

Chapter 2: The Basics of Record Keeping and Financial Statement Preparation: Balance Sheet

Student: _____

1. The T-account looks like the letter T, with a horizontal line bisected by a vertical line. Increases in shareholders' equity appear on the right side, and decreases in shareholders' equity appear on the left side of T-accounts.

True False

2. The T-account looks like the letter T, with a horizontal line bisected by a vertical line. Increases in liabilities appear on the right side, and decreases in liabilities appear on the left side of T-accounts.

True False

3. The T-account looks like the letter T, with a horizontal line bisected by a vertical line. Increases in assets appear on the left side, and decreases in assets appear on the right side of T-accounts.

True False

4. A T-account is a device or convention for organizing and accumulating the accounting entries of transactions that affect an individual account, such as cash, accounts receivable, bonds payable, or additional paid-in capital.

True False

5. The balance sheet equation maintains equality by reporting the financial statement effects of each event and transaction in a dual manner, or what are termed the dual effects of transactions.

True False

6. The balance sheet equation shows the equality of assets with liabilities plus shareholders' equity. This equation requires that an entity's assets exactly balance, or offset, an equal amount of financing provided by creditors and owners of the corporation.

True False

7. The balance sheet equation underlies the recording of transactions and events. It captures the financial statement effects of operating, investing, and financing transactions—three key activities of business firms.
True False
8. The balance sheet equation provides the analytical framework to understand the effects of transactions and events on the financial statements.
True False
9. The balance sheet groups individual accounts by type (asset, liability, or shareholders' equity) and lists these accounts with their balances as of the balance sheet date.
True False
10. The date of the balance sheet appears at the bottom of the balance sheet.
True False
11. The asset and liability categories group individual accounts by the expected timing of cash receipts (for assets) or cash payments (for liabilities).
True False
12. If the firm expects to collect or pay more than one year after the balance sheet date, the balance sheet classifies these as noncurrent assets and noncurrent liabilities, respectively.
True False
13. The balance sheet begins with a list of assets and then lists liabilities and shareholders' equity.
True False
14. Both U.S. GAAP and IFRS require firms to report balance sheet accounts for the prior year in addition to the current year.
True False
15. Under U.S. GAAP, assets and liabilities in the balance sheet appear in order of increasing closeness-to-cash.
True False

16. Common terminology describes items whose cash receipts or payments the firm expects will occur within one year as current assets or current liabilities, respectively.

True False

17. Under IFRS, assets and liabilities appear in the statement of financial position in order of decreasing closeness-to-cash.

True False

18. Total liabilities plus shareholders' equity shows the sources of all the firm's financing, and the assets show how the firm holds or has invested those funds.

True False

19. The beginning balance of the shareholders' equity account Retained Earnings plus net income from the income statement less dividends equals the ending balance of Retained Earnings.

True False

20. The equation that describes the relationship between the balance sheet and the income statement through the Retained Earnings account is as follows:

Retained Earnings (beginning) + Net Income - Dividends = Retained Earnings (ending)

True False

21. Retained earnings measures the cumulative excess of net income over dividends for the life of a firm. Cumulative means that retained earnings aggregates all undistributed earnings.

True False

22. Income statement accounts are temporary accounts and, as such, will have beginning and ending balances of zero.

True False

23. The closing process involves reducing to zero the balance in each income statement account by debiting the revenue accounts and crediting the expense accounts, and transferring to Retained Earnings the differences between total revenues and total expenses.

True False

24. A balance sheet account with a debit balance requires a closing entry that credits that account, because a credit closing entry will result in a zero ending balance in the account.

True False

25. A balance sheet account with a credit balance requires a closing entry that debits that account, because a debit closing entry will result in a zero ending balance in the account.

True False

26. The first step in the accounting record-keeping process is recording each transaction in a file or other record in the form of a journal entry.

True False

27. A balance sheet prepared according to U.S. GAAP lists assets from most liquid to least liquid, where liquid refers to the ease of converting the asset into cash.

True False

28. A balance sheet prepared according to U.S. GAAP lists liabilities starting with those that the firm will discharge soonest (the most current or closest to maturity liabilities) and ending with those that it will pay latest (the most noncurrent or distant to maturity liabilities).

True False

29. Firms that use International Financial Reporting Standards (IFRS) may, but need not, list their assets from least liquid to most liquid, with the same ordering used to list liabilities.

True False

30. Depreciation allocates the asset's cost to the periods of benefit in some systematic and rational way, and it attempts to track changes in the asset's fair value.

True False

31. Shareholders' equity is a residual interest or claim—that is, the owners (shareholders) of a firm have a claim on assets **not** required to meet the claims of creditors.

True False

32. The amounts that firms report as received from owners are equal to the amounts the firm received when it originally issued the shares of stock.

True False

33. The balance sheet amount of shareholders' equity does **not**, and is **not** intended to, provide the user of the financial reports with a measure of the market value of common equity.

True False

34. A potential investor can easily ascertain market value of common equity for a given publicly traded firm by looking up the most recent share price (as reported in various online services) and then multiplying this share price times the number of common shares outstanding, as reported on the balance sheet.

True False

35. The balance sheet provides all the information an analyst wants or needs about a firm's resources and the claims on those resources.

True False

36. Accounting does **not** normally recognize mutually unexecuted contracts as assets or liabilities.

True False

37. Both U.S. GAAP and IFRS require the disclosure, in the notes to the financial statements, of selected information about business segments.

True False

38. In computerized systems, posting occurs instantly and automatically after journalizing.

True False

39. Accounting is governed by the balance sheet equation, which shows the equality of

A. assets with liabilities plus shareholders' equity.

B. assets plus liabilities with shareholders' equity.

C. assets plus shareholders' equity with liabilities.

D. assets with liabilities minus shareholders' equity.

E. assets with shareholders' equity minus liabilities.

40. To maintain the balance sheet equality, it is necessary to report every event and transaction in a dual manner. If a transaction results in an increase in the left hand side of the balance sheet, dual transactions recording requires that which of the following must occur, to maintain the balance sheet equation?
- A. decrease another asset
 - B. increase a liability
 - C. increase shareholders equity
 - D. all of the above will maintain the balance sheet equation
 - E. none of the above
41. A detailed system of accounts allows the preparer of financial statements to decompose, or _____, each transaction to convey information about the effects of the transaction.
- A. mixup
 - B. disaggregate
 - C. aggregate
 - D. share
 - E. combine
42. To maintain balance sheet equality, it is necessary to report every event and transaction in a dual manner. If a transaction results in an increase in a Liability account, then which of the following must occur, to maintain the balance sheet equation?
- A. decrease another liability.
 - B. decrease shareholders' equity.
 - C. increase an asset.
 - D. all of the above will maintain the balance sheet equation
 - E. none of the above
43. T-accounts
- A. summarize the effects of transactions on specific accounts.
 - B. show all the accounts affected by a single event or transaction.
 - C. provide a record of transactions.
 - D. all of the above
 - E. none of the above
44. A T-account is a device or convention for organizing and accumulating the accounting entries of transactions that affect an individual account. Which of the following is/are true?
- A. Increases in assets appear on the left side, and decreases in assets appear on the right side of T-accounts.
 - B. Increases in liabilities appear on the right side, and decreases in liabilities appear on the left side of T-accounts.
 - C. Increases in shareholders' equity appear on the right side, and decreases in shareholders' equity appear on the left side of T-accounts
 - D. all of the above are true
 - E. none of the above are true

45. Brice Foods Group, a European food retailer that operates supermarkets in seven countries, engaged in the following transaction during 2013: purchased and received inventory costing €500 million on account from various suppliers. Indicate the effects of the transaction on the balance sheet equation. Brice Foods Group applies IFRS, and reports its results in millions of euros.

- A. Assets + €500 million; Liabilities + €500 million
- B. Assets + €500 million; Shareholders' Equity + €500 million
- C. Liabilities + €500 million; Shareholders' Equity + €500 million
- D. Liabilities + €500 million; Shareholders' Equity - €500 million
- E. Assets + €500 million; Shareholders' Equity - €500 million

46. Composite, Inc., a firm specializing in building materials, engaged in the following transaction during 2013: issued 2,000 shares of common stock for \$7,500 million in cash. Indicate the effects of the transaction on the balance sheet equation. (Composite Inc. applies U.S. GAAP financial reporting standards, and reports its results in millions of dollars.)

