again that no adjustments have been made at Nov. 30, 2013, for the year then ended.

#800616:

The balance of \$11,200 represents 16 months of coverage left at the **beginning** of fiscal year 2013.  $\$11,200/16 = \$700$ . 12 months of prepaid insurance should be expensed for the fiscal year ending 11/30/2013.  $12 \text{ months} \times \$700 = \text{\$8,400 to be expensed for the year ending 11/30/2013.}$

Total amount to be expensed at 11/30/2013:

#279248	\$ 6,000
#694421	\$ 9,600
#800616	<u>\$ 8,400</u>
Total	<u>\$24,000</u>

PTS: 1                      DIF: Challenging                      OBJ: LO 3                      TOP: AICPA FN-Measurement  
MSC: AACSB Analytic

44. Kite Company paid \$24,900 in insurance premiums during 2013. Kite showed \$3,600 in prepaid insurance on its December 31, 2013, balance sheet and \$4,500 on December 31, 2012. The insurance expense on the income statement for 2013 was
- \$16,800.
  - \$24,000.
  - \$25,800.
  - \$33,000.

ANS: C                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

45. Thompson Company sublet a portion of its office space for ten years at an annual rental of \$36,000, beginning on May 1. The tenant is required to pay one year's rent in advance, which Thompson recorded as a credit to Rental Income. Thompson reports on a calendar-year basis. The adjustment on December 31 of the first year should be

a.	Rental Income .....	12,000	
	Unearned Rental Income .....		12,000
b.	Rental Income .....	24,000	
	Unearned Rental Income .....		24,000
c.	Unearned Rental Income .....	12,000	
	Rental Income .....		12,000
d.	Unearned Rental Income .....	24,000	
	Rental Income .....		24,000

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

46. Sky Company collected \$12,350 in interest during 2013. Sky showed \$1,850 in interest receivable on its December 31, 2013, balance sheet and \$5,300 on December 31, 2012. The interest revenue on the income statement for 2013 was
- \$3,450.
  - \$8,900.
  - \$12,350.
  - \$14,200.

ANS: B                      PTS: 1                      DIF: Easy                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

47. On September 1, 2012, Star Corp. issued a note payable to Federal Bank in the amount of \$450,000. The note had an interest rate of 12 percent and called for three equal annual principal payments of \$150,000. The first payment for interest and principal was made on September 1, 2013. At December 31, 2013, Star should record accrued interest payable of

- \$11,000.
- \$12,000.
- \$16,500.
- \$18,000.

ANS: B                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

48. The following balances have been excerpted from Edwards' balance sheets:

	<u>December 31, 2013</u>	<u>December 31, 2012</u>
Prepaid Insurance	\$ 6,000	\$ 7,500
Interest Receivable	3,700	14,500
Salaries Payable	61,500	53,000

Edwards Company paid or collected during 2013 the following items:

Insurance premiums paid	\$ 41,500
Interest collected	123,500
Salaries paid	481,000

The insurance expense on the income statement for 2013 was

- a. \$28,000.
- b. \$40,000.
- c. \$43,000.
- d. \$55,000.

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

49. The work sheet of PSI Company shows Income Tax Expense of \$9,000 and Income Tax Payable of \$9,000 in the Adjustments columns. What will be the ultimate disposition of these items on the work sheet?
- a. Income Tax Expense will appear as a debit of \$9,000 and Income Tax Payable as credit in the Balance Sheet columns.
  - b. Income Tax Expense will appear as a debit of \$9,000 and Income Tax Payable as credit in the Income Statement columns.
  - c. Income Tax Expense will appear as a debit of \$9,000 in the Balance Sheet columns and Income Tax Payable as credit in the Income Statement columns.
  - d. Income Tax Expense will appear as a debit of \$9,000 in the Income Statement columns and Income Tax Payable as credit in the Balance Sheet columns.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

50. The following balances have been excerpted from Edwards' balance sheets:

	<u>December 31, 2013</u>	<u>December 31, 2012</u>
Prepaid Insurance .....	\$ 6,000	\$ 7,500
Interest Receivable .....	3,700	14,500
Salaries Payable .....	61,500	53,000

Edwards Company paid or collected during 2013 the following items:

Insurance premiums paid .....	\$ 41,500
Interest collected .....	123,500
Salaries paid .....	481,000

The interest revenue on the income statement for 2013 was

- a. \$90,500.
- b. \$112,700.
- c. \$117,500.
- d. \$156,500.

ANS: B                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

51. Chips-n-Bits Company sells service contracts for personal computers. The service contracts are for a one-year, two-year, or three-year period. All sales are for cash and all receipts are credited to Unearned Service Contract Revenues. This account had a balance of \$144,000 at December 31, 2012, before year-end adjustment. Service contract costs are charged as incurred to the Service Contract Expense account, which had a balance of \$36,000 at December 31, 2012. Service contracts still outstanding at December 31, 2012, expire as follows:

During 2013 .....	\$30,000
During 2014 .....	45,000
During 2015 .....	20,000

What amount should be reported as unearned service contract revenues in Chips-n-Bits December 31, 2012, balance sheet?

- a. \$49,000
- b. \$59,000
- c. \$95,000
- d. \$108,000

ANS: C                      PTS: 1                      DIF: Challenging    OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

52. Teller Inc. reported an allowance for doubtful accounts of \$30,000 (credit) at December 31, 2013, before performing an aging of accounts receivable. As a result of the aging, Teller Inc. determined that an estimated \$52,000 of the December 31, 2013, accounts receivable would prove uncollectible. The adjusting entry required at December 31, 2013, would be

a.	Doubtful Accounts Expense .....	22,000	
	Allowance for Doubtful Accounts ...		22,000
b.	Allowance for Doubtful Accounts .....	22,000	
	Accounts Receivable .....		22,000
c.	Doubtful Accounts Expense .....	52,000	
	Allowance for Doubtful Accounts ...		52,000
d.	Allowance for Doubtful Accounts .....	52,000	
	Doubtful Accounts Expense .....		52,000

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

53. Comet Corporation's liability account balances at June 30, 2013, included a 10 percent note payable. The note is dated October 1, 2011, and carried an original principal amount of \$600,000. The note is payable in three equal annual payments of \$200,000 plus interest. The first interest and principal payment was made on October 1, 2012. In Comet's June 30, 2013, balance sheet, what amount should be reported as Interest Payable for this note?

- a. \$10,000
- b. \$15,000
- c. \$30,000
- d. \$45,000

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

54. Scott Co. reported an allowance for doubtful accounts of \$28,000 (credit) at December 31, 2013, before performing an aging of accounts receivable. As a result of the aging, Scott determined that an estimated \$27,000 of the December 31, 2013, accounts receivable would prove uncollectible. The adjusting entry required at December 31, 2013, would be

a.	Doubtful Accounts Expense .....	27,000	
	Allowance for Doubtful Accounts ...		27,000

b.	Doubtful Accounts Expense .....	27,000	
	Accounts Receivable .....		27,000
c.	Allowance for Doubtful Accounts .....	1,000	
	Doubtful Accounts Expense .....		1,000
d.	Doubtful Accounts Expense .....	1,000	
	Allowance for Doubtful Accounts ...		1,000

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

55. The following balances have been excerpted from Edwards' balance sheets:

	<u>December 31, 2013</u>	<u>December 31, 2012</u>
Prepaid Insurance .....	\$ 6,000	\$ 7,500
Interest Receivable .....	3,700	14,500
Salaries Payable .....	61,500	53,000

Edwards Company paid or collected during 2013 the following items:

Insurance premiums paid .....	\$ 41,500
Interest collected .....	123,500
Salaries paid .....	481,000

The salary expense on the income statement for 2013 was

- \$366,500.
- \$472,500.
- \$489,500.
- \$595,500.

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

56. The use of computers in processing accounting data

- eliminates the need for accountants.
- eliminates the double entry system as a basis for analyzing transactions.
- eliminates the need for financial reporting standards such as those promulgated by the FASB.
- may result in the elimination of document trails used to verify accounting records.

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 5  
TOP: AICPA BB-Leveraging Technology                      MSC: AACSB Technology

57. The basic financial statements are listed below:

- Balance sheet
- Statement of retained earnings
- Income statement
- Statement of cash flows

In which of the following sequences does the accountant ordinarily prepare the statements?

- 1, 4, 3, 2
- 2, 1, 3, 4
- 3, 2, 1, 4
- 3, 2, 4, 1

ANS: C                      PTS: 1                      DIF: Easy                      OBJ: LO 1

58. Which of the following regarding accrual versus cash-basis accounting is true?
- a. The FASB believes that the cash basis is appropriate for some smaller companies, especially those in the service industry.
  - b. The cash basis is less useful in predicting the timing and amounts of future cash flows of an enterprise.
  - c. Application of the cash basis results in an income statement reporting only revenues.
  - d. The cash basis requires a complete set of double-entry records.

ANS: B

PTS: 1

DIF: Medium

OBJ: LO 4

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

59. Under the cash basis of accounting,
- a. revenues are recorded when they are earned.
  - b. accounts receivable would appear on the balance sheet.
  - c. depreciation of assets having an economic life of more than one year is recognized.
  - d. the matching principle is ignored.

ANS: D

PTS: 1

DIF: Easy

OBJ: LO 4

TOP: AICPA FN-Measurement

MSC: AACSB Reflective Thinking

60. Total net income over the life of an enterprise is
- a. higher under the cash basis than under the accrual basis.
  - b. lower under the cash basis than under the accrual basis.
  - c. the same under the cash basis as under the accrual basis.
  - d. not susceptible to measurement.

ANS: C

PTS: 1

DIF: Medium

OBJ: LO 4

TOP: AICPA FN-Measurement

MSC: AACSB Reflective Thinking

61. What is the correct order of the following events in the accounting process?

- I. Financial statements are prepared.
- II. Adjusting entries are recorded.
- III. Nominal accounts are closed.

- a. I, II, III
- b. II, I, III
- c. III, II, I
- d. II, III, I

ANS: B

PTS: 1

DIF: Easy

OBJ: LO 1

TOP: AICPA FN-Measurement

MSC: AACSB Reflective Thinking

62. Which of the following is true regarding the accounting process?
- a. Preparation of the trial balance ensures that all amounts have been posted to the correct accounts.
  - b. Preparation of the trial balance is a step in the recording process.
  - c. Preparation of the trial balance determines that total debits equal total credits.
  - d. Preparation of the trial balance determines both that total debits equal total credits and that all amounts have been posted to the correct accounts.

ANS: C

PTS: 1

DIF: Medium

OBJ: LO 1

TOP: AICPA FN-Measurement

MSC: AACSB Analytic

63. An example of a nominal account would be
- Allowance for Doubtful Accounts.
  - Notes Payable.
  - Prepaid Expense.
  - Cost of Goods Sold.

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 1  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

64. Which of the following accounts most likely would *not* appear in a post-closing trial balance?
- Retained Earnings
  - Inventory
  - Sales Revenue
  - Common Stock

ANS: C                      PTS: 1                      DIF: Easy                      OBJ: LO 1  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

65. Which of the following is true?
- Prepaid expenses are increased by a credit.
  - Gains are increased by a debit.
  - Losses are increased by a credit.
  - Accumulated depreciation is increased by a credit.

ANS: D                      PTS: 1                      DIF: Easy                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

66. The following summary balance sheet account categories of Sun Company increased during 2013 by the amounts shown:

Assets .....	\$178,000	Liabilities .....	\$54,000
Capital Stock .....	\$120,000	Additional Paid-in Capital ....	\$12,000

The only change to retained earnings during 2013 was for \$26,000 of dividends. What was Sun Company's net income for 2011?

- \$34,000
- \$26,000
- \$18,000
- \$8,000

ANS: C                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

67. How would proceeds received in advance from the sale of nonrefundable tickets for the Super Bowl be reported in the seller's financial statements published before the Super Bowl?
- Revenue for the entire proceeds.
  - Revenue less related costs.
  - Unearned revenue less related costs.
  - Unearned revenue for the entire proceeds.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

68. Melville Company manufactures electronic components. The company is a calendar-year company. The records of the company show the following information:

	<b><u>Dec.31</u></b> <b><u>2014</u></b>	<b><u>Dec. 31</u></b> <b><u>2013</u></b>
Inventory	\$ 65,000	\$ 72,500
Accounts Payable	18,750	12,500

Melville paid suppliers \$122,500 during 2013. What is Melville's cost of goods sold?

- a. \$136,250
- b. \$123,750
- c. \$121,250
- d. \$108,750

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

69. Richards Company, a calendar-year company, sells magazine subscriptions to subscribers. The magazine is published semiannually and is shipped to subscribers on April 15 and October 15. Only one-year subscriptions for two issues are accepted. Subscriptions received after the March 31 and September 30 cutoff dates are held for the following publication. Cash is received evenly during the year and is credited to deferred subscription revenue. During 2013, \$3,600,000 of cash was received from customers. The beginning balance for 2013 of the deferred subscription revenue account was \$750,000. What is Richards' December 31, 2013, deferred subscription revenue balance?
- a. \$2,700,000.
  - b. \$1,800,000.
  - c. \$1,650,000.
  - d. \$900,000.

ANS: D                      PTS: 1                      DIF: Medium                      OBJ: LO 2  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

70. A bond issued June 1, 2013, by a calendar-year company pays interest on April 1 and October 1. A bond is a financial security issued by a corporation in return for cash borrowed from investors. Bonds typically pay interest twice per year. The investor makes the investment on the date the bond is issued. Interest expense for 2013 is recognized on these bonds by the issuer for a period of
- a. Seven months.
  - b. Six months.
  - c. Four months.
  - d. Three months.

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Reflective Thinking

71. Five percent bonds with a total face value of \$12,000 were purchased at par during the year. The last interest payment for the year was received on July 31. The bonds pay interest semiannually. The adjusting entry at December 31 would include a
- a. debit to interest revenue of \$600.
  - b. debit to interest revenue of \$250.



- c. credit to interest revenue of \$300.
- d. credit to interest revenue of \$250.

ANS: D                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium              OBJ: LO 3  
MSC: AACSB Reflective Thinking

72. A company loaned \$6,000 to another corporation on December 1, Year 1, and received a 90-day, 10 percent, interest-bearing note with a face value of \$6,000. The lender's December 31, Year 1, adjusting entry is

- a. Interest Receivable              \$150  
   Interest Revenue                      \$150
- b. Interest Receivable              \$ 50  
   Interest Revenue                      \$ 50
- c. Interest Revenue              \$100  
   Interest Receivable                      \$100
- d. Interest Revenue              \$150  
   Interest Receivable                      \$150

ANS: B                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium              OBJ: LO 3  
MSC: AACSB Analytic

73. A company sold 10,000 shares of its own \$1 par value common stock for \$60,000. The entry to record the sale would include a

- a. debit to treasury stock for \$60,000.
- b. debit to contributed capital for \$10,000.
- c. credit to common stock, \$1 par value for \$10,000..
- d. credit to common stock, \$1 par value for \$60,000.

ANS: C                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium              OBJ: LO 3  
MSC: AACSB Analytic

74. Total sales for a year are \$40,000, which includes cash sales of \$5,000. The beginning and ending balances of accounts receivable are \$10,000 and \$15,000, respectively. How much cash was received from customers?

- a. \$30,000
- b. \$20,000
- c. \$25,000
- d. \$35,000

ANS: D                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium              OBJ: LO 4  
MSC: AACSB Analytic

75. On August 1, a company received cash of \$9,324 for one year's rent in advance and recorded the transaction on that day as a credit to rent revenue. The December 31 adjusting entry would include

- a. a debit to Rent Revenue for \$3,885.
- b. a credit to Unearned Rent Revenue for \$5,439.
- c. a debit to Unearned Rent Revenue for \$3,885.
- d. a credit to Rent Revenue for \$9,324.

ANS: B                      PTS: 1  
TOP: AICPA FN-Measurement

DIF: Medium              OBJ: LO 3  
MSC: AACSB Analytic

76. For a given year, beginning and ending total liabilities were \$18,000 and \$20,400, respectively. At year-end, owners' equity was \$40,200 and total assets were \$4,000 larger than at the beginning of the year. If new capital stock issued exceeded dividends by \$4,800, net income (loss) for the year was apparently
- \$(3,200).
  - \$(4,000).
  - \$800.
  - \$3,200.