- A. Liabilities +\$7,500 million; Shareholders' Equity -\$7,500 million
- B. Liabilities +\$7,500 million; Shareholders' Equity +\$7,500 million
- C. Assets +\$7,500 million ; Liabilities +\$7,500 million
- D. Assets +\$7,500 million ; Shareholders' Equity +\$7,500 million
- E. Assets -\$7,500 million ; Liabilities -\$7,500 million

47. The equation that describes the relationship between the balance sheet and the income statement through the Retained Earnings account is as follows:

- A. Retained Earnings (beginning) - Net Income = Retained Earnings (ending)
- B. Retained Earnings (beginning) + Net Income + Dividends = Retained Earnings (ending)
- C. Retained Earnings (beginning) - Net Income - Dividends = Retained Earnings (ending)
- D. Retained Earnings (beginning) - Net Income + Dividends = Retained Earnings (ending)
- E. Retained Earnings (beginning) + Net Income - Dividends = Retained Earnings (ending)

48. Any single event or transaction will have which of the following effect(s) on the balance sheet?

- A. It increases an asset and increases either a liability or shareholders' equity.
- B. It decreases an asset and decreases either a liability or shareholders' equity.
- C. It increases one asset and decreases another asset.
- D. It increases one liability or shareholders' equity and decreases another liability or shareholders' equity.
- E. all of the above

49. Which of the following is/are true regarding the T-account?

- A. Actual practice does not use this form of the account, except perhaps for memoranda or preliminary analyses
- B. looks like the letter T, with a horizontal line bisected by a vertical line.
- C. satisfies the requirement of an account and is easy to use.
- D. all of the above
- E. none of the above

50. Which of the following is/are true regarding the T-account?

- A. the name or title of the account appears on the horizontal line.
- B. dates and other information can appear in T-accounts.
- C. one side of the space formed by the vertical line records increases in the item and the other side records decreases.
- D. all of the above
- E. none of the above

51. Which of the following is/are true regarding T-accounts?

- A. for each transaction, the amount entered on the left side of (or debited to) the accounts for each transaction equals the amount entered on the right side of (or credited to) the accounts.
- B. recording equal amounts of debits and credits for each transaction ensures that the balance sheet equation will always balance.
- C. one side of the space formed by the vertical line records increases in the item and the other side records decreases.
- D. all of the above
- E. none of the above

52. Horton Company reports the following:

Contributed Capital	\$ 200
Total Revenues	\$ 800
Total Liabilities	\$1,200
Beginning Retained Earnings	(\$ 100)
Total Expenses	\$ 500
Dividends	\$ 0

What are Total Assets?

- A. \$2,600
- B. \$1,600
- C. \$1,400
- D. \$1,000
- E. \$800

53. Conrad Company reports the following:

Total Assets	\$800
Contributed Capital	\$300
Total Revenues	\$600
Beginning Retained Earnings	\$200
Total Expenses	\$700
Dividends	\$100

What are Total liabilities?

- A. \$600
- B. \$500
- C. \$400
- D. \$300
- E. \$200

54. The accounting system uses a device called an account. An account

- A. is created each time a transaction takes place.
- B. accumulates the increases and decreases that occur during the period for a single item.
- C. is created only for income statement items.
- D. is created only for balance sheet items.
- E. is created only for statement of cash flows items.

55. Marianne Company reports the following:

Total Assets	\$1,200
Total Revenues	\$ 800
Total Liabilities	\$ 500
Beginning Retained Earnings	\$ 200
Total Expenses	\$ 400
Dividends	\$ 0

What is Contributed Capital?

- A. \$300
- B. \$200
- C. \$100
- D. \$0
- E. \$400

56. Journal entries

- A. show all the accounts affected by a single event or transaction.
- B. provide a record of transactions.
- C. have the characteristics presented in choices a and b.
- D. summarize the effects of transactions on specific accounts.
- E. none of the above

57. Temporary accounts are for recording

- A. revenues and expenses.
- B. assets.
- C. liabilities.
- D. shareholders' equity.
- E. assets, liabilities, and shareholders' equity.

58. Current assets are expected to be converted to cash within

- A. a week.
- B. a month.
- C. a quarter.
- D. a year.
- E. two years.

59. Noncurrent assets are expected to be converted to cash over

- A. a month.
- B. a quarter.
- C. a half of a year.
- D. a year.
- E. a period of time greater than a year.

60. Retained Earnings measures the cumulative excess of _____ for the life of a firm

- A. dividends over net income
- B. net income over dividends
- C. assets over liabilities
- D. liabilities over shareholders' equity
- E. shareholders' equity over liabilities

61. _____ accounts provide disaggregated information concerning the net amount of an asset, liability, or shareholders' equity item. Note that the use of such accounts does **not** affect the total of assets, liabilities, shareholders' equity, revenues, or expenses, but only the balances in various accounts that comprise the totals for these items.

- A. Reversing
- B. Temporary
- C. Contra
- D. Closing
- E. None of the above

62. Benezra S.A., a large Brazilian petrochemical company, reported a balance of R\$1,600 million in Accounts Receivable at the beginning of 2013 and R\$1,500 million at the end of 2013. Its income statement reported total Sales Revenue of R\$12,000 million for 2013. Assuming that Benezra makes all sales on account, compute the amount of cash collected from customers during 2013. Benezra applies Brazilian accounting standards, and reports its results in thousands of reals (R\$), the Brazilian currency. (In answering this question, assume that Benezra uses either U.S. GAAP or IFRS; for purposes of this problem, this choice will **not** matter.)

- A. 12,000
- B. 11,900
- C. 12,100
- D. 13,600
- E. 13,500

63. Skyway Company, a U.S. airplane manufacturer, reported a balance of \$8,100 million in Inventory at the beginning of 2013 and \$9,600 million at the end of 2013. Its income statement reported Cost of Products Sold of \$45,400 million for 2013. Compute the cost of inventory either purchased or manufactured during 2013. (Skyway Company applies U.S. GAAP, and reports its results in millions of U.S. dollars.)

- A. \$49,500 million
- B. \$39,900 million
- C. \$46,900 million
- D. \$39,900 million
- E. none of the above

64. C-Swiss, a Swedish firm specializing in communication networks, reported a balance in Inventories of SEK21,500 million at the beginning of 2013 and SEK22,500 million at the end of 2013. During 2013, C-Swiss reported SEK114,100 million in Cost of Sales. How much was C-Swiss' inventory purchases during 2013? [Assume that all of C-Swiss' inventory purchases are made on account and C-Swiss applies IFRS, as well as reports its results in millions of Swedish kronor (SEK).]

- A. SEK115,300 million
- B. SEK115,200 million
- C. SEK115,100 million
- D. SEK113,100 million
- E. none of the above

65. Ying Corporation, a Japanese construction firm, reported a balance in Income Taxes Payable of ¥3,700 million at the beginning of 2013 and ¥14,300 million at the end of 2013. Net income before income taxes for 2013 totaled ¥73,000 million. Assume that the firm is subject to an income tax rate of 43%. Compute the amount of cash payments made for income taxes during 2013. (Ying Corporation applies Japanese accounting standards, and reports its results in millions of yen (¥). In answering this question, assume that Ying Corporation uses either U.S. GAAP or IFRS; for purposes of this problem, this choice will **not** matter.)

- A. ¥10,600 million
- B. ¥17,090 million
- C. ¥20,790 million
- D. ¥73,000 million
- E. none of the above

66. Energy Corporation, a U.S. diversified power management company, reported a balance in Retained Earnings of \$2,800 million at the beginning of 2013 and \$3,300 million at the end of 2013. Based on Energy Corporation's financial reports for fiscal 2013, it reported dividends declared and paid of \$250 million for 2013. Compute the amount of net income for 2013. (Energy Corporation applies U.S. GAAP, and reports its results in millions of U.S. dollars.)

- A. -\$250 million
- B. \$250 million
- C. \$550 million
- D. \$750 million
- E. none of the above

67. On December 31, 2013, the Merchandise Inventories account of the Japanese electronics firm Flower Limited (Flower) had a balance of ¥408,700 million, based on Flower's financial reports for fiscal 2013. Assume that during 2014, Flower purchased merchandise inventories on account for ¥1,456,400 million. On December 31, 2014, it finds that merchandise inventory on hand is ¥412,400 million. Select the correct journal entries to account for all changes in the Inventories during 2014. (Flower applies Japanese accounting standards, and reports its results in millions of yen (¥). In answering this question, assume that Flower uses either U.S. GAAP or IFRS; for purposes of this problem, this choice will **not** matter.)

- A. Cost of Goods Sold ¥1,452,700 million
 Merchandise Inventories ¥1,452,700 million
- B. Merchandise Inventories ¥1,452,700 million
 Cost of Goods Sold ¥1,452,700 million
- C. Cost of Goods Sold ¥1,449,000 million
 Merchandise Inventories ¥1,449,000 million
- D. Merchandise Inventories ¥1,449,000 million
 Cost of Goods Sold ¥1,449,000 million
- E. none of the above

68. Klothing Company, a U.S. clothing designer, manufacturer, and retailer, reported a balance in prepaid insurance of \$90.7 million, based on its financial reports dated March 31, 2013, the end of its fiscal year. Assume that of this balance, \$24 million relates to an insurance policy with two remaining months of coverage. Select the correct journal entries that Klothing would make on April 30, 2013 (Assume that the firm closes its books monthly. Klothing applies U.S. GAAP, and reports its results in millions of U.S. dollars.)