ANS: A                      PTS: 1                      DIF: Challenging    OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

77. At the beginning of the fiscal year, office supplies inventory amounted to \$600. During the year, office supplies amounting to \$8,800 were purchased. This amount was debited to office supplies expense. An inventory of office supplies at the end of the fiscal year showed \$400 of supplies remaining. The beginning of the year balance is still reflected in the office supplies inventory account. What is the required amount of the adjustment to the office supplies expense account?
- \$9,000 debit
  - \$200 debit
  - \$8,400 credit
  - \$8,800 credit

ANS: B                      PTS: 1                      DIF: Challenging    OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

78. Montague Company reported the following balances:

	Beginning of Year	End of Year
Inventory	\$65,000	\$72,500
Accounts payable	18,750	12,500

Montague paid suppliers \$122,500 during the year. What is Montague's cost of goods sold for the year?

- \$136,250
- \$123,750
- \$121,250
- \$108,750

ANS: D                      PTS: 1                      DIF: Medium        OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

79. Caribou Corporation shows the following balances:

	Beginning of Year	End of Year
Inventory	\$80,000	\$72,500
Accounts Payable	40,000	30,000

Caribou paid suppliers \$100,000 during the year. What is Caribou's cost of goods sold for the year?

- \$97,500
- \$107,500
- \$102,500
- \$92,500

ANS: A                      PTS: 1                      DIF: Medium        OBJ: LO 3  
 TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

80. The following is a summary of the increases in the account categories of the balance sheet of Riley Company for the most recent fiscal year:

Assets	\$187,000	Liabilities	\$45,000
Capital Stock	125,000	Additional Paid-in Capital	12,000

The only change to retained earnings during the fiscal year was for \$20,000 of dividends. What was the company's net income for the fiscal year?

- a. \$25,000
- b. \$15,000
- c. \$5,000
- d. \$20,000

ANS: A                      PTS: 1                      DIF: Challenging    OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

81. On August 1 of the current year, Kyle Company borrowed \$278,000 from the local bank. The loan was for 12 months at 9 percent interest payable at the maturity date. The adjusting entry at the end of the fiscal year relating to this obligation would include a
- a. debit to interest expense of \$25,020.
  - b. debit to interest expense of \$10,425.
  - c. credit to note payable of \$10,425.
  - d. debit to interest receivable of \$10,425.

ANS: B                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

82. Carbon Company's accounting records provided the following information (all amounts in thousands of dollars):

Account	Balances 12/31/2012	Balances 12/31/2013
Current Assets	\$ 240	\$ ?
Property, Plant, and Equipment	1,600	1,700
Current Liabilities	?	130
Long-term Liabilities	580	?

All assets and liabilities of the firm are reported in the schedule above. Working capital of \$92 remained unchanged from 2012 to 2013. Net income in 2011 was \$64. No dividends were declared during 2013 and there were no other changes in owners' equity. Total long-term liabilities at the end of 2013 would be

- a. \$340.
- b. \$432.
- c. \$580.
- d. \$616.

ANS: D                      PTS: 1                      DIF: Challenging    OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

83. At the end of the current fiscal year, an analysis of the payroll records of Bev Company showed accrued salaries of \$22,200. The Accrued Salaries Payable account had a balance of \$32,000 at the end of the current fiscal year, which was unchanged from its balance at the end of the prior fiscal year. The books of the company have not yet been closed. The entry needed in this situation would include a
- debit to Retained Earnings of \$9,800.
  - credit to Retained Earnings of \$9,800.
  - debit to Accrued Salaries payable of \$9,800.
  - debit to Salaries Expense of \$9,800.

ANS: C                      PTS: 1                      DIF: Challenging    OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

84. Ryan Company purchased a machine on July 1, 2013. The machine cost \$250,000 and has a salvage value of \$10,000 and a useful life of eight years. The adjusting entry for the year ending December 31, 2014, would include a debit to Depreciation Expense of
- \$30,000.
  - \$15,000.
  - \$31,250.
  - \$15,625.

ANS: A                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

85. Carlton Company sold equipment for \$3,700 that originally cost \$22,000. The balance of the Accumulated Depreciation account related to this equipment was \$19,000. The entry to record the disposal of this equipment would include a
- debit to Loss on Sale of Equipment of \$700.
  - credit to Gain on Sale of Equipment of \$700.
  - credit to Equipment of \$3,000.
  - debit to Gain on Sale of Equipment of \$700.

ANS: B                      PTS: 1                      DIF: Medium                      OBJ: LO 3  
TOP: AICPA FN-Measurement                      MSC: AACSB Analytic

## PROBLEM

- The records of McGarrett Corp. show the following information:
  - Purchased Machine B used in the factory for \$450,000 on July 1, 2010. Machine B has an estimated useful life of 12 years and a residual value of \$30,000. McGarrett uses straight-line depreciation.
  - Sales for 2013 amounted to \$4,000,000, including \$600,000 of sales on credit. Bad debt losses are estimated based on actual experience to be .25% of credit sales.
  - The dollar value of office supplies inventory at the beginning of 2013 equaled \$600. During 2013, office supplies costing \$8,800 were purchased. This amount was debited to office supplies expense. The dollar value of the ending inventory was determined to be \$400. The January 1 balance of \$600 still appears as the balance in the office supplies inventory account.
  - On July 1, 2013, the company paid a three-year insurance premium in the amount of \$2,160. This amount was debited to insurance expense.
  - On October 1, 2013, the company paid rent on some leased office space. The payment of \$7,200 cash was for the following six months. The \$7,200 payment was debited to rent expense

Prepare journal entries to adjust the books of McGarrett Corp. at December 31, 2013.

ANS:

(a)	Depreciation Expense .....	35,000	
	Accumulated Depreciation .....		35,000
(b)	Bad Debt Expense .....	1,500	
	Allowance for Doubtful Accounts .....		1,500
(c)	Office Supplies Expense .....	200	
	Office Supplies Inventory .....		200
(d)	Prepaid Insurance .....	1,800	
	Insurance Expense .....		1,800
(e)	Prepaid Rent .....	3,600	
	Rent Expense .....		3,600

PTS: 1                      DIF: Medium                      OBJ: LO 3                      TOP: AICPA FN-Measurement  
MSC: AACSB Analytic

2. The information listed below was obtained from the accounting records of Williams Company as of December 31, 2013, the end of the company's fiscal year.
  - (a) On August 1, 2013, the company borrowed \$120,000 from the Bank of Wistful Vista. The loan was for 12 months at 9 percent interest payable at the maturity date.
  - (b) Finished goods inventory on January 1, 2013, was \$200,000, and on December 31, 2013, it was \$260,000. Cost of goods sold was \$2,400,000. The company uses a perpetual inventory system.
  - (c) The company owned some property (land) that was rented to J. McArthur on April 1, 2013, for 12 months for \$8,400. On April 1, the entire annual rental of \$8,400 was credited to rent collected in advance, and cash was debited.
  - (d) .On September 1, 2013, the company loaned \$60,000 to an outside party. The loan was at 10 percent per annum and was due in six months; interest is payable at maturity. Cash was credited for \$60,000, and notes receivable was debited on September 1 for the entire amount.
  - (e) Accrued salaries and wages are \$18,000 at December 31, 2013.
  - (f) On January 1, 2013, factory supplies on hand equaled \$200. During 2013, factory supplies costing \$4,000 were purchased and debited to factory supplies inventory. At the end of 2013, a physical inventory count showed that factory supplies on hand equaled \$800..

Prepare journal entries to adjust the books of Williams Company at December 31, 2013.