- A. Insurance Expense \$ 24 million
 Prepaid Insurance \$24 million
- B. Prepaid Insurance \$24 million
 Insurance Expense \$24 million
- C. Insurance Expense \$12 million
 Prepaid Insurance \$12 million
- D. Prepaid Insurance \$12 million
 Insurance Expense \$12 million
- E. none of the above

69. ABC Group (ABC), headquartered in Switzerland, is one of the world's largest engineering companies. ABC applies U.S. GAAP, and reports its results in millions of U.S. dollars. Based on ABC's financial reports for fiscal 2013, at January 1, 2013, ABC reported a balance in its Prepaid Rent account of \$247 million; assume that this amount reflects its prepayments of rent on factory and office space for the next month. Assume also that on January 31, 2013, ABC paid \$3,200 million as the annual rent for the period from February 1, 2013, to January 31, 2014. ABC has a calendar year reporting period. Select the correct journal entries that ABC Group would make during January 2013 that affect the Prepaid Rent account.

A. Rent Expense \$3,200 million
 Cash \$3,200 million

Prepaid Rent \$247 million
 Rent Expense \$247 million

B. Rent Expense \$3,200 million
 Prepaid Rent \$3,200 million

Prepaid Rent \$247 million
 Cash \$247 million

C. Rent Expense \$3,200 million
 Prepaid Rent \$3,200 million

Prepaid Rent \$247 million
 Cash \$247 million

D. Rent Expense \$247 million
 Prepaid Rent \$247 million

Prepaid Rent \$3,200 million
 Cash \$3,200 million

E. none of the above

70. Tokyo Motor Company (Tokyo), a Japanese car manufacturer, reported Sales of Products of ¥22,670 billion for the year ended March 31, 2014. The Cost of Products Sold was ¥18,356 billion. Assume that Tokyo made all sales on credit. Select the correct journal entries that Tokyo made during the fiscal year ended March 31, 2014, related to these transactions. [Tokyo applies U.S. GAAP, and reports its results in millions of yen (¥).]

- A. Accounts Receivable ¥22,670 billion
Inventories ¥22,670 billion
Cost of Goods Sold ¥18,356 billion
 Revenues ¥18,356 billion
- B. Accounts Receivable ¥18,356 billion
Inventories ¥18,356 billion
Cost of Goods Sold ¥22,670 billion
 Revenues ¥22,670 billion
- C. Accounts Receivable ¥18,356 billion
Revenues ¥18,356 billion
Cost of Goods Sold ¥22,670 billion
 Inventories ¥22,670 billion
- D. Accounts Receivable ¥22,670 billion
Revenues ¥22,670 billion
Cost of Goods Sold ¥18,356 billion
Inventories ¥18,356 billion
- E. none of the above

71. Under U.S. GAAP, assets and liabilities in the balance sheet appear in order of

- A. decreasing closeness-to-cash.
- B. increasing closeness-to-cash.
- C. alphabetical order.
- D. numerical order.
- E. all of the above.

72. Under IFRS, assets and liabilities in the statement of financial position appear in order of

- A. decreasing closeness-to-cash.
- B. increasing closeness-to-cash.
- C. alphabetical order.
- D. numerical order.
- E. all of the above.

73. The first step in the accounting record-keeping process is:

- A. recording each transaction in a file or other record in the form of a journal entry.
- B. posting the amounts from the journal entries to individual balance sheet and income statement accounts in a general ledger.
- C. making adjusting journal entries to the accounts to correct errors and to reflect the financial statement impacts of items that occur because of usage or the passage of time.
- D. preparing the income statement for the period from amounts in the income statement accounts.
- E. preparing the balance sheet from amounts in the balance sheet accounts.

74. Assets are classified as current for reporting purposes when

- A. shares of common stock in a company's important supplier are acquired to ensure continued availability of raw materials.
- B. shares of common stock in another company are acquired to diversify operations.
- C. expenditures are made in developing new technologies or advertising products.
- D. they are reasonably expected to be turned into cash or to be sold or consumed during the normal operating cycle of the business.
- E. they are reasonably expected to be turned into cash or to be sold or consumed within the next three years.

75. Before preparing the balance sheet and income statement, an accountant would use what accounting record to first record the firm's transactions?

- A. the trial balance
- B. the adjusting entry
- C. the general ledger
- D. the subsidiary ledger
- E. the journal

76. Current liabilities

- A. are obligations that a firm expects to pay or discharge during the normal operating cycle of the firm, usually one year.
- B. include liabilities to merchandise suppliers, employees, and governmental units.
- C. include notes and bonds payable to the extent that they will require the use of current assets within the next year.
- D. include all of the above.
- E. None of the above answers is correct.

77. If a corporation issues 1,000 shares of \$1 par value common stock at \$5 per share, how should the transaction be accounted for?

- A. debit cash for \$5,000 and credit common stock for \$5,000
- B. debit cash for \$5,000 and credit common stock for \$1,000 and credit additional paid-in capital for \$4,000
- C. debit cash for \$5,000 and credit common stock for \$1,000 and credit retained earnings for \$4,000
- D. credit cash for \$5,000 and debit common stock for \$5,000
- E. debit common stock for \$1,000 and debit retained earnings for \$4,000 and credit cash for \$5,000

78. T-accounts are frequently used in textbooks, demonstration problems, and examinations to accumulate information about the effects of business transactions on individual balance sheet accounts and to prepare the balance sheet. Alternatively, to accomplish the same objectives, some instructors and students might prefer to use

- A. a computer spreadsheet program.
- B. P-accounts, only.
- C. a single-entry bookkeeping system.
- D. P&L-accounts.
- E. L-accounts, only.

79. Prepaid assets are valued on the balance sheet at

- A. cost paid to acquire the asset.
- B. acquisition cost less accumulated depreciation.
- C. cost less expired portion.
- D. replacement cost.
- E. present value of future cash flows.

80. On April 1, Year 1, Colonial Bookstore bought an insurance policy costing \$24,000 that would insure the retail building for two years against fire loss. What asset account and what amount are recorded on the balance sheet at December 31, Year 1?

- A. Prepaid Insurance, \$15,000
- B. Insurance Expense, \$15,000
- C. Prepaid Insurance, \$9,000
- D. Insurance Expense, \$9,000
- E. Prepaid Insurance, \$12,000

81. What (other than a transactions spreadsheet) serves the function of accumulating information about the effect of business transactions on each balance sheet and income statement account?

- A. Journals
- B. P&L-accounts
- C. T-accounts
- D. Subsidiary Ledgers
- E. Library

82. What does the word “marketable” imply as far as “marketable securities”?

- A. It implies that the securities should be classified as a temporary account.
- B. It implies that a firm owes money on the securities.
- C. It implies that the securities are considered to be goodwill.
- D. It implies that the firm can readily buy and sell the securities on an exchange.
- E. It implies that the firm has signed a formal written contract called an indenture.

83. Which of the following is **false** regarding a merchandising firm?

- A. A merchandising firm purchases inventory for resale.
- B. A merchandising firm does not change the physical form of the inventory.
- C. A merchandising firm performs no incremental work on the inventory.
- D. A merchandising firm adds nothing to the acquisition cost of the inventory after it is purchased.
- E. None of the above are false regarding a merchandising firm.

84. Which of the following is/are **not** true regarding a merchandising firm?

- A. Inventory appears on the merchandiser's balance sheet initially as an asset.
- B. Inventory for a merchandiser is measured at acquisition cost.
- C. When a sale takes place, the merchandising firm recognizes the cost of the inventory as an expense (cost of goods sold) on the income statement.
- D. When a sale takes place, the merchandising firm recognizes the inventory reduction on the statement of cash flows.
- E. All of the above are false regarding a merchandising firm.

85. For manufacturing firms, the balance sheet reports the costs of incomplete items as

- A. Raw Materials Inventory.
- B. Work-in-Process Inventory.
- C. Finished Goods Inventory.
- D. Cost of goods ready for sale.
- E. none of the above

86. Solve for the unknown item for each of the following independent situations.

	<u>CASE A</u>	<u>CASE B</u>	<u>CASE C</u>
Total assets	A	400	600
Contributed capital	100	150	C
Total revenues	400	300	400
Total liabilities	600	B	250
Beginning retained earnings	(50)	100	100
Total expenses	250	350	200
Dividends	0	50	0

87. The transactions listed below relate to Mountain Corporation. Indicate whether or not each transaction immediately gives rise to an **asset** or **liability** of Mountain Corporation under generally accepted accounting principles. If accounting recognizes an asset or a liability, give the account title and amount.

- a. Mountain Corporation signs a 3-year employment contract with Robert Lindsey, the chief financial officer, for \$375,000.
- b. Mountain Corporation sends a check for \$2,400 for two years' property insurance coverage beginning next month that would normally cost \$2,000 for a one-year policy.
- c. The firm paid \$250 for one-year subscriptions to ski magazines. None of the magazines have been received to date. In addition, it will cost the publisher \$100 to fulfill the subscription commitment.
- d. The firm acquires inventory with a list price of \$2,000, at a 3% discount for cash payment. The firm treats cash discounts as a reduction of acquisition cost.
- e. The firm agrees to purchase 25,000 units of inventory from a supplier over the next 3 years at an agreed cost of \$4/unit.

88. Culinary Delites, a European food retailer engaged in the following three transactions during 2013: (1) purchased and received inventory costing €978 million on account from various suppliers; (2) returned inventory costing €57 million because of damage that occurred during shipment; (3) paid the various suppliers the total amount due. Indicate the effects of each of these three transactions on the balance sheet equation. Culinary Delites applies IFRS and reports its results in millions of euros (€).