ANS:

(a)	Interest Expense .....	4,500	
	Interest Payable .....		4,500
(b)	No entry required		
(c)	Rent Collected in Advance .....	6,300	
	Rent Revenue .....		6,300
(d)	Interest Receivable .....	2,000	
	Interest Revenue .....		2,000
(e)	Salaries and Wages Expense .....	18,000	
	Salaries and Wages Payable .....		18,000
(f)	Office Supplies Expense .....	3,400	
	Office Supplies .....		3,400

PTS: 1                      DIF: Medium                      OBJ: LO 3                      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

3. The records of Majestic Co. showed the following account balances on December 31, 2013:

Inventory, December 31, 2013 .....	\$159,500
Purchases .....	376,500
Freight-In .....	1,200
Purchase Discounts .....	4,000
Purchase Returns and Allowance .....	8,200

Assuming that the inventory balance at January 1, 2013, is \$152,000, prepare the entry to adjust the inventory accounts.

ANS:

Inventory, 12/31/2013 .....	159,500	
Purchase Discounts .....	4,000	
Purchase Returns and Allowances .....	8,200	
Cost of Goods Sold .....	358,000	
Purchases .....		376,500
Freight-In .....		1,200
Inventory, 1/1/2013 .....		152,000

PTS: 1                      DIF: Medium                      OBJ: LO 3                      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

4. The following account balances pertain to the Henryville Manufacturing Co. at December 31, 2013 (before adjusting entries).

	<u>Debit</u>	<u>Credit</u>
Cash .....	\$300,000	
Prepaid Insurance .....	50,000	
Land .....	400,000	
Accounts Payable .....		30,000
Common Stock .....		250,000
Retained Earnings .....		150,000
Service Revenue .....		650,000
Wages Expense .....	150,000	
Rent Expense .....	180,000	
Total .....	<u>\$1,080,000</u>	<u>\$1,080,000</u>

Additional information:

- (a) Prepaid insurance in the trial balance represents an advance payment for 5 months of insurance made on November 1, 2013.
- (b) In July, the accountant debited accounts payable for a \$10,000 fine for a pollution violation; "Environmental Expense" should have been debited.
- (c) Rent expense in the trial balance represents an advance payment for 6 months rent paid on October 1, 2013. The Company begins occupying the property on that date.
- (d) Unpaid and unrecorded wages earned by employees at December 31, 2013, were \$60,000.

(e) The income tax liability for the year is \$100,000, payable April 15, 2014.

**Required:**

- (1) Prepare adjusting entries to Henryville Co.'s accounts at December 31, 2013. Each entry should be made in general journal format. Identify each entry by using the letter of the paragraph containing the additional information for the entry.
- (2) Prepare the current year income statement
- (3) Prepare the current year retained earnings statement.
- (4) Prepare the current year balance sheet.
- (5) Prepare the closing entries.

ANS:

**Part 1**

(a)	Insurance Expense .....	20,000	
	Prepaid Insurance .....		20,000
(b)	Environmental Expense .....	10,000	
	Accounts Payable .....		10,000
(c)	Prepaid Rent .....	90,000	
	Rent Expense .....		90,000
(d)	Wages Expense .....	60,000	
	Wages Payable .....		60,000
(e)	Income Tax Expense .....	100,000	
	Income Tax Payable .....		100,000

**Part 2**

**Henryville  
Manufacturing Co.  
Income Statement  
For the Year Ended December 31, 2013**

Service Revenue	\$
	650,000
Insurance Expense	20,000
Environmental Expense	10,000
Rent Expense	90,000
Wages Expense	210,000
Income Tax Expense	<u>100,000</u>
Net Income	<u>\$</u> <u>220,000</u>

**Part 3**

**Henryville Manufacturing Co.**

**Retained Earnings Statement**  
**For the Year Ending December 31, 2013**

Retained Earnings, January 1	\$
	150,000
Net Income	
	<u>220,000</u>
Retained Earnings, December 31	<u>\$</u>
	<u>370,000</u>

**Part 4**                      **Henryville**  
**Manufacturing Co.**  
**Balance Sheet**  
**December 31, 2013**

**Assets**

Cash	\$
	300,000
Prepaid Insurance	30000
Prepaid Rent	90000
Land	
	<u>400,000</u>

**Total Assets**

\$  
820,000

**Liabilities**

Accounts Payable	\$
	40,000
Wages Payable	
	60,000
Income Tax Payable	
	100,000
Common Stock	
	250,000
Retained Earnings	
	<u>370,000</u>

**Total Liabilities &**  
**Stockholders' Equity**

\$  
820,000

**Part 5**

Service Revenue		
	650,000	
Income		
Summary		650,000
Income Summary		
	430,000	
Insurance Expense		
		20,000
Environmental Expense		
		10,000



Rent Expense		90,000
Wages Expense		210,000
Income Tax Expense		100,000
Income Summary	220,000	
Retained Earnings		220,000

PTS: 1      DIF: Medium      OBJ: LO 3      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

5. Schroeder Co. had the following transactions pertaining to the fiscal year ended October 31, 2011.

- June 15, 2011, paid an annual casualty insurance premium of \$5,400 for a policy beginning July 1, 2011.
- October 1, 2011, received advance payment of \$6,930 from a customer for a 9-month equipment rental.

Provide the appropriate journal entries to record the preceding transactions. Adjust the accounts at year-end assuming that no entries have been made between the transaction date and year-end and assuming that:

- (1) transactions were originally recorded in asset and liability accounts.
- (2) transactions were originally recorded in revenue and expense accounts.

ANS:

- (1) Insurance:
- |         |   |       |       |
|---------|---|-------|-------|
| June 15 | Prepaid Insurance .....                           | 5,400 |       |
|         | Cash .....  |       | 5,400 |
| Oct. 31 | Insurance Expense ( $\$5,400 \times 4/12$ ) ..... | 1,800 |       |
|         | Prepaid Insurance .....                           |       | 1,800 |
- Equipment rental:
- |         |  |       |       |
|---------|--|-------|-------|
| Oct. 1  | Cash .....   | 6,930 |       |
|         | Unearned Rent Revenue .....                          |       | 6,930 |
| Oct. 31 | Unearned Rent Revenue ( $\$6,930 \times 1/9$ ) ..... | 770   |       |
|         | Rent Revenue .....                                   |       | 770   |
- (2) Insurance:
- |         |   |       |       |
|---------|---|-------|-------|
| June 15 | Insurance Expense .....                           | 5,400 |       |
|         | Cash .....  |       | 5,400 |
| Oct. 31 | Prepaid Insurance ( $\$5,400 \times 8/12$ ) ..... | 3,600 |       |
|         | Insurance Expense .....                           |       | 3,600 |
- Equipment rental:
- |        |            |       |  |
|--------|------------|-------|--|
| Oct. 1 | Cash ..... | 6,930 |  |
|--------|------------|-------|--|

	Rent Revenue .....		6,930
Oct. 31	Rent Revenue (\$6,930 × 8/9) .....	6,160	
	Unearned Rent Revenue .....		6,160

PTS: 1 DIF: Medium OBJ: LO 2 | LO 3 TOP: AICPA FN-Measurement  
MSC: AACSB Analytic

6. Record the following transactions and events of Royal Wulff Company in general journal form. If the item does not require a journal entry, write "no entry."
- Sold merchandise costing \$4,500 for \$1,000 cash and \$7,000 on open account. A perpetual inventory system is used.
  - Purchased land and building for \$100,000 cash and a \$300,000 mortgage. The land was recently appraised at \$60,000 and the building at \$340,000.
  - Received payment on account, \$12,000.
  - Estimated that utilities expense for the coming six months will total \$7,600.
  - Declared a cash dividend totaling \$13,500. The dividend will be paid in six weeks.

ANS:

(a)	Cash .....	1,000	
	Accounts Receivable .....	7,000	
	Sales .....		8,000
	Cost of Goods Sold .....	4,500	
	Inventory .....		4,500
(b)	Land .....	60,000	
	Building .....	340,000	
	Cash .....		100,000
	Mortgage Payable .....		300,000
(c)	Cash .....	12,000	
	Accounts Receivable .....		12,000
(d)	No entry .....		
(e)	Dividends (or Retained Earnings) .....	13,500	
	Dividends Payable .....		13,500

PTS: 1 DIF: Easy OBJ: LO 2 TOP: AICPA FN-Measurement  
MSC: AACSB Analytic

7. For each of the journal entries below, write a description of the underlying event. Assume that for prepaid expenses original debits are made to an expense account.