89. Supplies and More, a firm specializing in building materials, engaged in the following four transactions during 2014:

- (1) purchased and received inventory costing \$18,600 million, of which \$12,000 million was on account with the rest paid in cash;
- (2) purchased a machine for \$4,800 million with cash;
- (3) issued 2,000 shares of common stock for \$6,000 million in cash;
- (4) issued shares of common stock to its suppliers for the remaining amount due on purchases of inventory.

REQUIRED:

Indicate the effects of each of these four transactions on the balance sheet equation. Supplies and More applies U.S. GAAP financial reporting standards and reports its results in millions of U.S. dollars (\$).

90. Complete the shareholders' equity section for each of the following independent situations.

	<u>CASE A</u>	<u>CASE B</u>	<u>CASE C</u>
Common stock, 10,000 shares	A	C	E
Additional paid-in capital	25,000	D	30,000
Retained earnings	45,000	25,000	20,000
Total shareholders' equity	80,000	100,000	F
Par value per share	B	1.50	2.50

91. Indicate the effects of the following transactions on the balance sheet equation, using the format:

Transaction letter Assets = Liabilities + Shareholders' equity

- a. Issued 20,000 shares of \$0.10 par value common stock for \$100,000.
- b. Issued 5,000 shares of \$0.10 par value common stock in full payment for land worth \$25,000 to be used as a future building site.
- c. Acquired equipment costing \$7,500 for a cash payment of \$700 with the balance payable over the next five years.
- d. Paid \$1,000 for rent for the next two months.
- e. Completed a consulting job and invoiced the client for \$5,000, payable in 30 days.
- f. Ordered office supplies for the office, totaling \$225.
- g. Purchased a three-year fire insurance policy and pays in advance \$3,000.
- h. Received payment from the client for services rendered in (e) above.
- i. Received the office supplies. The invoice indicates payment is due within 10 days.
- j. Issued a check for the office supplies purchased in (i) above.

92. In European countries, terminology on financial statements sometimes differs from terminology commonly used in the United States. Match the European terms to commonly used United States counterparts.

- | <u>Common European Term</u> | <u>Common U.S. Term</u> |
|--|-----------------------------------|
| a. Tangible Fixed Asset | 1. Property, Plant, and Equipment |
| b. Financial Assets | 2. Common Stock |
| c. Trade Receivables | 3. Additional Paid-in Capital |
| d. Liquid Funds | 4. Investment in Securities |
| e. Subscribed Capital | 5. Retained Earnings |
| f. Capital Reserve | 6. Accounts Payable |
| g. Profit Reserves, Net Income Available for Distributions | 7. Accounts Receivable |
| h. Bonds | 8. Notes Payable to Banks |
| i. Due to Banks | 9. Bonds Payable |
| j. Trade Payables | 10. Cash |

93. The transactions listed below relate to the JB Corporation. Indicate whether or not each transaction immediately gives rise to an asset or liability of JB Corporation under generally accepted accounting principles. If accounting recognizes an asset or a liability, give the account title and amount.

- a. JB Corporation issues \$1 par value common stock for \$10,000,000, its market value.
- b. JB Corporation purchases a machine for \$20,000, freight of \$675, and installation costs of \$1,500.
- c. JB Corporation owes \$5,000 for utilities at the end of the year. The firm has 10 days before payment is due without paying a late fee.
- d. JB Corporation receives a 30-day, 10% loan of \$10,000 from a local bank.
- e. JB Corporation acquires property with an appraised value of \$2,000,000 for its stock.
- f. JB Corporation receives an order for merchandise totaling \$5,000 from a customer. The merchandise will be shipped next week.

94. Collette and Cohen incorporate as CC Designs, Inc. on January 1, Year 1. CC Designs creates custom wall finishes and sells painting products. The following transactions occur during January.

- a. Cohen contributes cash of \$75,000 and receives 15,000 shares of \$1 par value stock.
- b. Collette contributes \$35,000 cash, office furniture with a value of \$5,000, and computer equipment with a value of \$10,000 and receives 15,000 shares of \$1 par value stock. The furniture and equipment is expected to last 5 years and has no salvage value.
- c. On January 2, \$10,000 of painting products are purchased. CC paid \$8,000 cash with the remaining amount on account.
- d. During January, painting products are sold for \$8,000 cash. The cost of the products is \$2,000.
- e. Additional painting products with a value of \$5,000 are sold, with a cost of \$1,500, but the cash is not collected as of January 31st. It is expected that the \$5,000 will be collected in full by February 15th.
- f. Cohen is paid a salary of \$2,000.
- g. CC paid \$1,200 for January and February rent.

Required:

Prepare appropriate accrual basis journal entries.

95. Monmath Corp. started operations in March of Year 3. The following transactions occur during March.

- a. On March 1, Year 3, Monty contributes \$20,000 for 10,000 shares of \$1 par value stock.
- b. On March 1, Year 3, Monmath borrows \$50,000 on a note from the bank to finance the purchase of a building.
- c. Monmath buys \$15,000 of inventory on account (this is the gross price before any possible discounts).
- d. Monmath pays a \$12,000 account payable with cash.
- e. Monmath paid the annual rent of \$11,760.
- f. Monmath pays for one half of the inventory purchased in (c) above. There are no discounts given.
- g. Issued 300 shares of \$1 par value stock in settlement of \$300 accounts payable.
- h. Received \$400 from a customer for merchandise to be delivered on April 15, Year 3.

Required:

Prepare the journal entries for transactions a through h, assuming Monmath uses the accrual basis of accounting.

96. Assets are usually classified in one of following ways:

CA	-current assets
PPE	-property, plant, and equipment
IA	-intangible asset

Using the abbreviations above, indicate the appropriate classification of each of the following items.

- a. _____ merchandise inventory
- b. _____ goodwill
- c. _____ land
- d. _____ patent
- e. _____ work-in-process inventory
- f. _____ marketable equity securities
- g. _____ trademark
- h. _____ furniture and fixtures
- i. _____ cash
- j. _____ prepaid insurance

97. A friend of yours has prepared the following balance sheet for his bicycle shop but it has a problem. He thought his total assets did not reflect the assets available to the firm. He has asked you to take a look at this balance sheet and help him out.

Eric's Bike Shop, Inc.

Balance Sheet

As of December 31, Year 1

Assets

Current Assets:

Cash	\$15,000
Merchandise Inventory	30,000
Merchandise Sold, at cost	37,500
Prepaid Insurance	1,000
Advance from Customer	<u>(1,000)</u>
Total Current Assets	\$82,500

Property, Plant, and Equipment:

Equipment	8,000
Less Note Payable	<u>(5,000)</u>

Total Assets \$85,500

Liabilities and Shareholders' Equity

Current Liabilities:

Bike Sales	\$55,000
Accounts Payable	2,000
Accumulated Depreciation	700
Rent Payable	<u>1,000</u>
Total Current Liabilities	\$58,700

Shareholders' Equity:

Common Stock 1,000 shares at \$10 par value	\$10,000
Additional Paid-in Capital	7,500
Retained Earnings	<u>9,300</u>
Total Shareholders' Equity	<u>\$26,800</u>

Total Liabilities and Shareholders' Equity \$85,500

Required:

- Prepare a corrected balance sheet for Eric's Bike Shop, Inc.
- Draft a memo to Eric explaining the errors you corrected. Include your reasons.

98. Prepare journal entries for each of the following unrelated transactions. You may omit explanations for the journal entries.

- a. A firm issues 5,000 shares of \$2 par value common stock in exchange for \$20,000 cash.
- b. A firm acquires a building with \$30,000 cash and signs a 15-year note for \$60,000.
- c. A firm buys inventory for \$980 cash.
- d. A firm pays \$8,000 to its landlord for annual rent.
- e. A publisher sells \$3,000 in magazine subscriptions that will be filled over the next 12 months.

99. You've been asked to review the following balance sheet which has been prepared by a new staff member.

Calvin Springs Outfitters

Balance Sheet

As of December 31, Year 1

Assets

Current Assets:

Cash	\$ 7,500
Accounts Receivable	14,000
Merchandise Inventory	25,000
Land	<u>9,000</u>
Total Current Assets	\$ 46,500

Property, Plant, and Equipment:

Building	<u>\$125,000</u>
Total Assets	<u>\$180,500</u>

Liabilities and Shareholders' Equity

Current Liabilities:

Advance from Customer	\$ 500
Accounts Payable	21,000
Rent Payable	3,600
Utilities Payable	1,200
Salaries Payable	<u>1,800</u>
Total Current Liabilities	\$ 28,100

Shareholders' Equity:

Common Stock 2,000 shares at \$2.50 par value	\$ 5,000
Additional Paid-in Capital	85,000
Retained Earnings	<u>62,400</u>
Total Shareholders' Equity	<u>\$152,400</u>
Total Liabilities and Shareholders' Equity	<u>\$180,500</u>

a. Prepare the journal entries for the following transactions:

1. Merchandise purchased on account and costing \$5,000 was received but not recorded.
2. Payments by clients for previously billed invoices were found in the receptionist's desk drawer. The checks totaled \$2,100.
3. Written checks totaling \$2,700 for payment of accounts payable, were found in the treasurer's desk drawer. He was going to mail them out next Monday.
4. It was discovered that the company president had hired a new secretary for an annual salary of \$18,250.
5. Upon further investigation, you found that the company had paid but incorrectly recorded next year's fire insurance policy, totaling \$3,600. The payment was recorded as an expense.

b. Prepare a corrected balance sheet.

100. Express the following transactions of Forman's Store, Inc., in journal entry form. If an entry is not required, indicate the reason. You may omit explanations for the journal entries.

The store:

- (1) Receives \$35,000 from John Forman in return for 1,000 shares of the firm's \$35 par value common stock.
- (2) Gives a 60-day, 8% note to a bank and receives \$8,000 cash from the bank.
- (3) Rents a building and pays the annual rental of \$11,000 in advance.
- (4) Acquires display equipment costing \$7,000 and issues a check in full payment.
- (5) Acquires merchandise inventory costing \$22,000. The firm issues a check for \$12,000, with the remainder payable in 30 days.
- (6) Signs a contract with a nearby restaurant under which the restaurant agrees to purchase \$1,500 of groceries each week. The firm receives a check for the first two weeks' orders in advance.
- (7) Obtains a fire insurance policy providing \$50,000 coverage beginning next month. It pays the one-year premium of \$1,440.
- (8) Pays \$625 for advertisements that will appear in newspapers next month.
- (9) Places an order with suppliers for \$43,500 of merchandise to be delivered next month.

101. Assume that a firm uses the accrual basis of accounting. Indicate the amount of expense the firm recognizes during the month of November for each independent transaction.

- a. Rent of \$3,600 is paid on November 1 for the months November through January.
- b. Inventory costing \$2,500 is ordered on account. The invoice is received on November 25 and the goods are received on December 5.
- c. Insurance premium of \$900 is paid for a full year of coverage starting November 1.
- d. On December 3, an invoice for November utilities of \$325 is received.
- e. On November 1, supplies costing \$2,200 are purchased. At November 30, \$500 of supplies remained on hand.

102. Describe T-accounts and how they are used.

103. Explain the terms debit and credit. In your discussion, also present the debit and credit rules that are critical for maintaining T-accounts, as well as the equality of the balance sheet.

104. Why does every accounting transaction have two effects?

105. What is the relationship between a T-account and a journal entry?

106. Describe the balance sheet equation and the dual effects of transactions.

107. Describe a typical balance sheet.

108. What is the purpose of using contra accounts? What is the alternative to using them?

109. What distinguishes noncurrent assets from current assets?

110. Explain the difference between inventories for a retailer versus a manufacturer.

111. What is goodwill and how is it classified in terms of the accounting equation?

112. Explain the order of assets and liabilities in the balance sheet under U.S. GAAP and IFRS.

113. Explain how tenants record rent paid in advance for an office building and how a landlord or owner of the property rented records the receipt of the advance payment. Show journal entries as part of your answer.

114. Many firms, especially in their first years of operation and growth, face a variety of challenges obtaining funds to finance their growth.

Required:

Discuss how a small, young manufacturing firm that has a relatively unpredictable revenue stream might approach financing a new manufacturing line.

115. Several actions that an organization may take are not recognized or entered in the accounting records. While not entered into the formal accounting system, several such actions are exceedingly important to the organization.

Required:

Comment on the current and future implications that the hiring of a new president may have on the organization's accounting records.

Chapter 2: The Basics of Record Keeping and Financial Statement Preparation: Balance Sheet **Key**

1. The T-account looks like the letter T, with a horizontal line bisected by a vertical line. Increases in shareholders' equity appear on the right side, and decreases in shareholders' equity appear on the left side of T-accounts.

TRUE

2. The T-account looks like the letter T, with a horizontal line bisected by a vertical line. Increases in liabilities appear on the right side, and decreases in liabilities appear on the left side of T-accounts.

TRUE

3. The T-account looks like the letter T, with a horizontal line bisected by a vertical line. Increases in assets appear on the left side, and decreases in assets appear on the right side of T-accounts.

TRUE

4. A T-account is a device or convention for organizing and accumulating the accounting entries of transactions that affect an individual account, such as cash, accounts receivable, bonds payable, or additional paid-in capital.

TRUE

5. The balance sheet equation maintains equality by reporting the financial statement effects of each event and transaction in a dual manner, or what are termed the dual effects of transactions.

TRUE

6. The balance sheet equation shows the equality of assets with liabilities plus shareholders' equity. This equation requires that an entity's assets exactly balance, or offset, an equal amount of financing provided by creditors and owners of the corporation.

TRUE

7. The balance sheet equation underlies the recording of transactions and events. It captures the financial statement effects of operating, investing, and financing transactions—three key activities of business firms.

TRUE

8. The balance sheet equation provides the analytical framework to understand the effects of transactions and events on the financial statements.

TRUE

9. The balance sheet groups individual accounts by type (asset, liability, or shareholders' equity) and lists these accounts with their balances as of the balance sheet date.

TRUE

10. The date of the balance sheet appears at the bottom of the balance sheet.

FALSE

11. The asset and liability categories group individual accounts by the expected timing of cash receipts (for assets) or cash payments (for liabilities).

TRUE

12. If the firm expects to collect or pay more than one year after the balance sheet date, the balance sheet classifies these as noncurrent assets and noncurrent liabilities, respectively.

TRUE

13. The balance sheet begins with a list of assets and then lists liabilities and shareholders' equity.

TRUE

14. Both U.S. GAAP and IFRS require firms to report balance sheet accounts for the prior year in addition to the current year.

TRUE

15. Under U.S. GAAP, assets and liabilities in the balance sheet appear in order of increasing closeness-to-cash.

FALSE

16. Common terminology describes items whose cash receipts or payments the firm expects will occur within one year as current assets or current liabilities, respectively.

TRUE

17. Under IFRS, assets and liabilities appear in the statement of financial position in order of decreasing closeness-to-cash.

FALSE

18. Total liabilities plus shareholders' equity shows the sources of all the firm's financing, and the assets show how the firm holds or has invested those funds.

TRUE

19. The beginning balance of the shareholders' equity account Retained Earnings plus net income from the income statement less dividends equals the ending balance of Retained Earnings.

TRUE

20. The equation that describes the relationship between the balance sheet and the income statement through the Retained Earnings account is as follows:

Retained Earnings (beginning) + Net Income - Dividends = Retained Earnings (ending)

TRUE

21. Retained earnings measures the cumulative excess of net income over dividends for the life of a firm. Cumulative means that retained earnings aggregates all undistributed earnings.

TRUE

22. Income statement accounts are temporary accounts and, as such, will have beginning and ending balances of zero.

TRUE

23. The closing process involves reducing to zero the balance in each income statement account by debiting the revenue accounts and crediting the expense accounts, and transferring to Retained Earnings the differences between total revenues and total expenses.

TRUE

24. A balance sheet account with a debit balance requires a closing entry that credits that account, because a credit closing entry will result in a zero ending balance in the account.

FALSE

25. A balance sheet account with a credit balance requires a closing entry that debits that account, because a debit closing entry will result in a zero ending balance in the account.

FALSE

26. The first step in the accounting record-keeping process is recording each transaction in a file or other record in the form of a journal entry.

TRUE

27. A balance sheet prepared according to U.S. GAAP lists assets from most liquid to least liquid, where liquid refers to the ease of converting the asset into cash.

TRUE

28. A balance sheet prepared according to U.S. GAAP lists liabilities starting with those that the firm will discharge soonest (the most current or closest to maturity liabilities) and ending with those that it will pay latest (the most noncurrent or distant to maturity liabilities).

TRUE

29. Firms that use International Financial Reporting Standards (IFRS) may, but need not, list their assets from least liquid to most liquid, with the same ordering used to list liabilities.

TRUE

30. Depreciation allocates the asset's cost to the periods of benefit in some systematic and rational way, and it attempts to track changes in the asset's fair value.

FALSE

31. Shareholders' equity is a residual interest or claim—that is, the owners (shareholders) of a firm have a claim on assets **not** required to meet the claims of creditors.

TRUE

32. The amounts that firms report as received from owners are equal to the amounts the firm received when it originally issued the shares of stock.

TRUE

33. The balance sheet amount of shareholders' equity does **not**, and is **not** intended to, provide the user of the financial reports with a measure of the market value of common equity.

TRUE

34. A potential investor can easily ascertain market value of common equity for a given publicly traded firm by looking up the most recent share price (as reported in various online services) and then multiplying this share price times the number of common shares outstanding, as reported on the balance sheet.

TRUE

35. The balance sheet provides all the information an analyst wants or needs about a firm's resources and the claims on those resources.

FALSE

36. Accounting does **not** normally recognize mutually unexecuted contracts as assets or liabilities.

TRUE

37. Both U.S. GAAP and IFRS require the disclosure, in the notes to the financial statements, of selected information about business segments.