(a)	Allowance for Doubtful Accounts .....	xxx	
	Accounts Receivable .....		xxx
(b)	Interest Expense .....	xxx	
	Notes Payable .....	xxx	
	Cash .....		xxx
(c)	Cash .....	xxx	
	Unearned Revenue .....		xxx
(d)	Supplies on Hand .....	xxx	
	Supplies Expense .....		xxx
(e)	Cash .....	xxx	
	Accounts Receivable .....		xxx

ANS:

- (a) Write-off of an uncollectible account.
- (b) Cash payment on a note payable. Part of the payment is for principal and part is for interest.
- (c) Received cash in advance for products or services not yet delivered.
- (d) Adjusting entry to record supplies on hand.
- (e) Received customer payment on account.

PTS: 1                      DIF: Easy                      OBJ: LO 2                      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

8. The following data are from a comparison of the balance sheets of Brassie Company as of December 31, 2013, and December 31, 2012:

Accounts Receivable .....	increase	\$7,600
Inventory .....	decrease	4,500
Accounts Payable .....	increase	2,400
(all accounts payable relate to inventory purchases)		
Prepaid Insurance .....	decrease	1,350
Wages Payable .....	decrease	670

The following data are from Brassie's 2011 income statement:

Sales .....	\$200,000
Cost of Goods Sold .....	110,000
Insurance Expense .....	25,000
Wages Expense .....	40,000

During 2013:

- (a) How much cash was collected from customers?
- (b) How much cash was paid for inventory purchases?
- (c) How much cash was paid for insurance?
- (d) How much cash was paid for wages?

ANS:

- (a)  $\$200,000 - \$7,600 = \$192,400$
- (b)  $\$110,000 - \$4,500 - \$2,400 = \$103,100$
- (c)  $\$25,000 - \$1,350 = \$23,650$
- (d)  $\$40,000 + \$670 = \$40,670$

PTS: 1                      DIF: Medium                      OBJ: LO 2                      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

9. Pheasant Tail Company's total equity increased by \$32,000 during 2013. New stockholder investment during the year totaled \$65,000. Total revenues during the year were \$500,000 and total expenses were \$460,000. Cash on hand decreased by \$7,500 during the year. What amount of dividends did Pheasant Tail declare during 2013?

ANS:

Increase in total equity during 2013 .....	\$ 32,000
New stockholder investment .....	<u>65,000</u>
Decrease in retained earnings during 2013 .....	<u>\$(33,000)</u>

Net income (\$500,000 – \$460,000) .....	<u>40,000</u>
Difference = Dividends declared during 2013 .....	<u>\$ 73,000</u>

PTS: 1                      DIF: Medium                      OBJ: LO 2                      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

10. The trial balance and transaction descriptions below are for Coachman Company:

Coachman Company Trial Balance February 1, 2013		
	<u>Debit</u>	<u>Credit</u>
Cash .....	\$ 250	
Accounts Receivable .....	320	
Inventory .....	495	
Equipment .....	1,200	
Accumulated Depreciation .....		\$ 245
Accounts Payable .....		185
Mortgage Payable .....		900
Common Stock .....		300
Retained Earnings .....		<u>635</u>
	<u>\$2,265</u>	<u>\$2,265</u>

Summary transactions for February:

- (a) Collected \$100 on open account
- (b) Purchased \$130 inventory for \$20 cash and the remainder on open account.
- (c) Bought new equipment costing \$200 for \$50 cash, with the remainder due on a mortgage payable.
- (d) Paid \$85 on open account.
- (e) Recorded depreciation expense of \$35.
- (f) Sold goods costing \$90 for \$30 cash and \$120 on open account.

What is Coachman's total equity at the end of February?

ANS:

Retained Earnings			
		Begin	635
(e)	35		
(f)	90	(f)	150
			660

Total equity = Retained Earnings \$660 + Common Stock \$300 = \$960.

PTS: 1                      DIF: Medium                      OBJ: LO 2                      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

11. Account balances taken from the ledger of Middler Company on December 31, 2013, are as follows:

Accounts Payable .....	\$119,000
------------------------	-----------

Accounts Receivable .....	139,200
Advertising Expense .....	12,000
Accumulated Depreciation--Buildings .....	31,500
Allowance for Doubtful Accounts .....	2,550
Buildings .....	315,000
Capital Stock, \$10 par .....	450,000
Cash .....	45,750
Dividends .....	12,000
Freight-In .....	10,500
Insurance Expense .....	2,100
Interest Expense .....	5,295
Interest Revenue .....	1,335
Inventory, December 31, 2012 .....	104,850
Land .....	78,000
Long-Term Investments .....	12,150
Mortgage Payable .....	43,500
Notes Payable--Short-Term .....	24,000
Office Expense .....	28,800
Purchases .....	521,130
Purchase Discounts .....	12,150
Retained Earnings, December 31, 2012 .....	13,695
Sales .....	745,000
Sales Discounts .....	24,750
Sales Returns .....	14,400
Selling Expense .....	94,050
Supplies Expense .....	3,450
Real Estate and Payroll Taxes .....	19,305

Adjustments on December 31, 2013, are required as follows:

- (a) The inventory on hand is \$135,915.
- (b) The allowance for doubtful accounts is to be increased to a balance of \$6,250.
- (c) Buildings are depreciated at the rate of 5 percent per year.
- (d) Accrued selling expenses are \$6,075.
- (e) There are supplies of \$1,050 on hand.
- (f) Prepaid insurance at December 31, 2013, totals \$1,290.
- (g) Accrued interest on long-term investments is \$360.
- (h) Accrued real estate and payroll taxes are \$1,170.
- (i) Accrued interest on the mortgage is \$240.
- (j) Income tax is estimated to be 30 percent of the income before income tax (round to nearest dollar).

- (1) Prepare an eight-column work sheet.
- (2) Prepare adjusting and closing entries.

ANS:

- (1)

Middler Company  
Work Sheet  
For Year Ended December 31, 2013

Trial Balance		Adjustment	
<u>Debit</u>	<u>Credit</u>	<u>Debit</u>	<u>Credit</u>

Cash .....	45,750				
Accounts Receivable .....	139,200				
Allowance for Doubtful					
Accounts .....		2,550		(b)	3,700
Inventory .....	104,850		(a)	31,065	
Interest Receivable .....			(g)	360	
Prepaid Insurance .....			(f)	1,290	
Supplies on Hand .....			(e)	1,050	
Long-Term Investments .....	12,150				
Land .....	78,000				
Buildings .....	315,000				
Accumulated					
Depreciation--Buildings.....		31,500		(c)	15,750
Accounts Payable .....		119,000			
Selling Expense Payable.....				(d)	6,075
Real Estate and Payroll Taxes					
Payable .....				(h)	1,170
Interest Payable .....				(i)	240
Income Taxes Payable					
(0.30 × \$29,535) .....				(j)	8,861
Notes Payable--Short-Term...		24,000			
Mortgage Payable .....		43,500			
Capital Stock, \$10 par.....		450,000			
Retained Earnings, Dec. 31,					
2012.....		13,695			
Dividends .....	12,000				
Sales .....		745,000			
Sales Discounts .....	24,750				
Sales Returns .....	14,400				
Interest Revenue .....		1,335		(g)	360
Purchases .....	521,130			(a)	521,130
Purchase Discounts .....		12,150	(a)	12,150	
Freight-In .....	10,500			(a)	10,500
Cost of Goods Sold .....			(a)	488,415	
Real Estate and Payroll .....					
Taxes Expense .....	19,305		(h)	1,170	
Selling Expense .....	94,050		(d)	6,075	
Supplies Expense .....	3,450			(e)	1,050
Doubtful Accounts Expense..			(b)	3,700	
Depreciation Expense--					
Buildings .....			(c)	15,750	
Income Tax Expense .....			(j)	8,861	
Advertising Expense .....	12,000				
Insurance Expense .....	2,100			(f)	1,290
Interest Expense .....	5,295		(i)	240	
Office Expense .....	<u>28,800</u>				
	<u>1,442,730</u>	<u>1,442,730</u>		<u>570,126</u>	<u>570,126</u>

Middler Company  
Work Sheet  
For Year Ended December 31, 2013

<u>Income Statement</u>	<u>Balance Sheet</u>
<u>Debit</u> <u>Credit</u>	<u>Debit</u> <u>Credit</u>

Cash .....			45,750	
Accounts Receivable .....			139,200	
Allowance for Doubtful Accounts .....				6,250
Inventory .....			135,915	
Interest Receivable .....			360	
Prepaid Insurance .....			1,290	
Supplies on Hand .....			1,050	
Long-Term Investments .....			12,150	
Land .....			78,000	
Buildings .....			315,000	
Accumulated Depreciation-- Buildings .....				47,250
Accounts Payable .....				119,000
Selling Expense Payable .....				6,075
Real Estate and Payroll Taxes Payable .....				1,170
Interest Payable .....				240
Income Taxes Payable (.30 × \$29,535) .....				8,861
Notes Payable--Short-Term .....				24,000
Mortgage Payable .....				43,500
Capital Stock, \$10 par .....				450,000
Retained Earnings, Dec. 31, 2013 .....				13,695
Dividends .....			12,000	
Sales .....		745,000		
Sales Discounts .....	24,750			
Sales Returns .....	14,400			
Interest Revenue .....		1,695		
Purchases .....				
Purchase Discounts .....				
Freight-In .....				
Cost of Goods Sold .....	488,415			
Real Estate and Payroll Taxes Expense .....	20,475			
Selling Expense .....	100,125			
Supplies Expense .....	2,400			
Doubtful Accounts Expense .....	3,700			
Depreciation Expense-- Buildings .....	15,750			
Income Tax Expense .....	8,861			
Advertising Expense .....	12,000			
Insurance Expense .....	810			
Interest Expense .....	5,535			
Office Expense .....	<u>28,800</u>			
	726,021	746,695	740,715	720,041
Net Income.....	<u>20,674</u>	<u>      </u>	<u>      </u>	<u>20,674</u>
	<u>746,695</u>	<u>746,695</u>	<u>740,715</u>	<u>740,715</u>

(2)

#### Adjusting Entries

(a) Inventory ..... 31,065

	Purchase Discounts .....	12,150	
	Cost of Goods Sold .....	488,415	
	Purchases .....		521,130
	Freight-In .....		10,500
(b)	Doubtful Accounts Expense .....	3,700	
	Allowance for Doubtful Accounts .....		3,700
(c)	Depreciation Expense, Buildings .....	15,750	
	Accumulated Depreciation, Buildings .....		15,750
(d)	Selling Expense .....	6,075	
	Selling Expense Payable .....		6,075
(e)	Supplies on Hand .....	1,050	
	Supplies Expense .....		1,050
(f)	Prepaid Insurance .....	1,290	
	Insurance Expense .....		1,290
(g)	Interest Receivable .....	360	
	Interest Revenue .....		360
(h)	Real Estate and Payroll Taxes .....	1,170	
	Real Estate and Payroll Taxes Payable .....		1,170
(i)	Interest Expense .....	240	
	Interest Payable .....		240
(j)	Income Tax .....	8,861	
	Income Tax Payable .....		8,861

#### Closing Entries

	Interest Revenue .....	1,695	
	Sales .....	745,000	
	Retained Earnings .....		746,695
	Retained Earnings .....	726,021	
	Cost of Goods Sold .....		488,415
	Advertising Expense .....		12,000
	Insurance Expense .....		810
	Interest Expense .....		5,535
	Office Expense .....		28,800
	Sales Discounts .....		24,750
	Sales Returns .....		14,400
	Selling Expense .....		100,125
	Real Estate and Payroll Taxes .....		20,475
	Supplies Expense .....		2,400
	Doubtful Accounts Expense .....		3,700
	Depreciation Expense, Buildings .....		15,750
	Income Tax Expense .....		8,861
	Retained Earnings .....	12,000	
	Dividends .....		12,000

PTS: 1                      DIF: Challenging    OBJ: LO 2 | LO 3

TOP: AICPA FN-Measurement | AICPA FN-Reporting

MSC: AACSB Analytic

12. Account balances taken from the ledger of Owens Company on December 31, 2013, are as follows:

Accounts Payable .....	\$ 23,000
------------------------	-----------



Accounts Receivable .....	38,000
Accumulated Depreciation--Equipment .....	64,000
Allowance for Doubtful Accounts .....	2,000
Patent .....	8,400
Capital Stock, \$10 par .....	100,000
Cash .....	60,260
Inventory .....	105,000
Sales Supplies Inventory .....	900
Extraordinary Gain (net of tax) .....	10,000
Interest Expense .....	6,600
Inventory, December 31, 2012 .....	104,850
Contributed Capital in Excess of Par Value .....	15,000
Long-Term Note Receivable, 14% .....	12,000
Mortgage Payable, 12% .....	60,000
Investment Revenue .....	1,120
Accumulated Depreciation-Equipment .....	64,000
Rent Revenue .....	3,000
Retained Earnings, December 31, 2012 .....	32,440
Sales .....	700,000
Cost of Goods Sold .....	380,000
Selling Expenses .....	164,400
General and Administrative Expenses .....	55,000
Equipment .....	180,000

Adjustments on December 31, 2013, are required as follows:

- (a) Estimated bad debt loss rate is 1/4 percent of credit sales. Credit sales for the year amounted to \$200,000. Classify bad debt expense as a selling expense.
  - (b) Interest on the long-term note receivable was last collected August 31, 2013.
  - (c) Estimated life of the equipment is 10 years, with a residual value of \$20,000. Allocate 10 percent of depreciation expense to general and administrative expense and the remainder to selling expenses. Use straight-line depreciation.
  - (d) Estimated economic life of the patent is 14 years (from January 1, 2013) with no residual value. Straight-line amortization is used. Depreciation expense is classified as selling expense.
  - (e) Interest on the mortgage payable was last paid on November 30, 2013.
  - (f) On June 1, 2013, the company rented some office space to a tenant for one year and collected \$3,000 rent in advance for the year; the entire amount was credited to rent revenue on this date.
  - (g) On December 31, 2013, the company received a statement for calendar year 2013 property taxes amounting to \$1,300. The payment is due February 15, 2014. Assume that the payment will be made on February 15, 2014, and classify expense as selling expense.
  - (h) Sales supplies on hand at December 31, 2013, amounted to \$300; classify as selling expense.
  - (i) Assume an average income tax rate of 40 percent corporate tax rate on all items including the extraordinary gain..
- (1) Prepare an eight-column work sheet.
  - (2) Prepare adjusting and closing entries.

ANS:

(1)

Owens Company  
Work Sheet  
For Year Ended December 31, 2013

	Trial Balance		Adjustment	
	<u>Debit</u>	<u>Credit</u>	<u>Debit</u>	<u>Credit</u>
Cash .....	60,260			
Accounts Receivable .....	38,000			
Allowance for Doubtful Accounts .....		2,000	(a)	500
Inventory .....	105,000			
Interest Receivable .....		(b)	560	
Sales Supplies Inventory .....	900		(h)	600
Long-Term Note Receivable, 12% .....	12,000			
Equipment .....	180,000			
Accumulated Depreciation--Equipment .....		64,000	(c)	16,000
Patent.....	8,400		(d)	600
Accounts Payable .....		23,000		
Interest Payable .....			(e)	600
Property Taxes Payable .....			(g)	1,300
Rent Collected in Advance ...			(f)	1,250
Mortgage Payable .....		60,000		
Capital Stock, \$10 par.....		100,000		
Contributed Capital in Excess of Par .....		15,000		
Retained Earnings, Jan. 1, 2013.....		32,440		
Sales .....		700,000		
Interest Revenue .....		1,120	(b)	560
Rent Revenue .....		3,000	(f)	1,250
Cost of Goods Sold .....	380,000			
Selling Expenses .....	164,400		(a)	500
			(c)	14,400
			(d)	600
			(g)	1,300
			(h)	600
General and Administrative Expenses .....	55,000		(c)	1,600
Interest Expense .....	6,600		(e)	600
Extraordinary Gain .....		10,000		
	<u>1,010,560</u>	<u>1,010,560</u>	<u>21,410</u>	<u>21,410</u>
Income Tax Expense .....			(i)	35,132
Income Tax Payable .....			(i)	35,132
Net Income .....				
Totals .....				