TRUE

38. In computerized systems, posting occurs instantly and automatically after journalizing.

TRUE

39. Accounting is governed by the balance sheet equation, which shows the equality of

- A.** assets with liabilities plus shareholders' equity.
- B. assets plus liabilities with shareholders' equity.
- C. assets plus shareholders' equity with liabilities.
- D. assets with liabilities minus shareholders' equity.
- E. assets with shareholders' equity minus liabilities.

40. To maintain the balance sheet equality, it is necessary to report every event and transaction in a dual manner. If a transaction results in an increase in the left hand side of the balance sheet, dual transactions recording requires that which of the following must occur, to maintain the balance sheet equation?

- A. decrease another asset
- B. increase a liability
- C. increase shareholders equity
- D.** all of the above will maintain the balance sheet equation
- E. none of the above

41. A detailed system of accounts allows the preparer of financial statements to decompose, or _____, each transaction to convey information about the effects of the transaction.

- A. mixup
- B.** disaggregate
- C. aggregate
- D. share
- E. combine

42. To maintain balance sheet equality, it is necessary to report every event and transaction in a dual manner. If a transaction results in an increase in a Liability account, then which of the following must occur, to maintain the balance sheet equation?

- A. decrease another liability.
- B. decrease shareholders' equity.
- C. increase an asset.
- D.** all of the above will maintain the balance sheet equation
- E. none of the above

43. T-accounts

- A.** summarize the effects of transactions on specific accounts.
- B. show all the accounts affected by a single event or transaction.
- C. provide a record of transactions.
- D. all of the above
- E. none of the above

44. A T-account is a device or convention for organizing and accumulating the accounting entries of transactions that affect an individual account. Which of the following is/are true?

- A. Increases in assets appear on the left side, and decreases in assets appear on the right side of T-accounts.
- B. Increases in liabilities appear on the right side, and decreases in liabilities appear on the left side of T-accounts.
- C. Increases in shareholders' equity appear on the right side, and decreases in shareholders' equity appear on the left side of T-accounts
- D.** all of the above are true
- E. none of the above are true

45. Brice Foods Group, a European food retailer that operates supermarkets in seven countries, engaged in the following transaction during 2013: purchased and received inventory costing €500 million on account from various suppliers. Indicate the effects of the transaction on the balance sheet equation. Brice Foods Group applies IFRS, and reports its results in millions of euros.

- A.** Assets + €500 million; Liabilities + €500 million
- B. Assets + €500 million; Shareholders' Equity + €500 million
- C. Liabilities + €500 million; Shareholders' Equity + €500 million
- D. Liabilities + €500 million; Shareholders' Equity - €500 million
- E. Assets + €500 million; Shareholders' Equity - €500 million

46. Composite, Inc., a firm specializing in building materials, engaged in the following transaction during 2013: issued 2,000 shares of common stock for \$7,500 million in cash. Indicate the effects of the transaction on the balance sheet equation. (Composite Inc. applies U.S. GAAP financial reporting standards, and reports its results in millions of dollars.)

- A. Liabilities +\$7,500 million; Shareholders' Equity -\$7,500 million
- B. Liabilities +\$7,500 million; Shareholders' Equity +\$7,500 million
- C. Assets +\$7,500 million ; Liabilities +\$7,500 million
- D.** Assets +\$7,500 million ; Shareholders' Equity +\$7,500 million
- E. Assets -\$7,500 million ; Liabilities -\$7,500 million

47. The equation that describes the relationship between the balance sheet and the income statement through the Retained Earnings account is as follows:

- A. Retained Earnings (beginning) - Net Income = Retained Earnings (ending)
- B. Retained Earnings (beginning) + Net Income + Dividends = Retained Earnings (ending)
- C. Retained Earnings (beginning) - Net Income - Dividends = Retained Earnings (ending)
- D. Retained Earnings (beginning) - Net Income + Dividends = Retained Earnings (ending)
- E.** Retained Earnings (beginning) + Net Income - Dividends = Retained Earnings (ending)

48. Any single event or transaction will have which of the following effect(s) on the balance sheet?

- A. It increases an asset and increases either a liability or shareholders' equity.
- B. It decreases an asset and decreases either a liability or shareholders' equity.
- C. It increases one asset and decreases another asset.
- D. It increases one liability or shareholders' equity and decreases another liability or shareholders' equity.
- E.** all of the above

49. Which of the following is/are true regarding the T-account?

- A. Actual practice does not use this form of the account, except perhaps for memoranda or preliminary analyses
- B. looks like the letter T, with a horizontal line bisected by a vertical line.
- C. satisfies the requirement of an account and is easy to use.
- D.** all of the above
- E. none of the above

50. Which of the following is/are true regarding the T-account?

- A. the name or title of the account appears on the horizontal line.
- B. dates and other information can appear in T-accounts.
- C. one side of the space formed by the vertical line records increases in the item and the other side records decreases.
- D.** all of the above
- E. none of the above

51. Which of the following is/are true regarding T-accounts?

- A. for each transaction, the amount entered on the left side of (or debited to) the accounts for each transaction equals the amount entered on the right side of (or credited to) the accounts.
- B. recording equal amounts of debits and credits for each transaction ensures that the balance sheet equation will always balance.
- C. one side of the space formed by the vertical line records increases in the item and the other side records decreases.
- D.** all of the above
- E. none of the above

52. Horton Company reports the following:

Contributed Capital	\$ 200
Total Revenues	\$ 800
Total Liabilities	\$1,200
Beginning Retained Earnings	(\$ 100)
Total Expenses	\$ 500
Dividends	\$ 0

What are Total Assets?

- A. \$2,600
- B.** \$1,600
- C. \$1,400
- D. \$1,000
- E. \$800

53. Conrad Company reports the following:

Total Assets	\$800
Contributed Capital	\$300
Total Revenues	\$600
Beginning Retained Earnings	\$200
Total Expenses	\$700
Dividends	\$100

What are Total liabilities?

- A. \$600
- B. \$500**
- C. \$400
- D. \$300
- E. \$200

54. The accounting system uses a device called an account. An account

- A. is created each time a transaction takes place.
- B. accumulates the increases and decreases that occur during the period for a single item.**
- C. is created only for income statement items.
- D. is created only for balance sheet items.
- E. is created only for statement of cash flows items.

55. Marianne Company reports the following:

Total Assets	\$1,200
Total Revenues	\$ 800
Total Liabilities	\$ 500
Beginning Retained Earnings	\$ 200
Total Expenses	\$ 400
Dividends	\$ 0

What is Contributed Capital?

- A. \$300
- B. \$200
- C. \$100**
- D. \$0
- E. \$400

56. Journal entries

- A. show all the accounts affected by a single event or transaction.
- B. provide a record of transactions.
- C. have the characteristics presented in choices a and b.**
- D. summarize the effects of transactions on specific accounts.
- E. none of the above

57. Temporary accounts are for recording

- A. revenues and expenses.**
- B. assets.
- C. liabilities.
- D. shareholders' equity.
- E. assets, liabilities, and shareholders' equity.

58. Current assets are expected to be converted to cash within

- A. a week.
- B. a month.
- C. a quarter.
- D.** a year.
- E. two years.

59. Noncurrent assets are expected to be converted to cash over

- A. a month.
- B. a quarter.
- C. a half of a year.
- D. a year.
- E.** a period of time greater than a year.

60. Retained Earnings measures the cumulative excess of _____ for the life of a firm

- A. dividends over net income
- B.** net income over dividends
- C. assets over liabilities
- D. liabilities over shareholders' equity
- E. shareholders' equity over liabilities

61. _____ accounts provide disaggregated information concerning the net amount of an asset, liability, or shareholders' equity item. Note that the use of such accounts does **not** affect the total of assets, liabilities, shareholders' equity, revenues, or expenses, but only the balances in various accounts that comprise the totals for these items.

- A. Reversing
- B. Temporary
- C.** Contra
- D. Closing
- E. None of the above

62. Benezra S.A., a large Brazilian petrochemical company, reported a balance of R\$1,600 million in Accounts Receivable at the beginning of 2013 and R\$1,500 million at the end of 2013. Its income statement reported total Sales Revenue of R\$12,000 million for 2013. Assuming that Benezra makes all sales on account, compute the amount of cash collected from customers during 2013. Benezra applies Brazilian accounting standards, and reports its results in thousands of reals (R\$), the Brazilian currency. (In answering this question, assume that Benezra uses either U.S. GAAP or IFRS; for purposes of this problem, this choice will **not** matter.)

- A. 12,000
- B. 11,900
- C.** 12,100
- D. 13,600
- E. 13,500

63. Skyway Company, a U.S. airplane manufacturer, reported a balance of \$8,100 million in Inventory at the beginning of 2013 and \$9,600 million at the end of 2013. Its income statement reported Cost of Products Sold of \$45,400 million for 2013. Compute the cost of inventory either purchased or manufactured during 2013. (Skyway Company applies U.S. GAAP, and reports its results in millions of U.S. dollars.)

- A. \$49,500 million
- B. \$39,900 million
- C. \$46,900 million**
- D. \$39,900 million
- E. none of the above

64. C-Swiss, a Swedish firm specializing in communication networks, reported a balance in Inventories of SEK21,500 million at the beginning of 2013 and SEK22,500 million at the end of 2013. During 2013, C-Swiss reported SEK114,100 million in Cost of Sales. How much was C-Swiss' inventory purchases during 2013? [Assume that all of C-Swiss' inventory purchases are made on account and C-Swiss applies IFRS, as well as reports its results in millions of Swedish kronor (SEK).]