Owens Company  
Work Sheet  
For Year Ended December 31, 2013

<u>Income Statement</u>		<u>Balance Sheet</u>	
<u>Debit</u>	<u>Credit</u>	<u>Debit</u>	<u>Credit</u>

Cash .....	60,260	
Accounts Receivable .....	38,000	
Allowance for Doubtful Accounts .....		2,500
Inventory .....	105,000	
Sales Supplies Inventory .....	300	
Interest Receivable .....	560	
Long-Term Note Receivable, 12% .....	12,000	
Equipment .....	180,000	
Accumulated Depreciation-Equipment .....		80,000
Patent .....	7,800	
Accounts Payable .....		23,000
Interest Payable .....		600
Property Taxes Payable .....		1,300
Rent Collected in Advance .....		1,250
Mortgage Payable .....		60,000
Common Stock, par \$10 .....		100,000
Contributed Capital in Excess of Par .....		15,000
Retained Earnings, Jan. 1, 2013 .....		32,440
Sales .....	700,000	
Interest Revenue .....	1,680	
Rent Revenue .....	1,750	
Cost of Goods Sold .....	380,000	
Selling Expense .....	181,800	

General and Administrative Expense .....	56,600		
Extraordinary Gain .....		10,000	
Interest Expense .....	7,200		
Income Tax Expense .....	35,132		
Income Tax Payable .....			35,132
Net Income .....	<u>52,698</u>		<u>52,698</u>
Totals .....	<u>713,430</u>	<u>713,430</u>	<u>403,920</u> <u>403,920</u>

(2)

#### Adjusting Entries

(a) Bad Debt Expense .....	500	
Allowance for Doubtful Accounts .....		500
(b) Interest Receivable .....	560	
Interest Revenue .....		560
(c) Depreciation Expense, Equipment (Selling) .....	14,400	
Depreciation Expense, Equipment (General/Admin) ....	1,600	
Accumulated Depreciation, Equipment .....		16,000
(d) Selling Expenses (Patent Amortization) .....	600	
Patent .....		600
(e) Interest Expense .....	600	

	Interest Payable .....		600
(f)	Rent Revenue .....	1,250	
	Rent Collected in Advance .....		1,250
(g)	Selling Expenses (Property Taxes) .....	1,300	
	Property Taxes Payable .....		1,300
(h)	Selling Expenses (Sales Supplies) .....	600	
	Sales Supplies Inventory .....		600
(i)	Income Tax .....	35,132	
	Income Tax Payable .....		35,132

#### Closing Entries

Interest Revenue .....	1,680	
Sales .....	700,000	
Rent Revenue .....	1,750	
Extraordinary Gain .....	10,000	
Retained Earnings .....		713,430
Retained Earnings .....	660,732	
Cost of Goods Sold .....		380,000
Selling Expenses .....		181,800
General and Administrative Expenses .....		56,600
Interest Expense .....		7,200
Income Tax Expense .....		35,132

PTS: 1                      DIF: Challenging    OBJ: LO 2 | LO 3

TOP: AICPA FN-Measurement | AICPA FN-Reporting

MSC: AACSB Analytic

13. Presented below is the December 31 trial balance of Cassini Studios.

#### Cassini Studios Trial Balance December 31, 2013

	<u>Debit</u>	<u>Credit</u>
Cash .....	\$ 14,800	
Accounts Receivable .....	33,600	
Allowances for Doubtful Accounts .....		\$ 2,160
Inventory, January 1 .....	62,400	
Furniture and Equipment .....	67,200	
Accumulated Depreciation--Furniture and Equipment .....		26,880
Prepaid Insurance .....	4,080	
Notes Payable .....		22,400
Cassini, Capital .....		72,000
Sales .....		480,000
Purchases .....	320,000	
Sales Salaries Expense .....	40,000	
Advertising Expense .....	5,360	
Administrative Salaries Expense .....	52,000	
Office Expense .....	4,000	
	<u>\$603,440</u>	<u>\$603,440</u>

- (1) Prepare adjusting journal entries for the following items:

- (a) Adjust the Allowance for Doubtful Accounts to 8 percent of the accounts receivable.
  - (b) Furniture and equipment is depreciated at 20 percent per year.
  - (c) Insurance expired during the year, \$2,040.
  - (d) Interest accrued on notes payable, \$2,688.
  - (e) Sales salaries earned but not paid, \$1,920.
  - (f) Advertising paid in advance, \$560.
  - (g) Office supplies on hand, \$1,200, charged to Office Expense when purchased.
- (2) Prepare closing entries for Cassini after the above adjusting entries have been made. Additional information shows the inventory on December 31 was \$64,000.

ANS:

(1)			
(a)	Bad Debts Expense .....	528	
	Allowance for Doubtful Accounts .....		528
(b)	Depreciation Expense--Furniture and Equipment .....	13,440	
	Accumulated Depreciation--Furniture and Equipment .....		13,440
(c)	Insurance Expense .....	2,040	
	Prepaid Insurance .....		2,040
(d)	Interest Expense .....	2,688	
	Interest Payable .....		2,688
(e)	Sales Salaries Expense .....	1,920	
	Salaries Payable .....		1,920
(f)	Prepaid Advertising .....	560	
	Advertising Expense .....		560
(g)	Office Supplies on Hand .....	1,200	
	Office Expense .....		1,200
(2)			
Dec. 31	Cost of Goods Sold .....	318,400	
	Inventory .....	1,600	
	Purchases .....		320,000
Dec. 31	Sales .....	480,000	
	Retained Earnings .....		480,000
Dec. 31	Retained Earnings .....	438,616	
	Cost of Goods Sold .....		318,400
	Advertising Expense .....		4,800
	Administrative Salaries Expense .....		52,000
	Sales Salaries Expense .....		41,920
	Office Expense .....		2,800
	Insurance Expense .....		2,040
	Bad Debts Expense .....		528
	Depreciation Expense--Furniture and Equipment .....		13,440
	Interest Expense .....		2,688

PTS: 1      DIF: Medium      OBJ: LO 3      TOP: AICPA FN-Measurement  
 MSC: AACSB Analytic

14. The following ten items are independent of each other. For each item, indicate the amount of any cash flow that occurs or state that no cash flow resulted from the item.
1. Prepaid rent decreased \$20,000 during the year. Rent expense recognized for the year amounted to \$30,000.
  2. Patent amortization recognized amounted to \$30,000.
  3. Net income was \$100,000; retained earnings increased \$60,000; and dividends payable decreased \$20,000.
  4. Wages payable decreased \$12,000 and wages expense for the year amounted to \$48,000.
  5. The balance in accounts receivable at the beginning of the year was \$600,000, and at the end of the year was \$175,000. Sales for the year were \$1,000,000. The balance of the allowance for doubtful accounts was \$20,000 at the beginning of the year and \$35,000 at the end of the year. Bad debt expense for the year was \$40,000.
  6. Sales on account for the year are \$1,000 and the balance in accounts receivable increased \$200 during the year. All sales are on account.
  7. Sale at a gain of \$500 of a plant asset costing \$4,000 with \$2,500 of accumulated depreciation.
  8. The balance in accumulated depreciation increased \$10,000 for the year. No disposals of plant assets occurred during the year.
  9. At the beginning of the fiscal year, merchandise inventory amounted to \$30,000. A physical count at year-end showed \$37,000 worth of inventory on hand. The balance of accounts payable at the beginning of the fiscal year was \$26,000 and at the end of the fiscal year was \$30,000. Cost of goods sold for the fiscal year was \$42,000. The company uses a perpetual inventory system.
  10. The retained earnings account decreased \$10,000. Net income for the fiscal year was \$15,000. Dividends payable decreased \$10,000.