- A. SEK115,300 million
- B. SEK115,200 million
- C. SEK115,100 million**
- D. SEK113,100 million
- E. none of the above

65. Ying Corporation, a Japanese construction firm, reported a balance in Income Taxes Payable of ¥3,700 million at the beginning of 2013 and ¥14,300 million at the end of 2013. Net income before income taxes for 2013 totaled ¥73,000 million. Assume that the firm is subject to an income tax rate of 43%. Compute the amount of cash payments made for income taxes during 2013. (Ying Corporation applies Japanese accounting standards, and reports its results in millions of yen (¥). In answering this question, assume that Ying Corporation uses either U.S. GAAP or IFRS; for purposes of this problem, this choice will **not** matter.)

- A. ¥10,600 million
- B. ¥17,090 million
- C. ¥20,790 million**
- D. ¥73,000 million
- E. none of the above

66. Energy Corporation, a U.S. diversified power management company, reported a balance in Retained Earnings of \$2,800 million at the beginning of 2013 and \$3,300 million at the end of 2013. Based on Energy Corporation's financial reports for fiscal 2013, it reported dividends declared and paid of \$250 million for 2013. Compute the amount of net income for 2013. (Energy Corporation applies U.S. GAAP, and reports its results in millions of U.S. dollars.)

- A. -\$250 million
- B. \$250 million
- C. \$550 million
- D. \$750 million**
- E. none of the above

67. On December 31, 2013, the Merchandise Inventories account of the Japanese electronics firm Flower Limited (Flower) had a balance of ¥408,700 million, based on Flower's financial reports for fiscal 2013. Assume that during 2014, Flower purchased merchandise inventories on account for ¥1,456,400 million. On December 31, 2014, it finds that merchandise inventory on hand is ¥412,400 million. Select the correct journal entries to account for all changes in the Inventories during 2014. (Flower applies Japanese accounting standards, and reports its results in millions of yen (¥). In answering this question, assume that Flower uses either U.S. GAAP or IFRS; for purposes of this problem, this choice will **not** matter.)

- A.** Cost of Goods Sold ¥1,452,700 million
 Merchandise Inventories ¥1,452,700 million
- B. Merchandise Inventories ¥1,452,700 million
 Cost of Goods Sold ¥1,452,700 million
- C. Cost of Goods Sold ¥1,449,000 million
 Merchandise Inventories ¥1,449,000 million
- D. Merchandise Inventories ¥1,449,000 million
 Cost of Goods Sold ¥1,449,000 million
- E. none of the above

68. Klothing Company, a U.S. clothing designer, manufacturer, and retailer, reported a balance in prepaid insurance of \$90.7 million, based on its financial reports dated March 31, 2013, the end of its fiscal year. Assume that of this balance, \$24 million relates to an insurance policy with two remaining months of coverage. Select the correct journal entries that Klothing would make on April 30, 2013 (Assume that the firm closes its books monthly. Klothing applies U.S. GAAP, and reports its results in millions of U.S. dollars.)

- A. Insurance Expense \$ 24 million
 Prepaid Insurance \$24 million
- B. Prepaid Insurance \$24 million
 Insurance Expense \$24 million
- C.** Insurance Expense \$12 million
 Prepaid Insurance \$12 million
- D. Prepaid Insurance \$12 million
 Insurance Expense \$12 million
- E. none of the above

69. ABC Group (ABC), headquartered in Switzerland, is one of the world's largest engineering companies. ABC applies U.S. GAAP, and reports its results in millions of U.S. dollars. Based on ABC's financial reports for fiscal 2013, at January 1, 2013, ABC reported a balance in its Prepaid Rent account of \$247 million; assume that this amount reflects its prepayments of rent on factory and office space for the next month. Assume also that on January 31, 2013, ABC paid \$3,200 million as the annual rent for the period from February 1, 2013, to January 31, 2014. ABC has a calendar year reporting period. Select the correct journal entries that ABC Group would make during January 2013 that affect the Prepaid Rent account.

A. Rent Expense \$3,200 million
 Cash \$3,200 million

Prepaid Rent \$247 million
 Rent Expense \$247 million

B. Rent Expense \$3,200 million
 Prepaid Rent \$3,200 million

Prepaid Rent \$247 million
 Cash \$247 million

C. Rent Expense \$3,200 million
 Prepaid Rent \$3,200 million

Prepaid Rent \$247 million
 Cash \$247 million

D. Rent Expense \$247 million
 Prepaid Rent \$247 million

Prepaid Rent \$3,200 million
 Cash \$3,200 million

E. none of the above

70. Tokyo Motor Company (Tokyo), a Japanese car manufacturer, reported Sales of Products of ¥22,670 billion for the year ended March 31, 2014. The Cost of Products Sold was ¥18,356 billion. Assume that Tokyo made all sales on credit. Select the correct journal entries that Tokyo made during the fiscal year ended March 31, 2014, related to these transactions. [Tokyo applies U.S. GAAP, and reports its results in millions of yen (¥).]

A. Accounts Receivable ¥22,670 billion
Inventories ¥22,670 billion
Cost of Goods Sold ¥18,356 billion
 Revenues ¥18,356 billion

B. Accounts Receivable ¥18,356 billion
Inventories ¥18,356 billion
Cost of Goods Sold ¥22,670 billion
 Revenues ¥22,670 billion

C. Accounts Receivable ¥18,356 billion
Revenues ¥18,356 billion
Cost of Goods Sold ¥22,670 billion
 Inventories ¥22,670 billion

D. Accounts Receivable ¥22,670 billion
Revenues ¥22,670 billion
Cost of Goods Sold ¥18,356 billion
Inventories ¥18,356 billion

E. none of the above

71. Under U.S. GAAP, assets and liabilities in the balance sheet appear in order of

- A.** decreasing closeness-to-cash.
- B. increasing closeness-to-cash.
- C. alphabetical order.
- D. numerical order.
- E. all of the above.

72. Under IFRS, assets and liabilities in the statement of financial position appear in order of

- A. decreasing closeness-to-cash.
- B.** increasing closeness-to-cash.
- C. alphabetical order.
- D. numerical order.
- E. all of the above.

73. The first step in the accounting record-keeping process is:

- A.** recording each transaction in a file or other record in the form of a journal entry.
- B. posting the amounts from the journal entries to individual balance sheet and income statement accounts in a general ledger.
- C. making adjusting journal entries to the accounts to correct errors and to reflect the financial statement impacts of items that occur because of usage or the passage of time.
- D. preparing the income statement for the period from amounts in the income statement accounts.
- E. preparing the balance sheet from amounts in the balance sheet accounts.

74. Assets are classified as current for reporting purposes when

- A. shares of common stock in a company's important supplier are acquired to ensure continued availability of raw materials.
- B. shares of common stock in another company are acquired to diversify operations.
- C. expenditures are made in developing new technologies or advertising products.
- D.** they are reasonably expected to be turned into cash or to be sold or consumed during the normal operating cycle of the business.
- E. they are reasonably expected to be turned into cash or to be sold or consumed within the next three years.

75. Before preparing the balance sheet and income statement, an accountant would use what accounting record to first record the firm's transactions?

- A. the trial balance
- B. the adjusting entry
- C. the general ledger
- D. the subsidiary ledger
- E.** the journal

76. Current liabilities

- A. are obligations that a firm expects to pay or discharge during the normal operating cycle of the firm, usually one year.
- B. include liabilities to merchandise suppliers, employees, and governmental units.
- C. include notes and bonds payable to the extent that they will require the use of current assets within the next year.
- D.** include all of the above.
- E. None of the above answers is correct.

77. If a corporation issues 1,000 shares of \$1 par value common stock at \$5 per share, how should the transaction be accounted for?

- A. debit cash for \$5,000 and credit common stock for \$5,000
- B.** debit cash for \$5,000 and credit common stock for \$1,000 and credit additional paid-in capital for \$4,000
- C. debit cash for \$5,000 and credit common stock for \$1,000 and credit retained earnings for \$4,000
- D. credit cash for \$5,000 and debit common stock for \$5,000
- E. debit common stock for \$1,000 and debit retained earnings for \$4,000 and credit cash for \$5,000

78. T-accounts are frequently used in textbooks, demonstration problems, and examinations to accumulate information about the effects of business transactions on individual balance sheet accounts and to prepare the balance sheet. Alternatively, to accomplish the same objectives, some instructors and students might prefer to use

- A.** a computer spreadsheet program.
- B. P-accounts, only.
- C. a single-entry bookkeeping system.
- D. P&L-accounts.
- E. L-accounts, only.

79. Prepaid assets are valued on the balance sheet at

- A. cost paid to acquire the asset.
- B. acquisition cost less accumulated depreciation.
- C.** cost less expired portion.
- D. replacement cost.
- E. present value of future cash flows.