ANS:

1. Of the total rent expense, \$20,000 represented the expiration of prepaid rent paid for an earlier period while \$10,000 of rent was actually paid in cash during the current period.
2. No cash flow is associated with depreciation or amortization; these are noncash expenses.
3. Dividends declared equals  $\$100,000 - \$60,000 = \$40,000$ . Dividends payable decreased \$20,000 such that \$60,000 of dividends were paid.
4. Wages expense for the year was \$48,000 and wages payable decreased by \$12,000, which means that wages paid must have been \$60,000.
5. Begin with the allowance account and determine the amount of the accounts written off ( $\$20,000 + \$40,000 - \$35,000 = \$25,000$ ). Go to the accounts receivable account and calculate the amount of cash collected on receivables ( $\$600,000 + \$1,000,000 - \$25,000 - \$175,000 = \$1,400,000$ ).
6. Sales exceeded cash collections by \$200 since accounts receivable increased resulting in cash flows of \$800.
7. Book value of the plant asset costing \$4,000 with \$2,500 accumulated depreciation is \$1,500. A gain of \$500 results from a selling price of \$1,500 book value + \$500 gain, or \$2,000, the amount of the cash flow in the transaction.
8. Depreciation expense for the year was \$10,000. There was no cash flow since depreciation is a noncash expense.
9. Cash payments to supplies equal \$45,000. This amount is determined by subtracting from cost of goods sold of \$42,000 the \$4,000 increase in accounts payable and adding the \$7,000 increase in inventory.
10. Dividends declared equals  $\$15,000 + \$10,000 = \$25,000$ . Dividends payable

decreased \$10,000 such that dividends paid equals \$35,000.

PTS: 1 DIF: Challenging OBJ: LO 2 | LO 4 TOP: AICPA FN-Measurement  
MSC: AACSB Analytic

15. The following information is available for the Central Company:

**Central Company  
Balance Sheet  
December 31, xxxx**

<b><u>ASSETS</u></b>		
	<b><u>Current Year</u></b>	<b><u>Prior Year</u></b>
Cash	\$125,000	\$100,000
Accounts Receivable	515,000	500,000
Allowance for Doubtful Accounts	(70,150)	(60,000)
Inventory	660,000	500,000
Prepaid Expenses	80,000	72,000
Equipment	892,000	900,000
Less: Accumulated Depreciation	(460,000)	(452,500)
<b><u>LIABILITIES</u></b>		
Accounts Payable	430,000	370,000
Accrued Expenses	250,000	230,000
Income Tax Payable	58,000	50,000

**Central Company  
Income Statement  
For Year Ending December 31, xxxx**

Sales (all sales are on credit)	\$780,000
Cost of Goods Sold	<u>450,000</u>
Gross Profit	\$330,000
Operating Expenses:	
Bad Debt Expense	25,150
Depreciation Expense	11,500
Other Operating Expenses	160,000
Loss on Sale of Equipment	1,500
Income Tax Expense	43,000

Determine the amount of cash flow associated with each of the following items:

1. Cash receipts from customers.
2. Cash payments to suppliers.
3. Cash payments for other operating expenses.
4. Cash received from sale of equipment (no equipment purchases were made during the year and only one sale of equipment occurred during the years).
5. Cash paid for income taxes.

ANS:

1. Cash flows from sales to customers for the fiscal year equals the amount of cash collected on accounts receivable. The change in accounts receivable cannot be determined without considering the change in the allowance account. The allowance account had a beginning balance of \$60,000, bad debt expense for the year was \$25,150, and the ending balance of the allowance was \$70,150. The amount of accounts written off against the allowance for the year is  $\$60,000 + \$25,150 - \$70,150 = \$15,000$ . The change in accounts receivable is determined by taking the beginning balance of receivables, adding credit sales, subtracting the amount of accounts written off, and subtracting the ending balance of accounts receivable. This computation is  $\$500,000 + \$780,000 - \$15,000 - \$515,000 = \$750,000$ , the amount of cash collected from customers.
2. Cash payments to suppliers equals purchases minus increase in accounts payable. Purchases for the period equals cost of goods sold plus increase in inventory, or  $\$450,000 + (\$660,000 - \$500,000) = \$610,000$ . Change in accounts payable equals  $\$430,000 - \$370,000 = \$60,000$ . Purchases minus increase in accounts payable equals  $\$610,000 - \$60,000 = \$550,000$ , the total cash payments to suppliers.
3. Cash payments for other operating expenses equals accrual basis operating expenses plus the increase in prepaid expenses minus the increase in accrued expenses, or  $\$160,000 + (\$80,000 - \$72,000) - (\$250,000 - \$230,000) = \$148,000$ .
4. Cash received from the sale of equipment equals the original cost of the equipment sold minus the accumulated depreciation on the equipment sold plus the loss on the sale of the equipment. Since no equipment purchases were made during the year, the cost of the equipment sold is  $\$892,000 - \$900,000 = \$8,000$ . Depreciation on the equipment sold equals the beginning balance of accumulated depreciation plus the depreciation expense during the period minus the ending balance of accumulated depreciation ( $\$452,500 + \$11,500 - \$460,000 = \$4,000$ ). The loss is given as \$1,500. As a result,  $\$8,000 - \$4,000 - (1,500) = \$2,500$ , the amount of the cash proceeds.
5. Cash paid for income taxes equals income tax expense minus the increase in income tax payable, or  $\$43,000 - \$8,000 = \$35,000$ .

PTS: 1                      DIF: Challenging    OBJ: LO 2 | LO 3    TOP: AICPA FN-Measurement  
MSC: AACSB Analytic

16. *Statement of Financial Accounting Concepts No. 1* states that one of the objectives of financial reporting is to help “current and potential investors and creditors (and other users) in assessing the amounts, timing, and uncertainty of future cash flows such as dividends or interest payments.” Generally Accepted Accounting Principles (GAAP) require the use of the accrual basis of accounting.

Explain the difference between the accrual basis and the cash basis of accounting and why GAAP requires the accrual basis.

ANS:

*Statement of Financial Accounting Concepts No. 1* assumes that investors and creditors are interested in cash-flow information when evaluating investment opportunities. Accrual information helps investors estimate future net cash flows and the risks associated with these flows. The accrual basis is required under Generally Accepted Accounting Principles (GAAP).



Accrual basis accounting requires that an event that alters the economic status of a firm as represented in the firm's financial statements be recognized in the period in which the event occurs rather than when cash is exchanged. The accrual basis focuses on transactions and related events with cash consequences. Under the accrual basis, revenues are recorded when they are earned and expenses when they are incurred. Recognition of expenses or revenues in the accounting records under the accrual basis often occurs before or after the payment or receipt of cash.

The earnings figure resulting from application of the accrual basis reflects changes in financial position rather than immediate cash consequences. Accrual basis earnings more fully reflect the resource changes affecting the firm's net assets for a period than does the cash basis. Financial statement users find earnings information valuable because profits determine the long-run success of a company. Accrual measures, including financial statement ratios, have been found by researchers to be more accurate predictors of business failure. Companies with poor operating cash flows can survive for extended periods of time if creditors are willing to renegotiate and restructure debt. Companies that are growing rapidly may have negative cash flows because these companies may need to invest heavily in capital expenditures.

Adjusting journal entries are required under the accrual basis to ensure that revenues are recorded when earned and expenses are recorded when incurred. For example, an adjusting journal entry records interest expense before cash is paid since the passage of time results in the obligation to ultimately pay interest.

A cash basis accounting system reports only the receipt and disbursement of cash. Cash basis accounting requires few, if any adjusting entries. Cash information is far from useless, however.

In the short run, cash flow information is most important since it indicates whether a borrower will produce sufficient cash to pay its liabilities. Creditors are interested in a company's past and future ability to generate positive cash flows.

Research has found that cash flow information increases the overall information content of financial statements. Cash flow information also has been shown to supply risk assessment information beyond that provided by accrual basis earnings information. For example, a company with a strong working capital position but with large amounts of inventories, prepaid expenses, and receivables might be in a weak cash position.

The increasing complexity of financial accounting principles and the increasing complexity of financial statements as a result of applying these principles has increased the demand by financial statement users for cash flow information. Under current accrual basis accounting principles, managers also have flexibility to choose among several reporting choices thus allowing the manipulation of earnings under current GAAP.

The prevailing view currently is that neither cash flow nor accrual basis information alone is sufficient for a complete understanding of a company's performance. The relationships between revenues and cash inflows and between expenses and cash outflows can be understood only by studying both types of information.

PTS: 1                      DIF: Challenging    OBJ: LO 4  
TOP: AICPA FN-Measurement | AICPA FN-Reporting  
MSC: AACSB Communication | AACSB Reflective Thinking