80. On April 1, Year 1, Colonial Bookstore bought an insurance policy costing \$24,000 that would insure the retail building for two years against fire loss. What asset account and what amount are recorded on the balance sheet at December 31, Year 1?

- A.** Prepaid Insurance, \$15,000
- B. Insurance Expense, \$15,000
- C. Prepaid Insurance, \$9,000
- D. Insurance Expense, \$9,000
- E. Prepaid Insurance, \$12,000

81. What (other than a transactions spreadsheet) serves the function of accumulating information about the effect of business transactions on each balance sheet and income statement account?

- A. Journals
- B. P&L-accounts
- C.** T-accounts
- D. Subsidiary Ledgers
- E. Library

82. What does the word “marketable” imply as far as “marketable securities”?

- A. It implies that the securities should be classified as a temporary account.
- B. It implies that a firm owes money on the securities.
- C. It implies that the securities are considered to be goodwill.
- D.** It implies that the firm can readily buy and sell the securities on an exchange.
- E. It implies that the firm has signed a formal written contract called an indenture.

83. Which of the following is **false** regarding a merchandising firm?

- A. A merchandising firm purchases inventory for resale.
- B. A merchandising firm does not change the physical form of the inventory.
- C. A merchandising firm performs no incremental work on the inventory.
- D. A merchandising firm adds nothing to the acquisition cost of the inventory after it is purchased.
- E.** None of the above are false regarding a merchandising firm.

84. Which of the following is/are **not** true regarding a merchandising firm?

- A. Inventory appears on the merchandiser's balance sheet initially as an asset.
- B. Inventory for a merchandiser is measured at acquisition cost.
- C. When a sale takes place, the merchandising firm recognizes the cost of the inventory as an expense (cost of goods sold) on the income statement.
- D.** When a sale takes place, the merchandising firm recognizes the inventory reduction on the statement of cash flows.
- E. All of the above are false regarding a merchandising firm.

85. For manufacturing firms, the balance sheet reports the costs of incomplete items as

- A. Raw Materials Inventory.
- B.** Work-in-Process Inventory.
- C. Finished Goods Inventory.
- D. Cost of goods ready for sale.
- E. none of the above

86. Solve for the unknown item for each of the following independent situations.

	<u>CASE A</u>	<u>CASE B</u>	<u>CASE C</u>
Total assets	A	400	600
Contributed capital	100	150	C
Total revenues	400	300	400
Total liabilities	600	B	250
Beginning retained earnings	(50)	100	100
Total expenses	250	350	200
Dividends	0	50	0

- A. \$800
- B. \$250
- C. \$50

87. The transactions listed below relate to Mountain Corporation. Indicate whether or not each transaction immediately gives rise to an **asset** or **liability** of Mountain Corporation under generally accepted accounting principles. If accounting recognizes an asset or a liability, give the account title and amount.

- a. Mountain Corporation signs a 3-year employment contract with Robert Lindsey, the chief financial officer, for \$375,000.
- b. Mountain Corporation sends a check for \$2,400 for two years' property insurance coverage beginning next month that would normally cost \$2,000 for a one-year policy.
- c. The firm paid \$250 for one-year subscriptions to ski magazines. None of the magazines have been received to date. In addition, it will cost the publisher \$100 to fulfill the subscription commitment.
- d. The firm acquires inventory with a list price of \$2,000, at a 3% discount for cash payment. The firm treats cash discounts as a reduction of acquisition cost.
- e. The firm agrees to purchase 25,000 units of inventory from a supplier over the next 3 years at an agreed cost of \$4/unit.

- a. No effect
- b. Prepaid Insurance, \$2,400
- c. Prepaid Subscriptions, \$250
- d. Inventory, \$1,940
- e. No effect

88. Culinary Delites, a European food retailer engaged in the following three transactions during 2013: (1) purchased and received inventory costing €978 million on account from various suppliers; (2) returned inventory costing €57 million because of damage that occurred during shipment; (3) paid the various suppliers the total amount due. Indicate the effects of each of these three transactions on the balance sheet equation. Culinary Delites applies IFRS and reports its results in millions of euros (€).

Transaction	Assets	=	Shareholders' Liabilities +	Equity
(1)	+ €978		+ €978	
(2)	- € 57		- € 57	
(3)	- €921		- €921	

89. Supplies and More, a firm specializing in building materials, engaged in the following four transactions during 2014:

- (1) purchased and received inventory costing \$18,600 million, of which \$12,000 million was on account with the rest paid in cash;
- (2) purchased a machine for \$4,800 million with cash;
- (3) issued 2,000 shares of common stock for \$6,000 million in cash;
- (4) issued shares of common stock to its suppliers for the remaining amount due on purchases of inventory.

REQUIRED:

Indicate the effects of each of these four transactions on the balance sheet equation. Supplies and More applies U.S. GAAP financial reporting standards and reports its results in millions of U.S. dollars (\$).

Transaction	Assets	Shareholders'	
		=	Liabilities + Equity
(1)	+ \$18,600	=	+\$12,000
	-\$6,600		
(2)	+\$4,800		
	-\$4,800		
(3)	+\$6,000		+\$6,000
(4)		-\$12,000	+\$12,000

90. Complete the shareholders' equity section for each of the following independent situations.

	<u>CASE A</u>	<u>CASE B</u>	<u>CASE C</u>
Common stock, 10,000 shares	A	C	E
Additional paid-in capital	25,000	D	30,000
Retained earnings	45,000	25,000	20,000
Total shareholders' equity	80,000	100,000	F
Par value per share	B	1.50	2.50

- A.\$10,000
- B.\$1.00
- C.\$15,000
- D.\$60,000
- E.\$25,000
- F.\$75,000

91. Indicate the effects of the following transactions on the balance sheet equation, using the format:

Transaction letter Assets = Liabilities + Shareholders' equity

- a. Issued 20,000 shares of \$0.10 par value common stock for \$100,000.
- b. Issued 5,000 shares of \$0.10 par value common stock in full payment for land worth \$25,000 to be used as a future building site.
- c. Acquired equipment costing \$7,500 for a cash payment of \$700 with the balance payable over the next five years.
- d. Paid \$1,000 for rent for the next two months.
- e. Completed a consulting job and invoiced the client for \$5,000, payable in 30 days.
- f. Ordered office supplies for the office, totaling \$225.
- g. Purchased a three-year fire insurance policy and pays in advance \$3,000.
- h. Received payment from the client for services rendered in (e) above.
- i. Received the office supplies. The invoice indicates payment is due within 10 days.
- j. Issued a check for the office supplies purchased in (i) above.

<u>Transaction letter</u>	<u>Assets</u>	=	<u>Liabilities</u>	+	<u>Shareholders' Equity</u>
a.	+100,000		+100,000		
b.	+ 25,000		+ 25,000		
c.	+ 6,800	+6,800			
d.		0			
e.	+ 5,000	+ 5,000			
f.	No entry				
g.	0				
h.	0				
i.	+ 225	+ 225			
j.	- 225	- 225			

92. In European countries, terminology on financial statements sometimes differs from terminology commonly used in the United States. Match the European terms to commonly used United States counterparts.

<u>Common European Term</u>	<u>Common U.S. Term</u>
a. Tangible Fixed Asset	1. Property, Plant, and Equipment
b. Financial Assets	2. Common Stock
c. Trade Receivables	3. Additional Paid-in Capital
d. Liquid Funds	4. Investment in Securities
e. Subscribed Capital	5. Retained Earnings
f. Capital Reserve	6. Accounts Payable
g. Profit Reserves, Net Income Available for Distributions	7. Accounts Receivable
h. Bonds	8. Notes Payable to Banks
i. Due to Banks	9. Bonds Payable
j. Trade Payables	10. Cash

- a.1
- b.4
- c.7
- d.10
- e.2
- f.3
- g.5
- h.9
- i.8
- j.6

93. The transactions listed below relate to the JB Corporation. Indicate whether or not each transaction immediately gives rise to an asset or liability of JB Corporation under generally accepted accounting principles. If accounting recognizes an asset or a liability, give the account title and amount.

- a. JB Corporation issues \$1 par value common stock for \$10,000,000, its market value.
- b. JB Corporation purchases a machine for \$20,000, freight of \$675, and installation costs of \$1,500.
- c. JB Corporation owes \$5,000 for utilities at the end of the year. The firm has 10 days before payment is due without paying a late fee.
- d. JB Corporation receives a 30-day, 10% loan of \$10,000 from a local bank.
- e. JB Corporation acquires property with an appraised value of \$2,000,000 for its stock.
- f. JB Corporation receives an order for merchandise totaling \$5,000 from a customer. The merchandise will be shipped next week.

- a. Asset Cash, \$10,000,000
- b. Asset Machinery, \$22,175 Asset Cash, (\$22,175)
- c. Liability Accounts Payable, \$5,000
- d. Asset Cash, \$10,000 Liability Note Payable, \$10,000
- e. Asset Property, \$2,000,000
- f. No effect

94. Collette and Cohen incorporate as CC Designs, Inc. on January 1, Year 1. CC Designs creates custom wall finishes and sells painting products. The following transactions occur during January.

- a. Cohen contributes cash of \$75,000 and receives 15,000 shares of \$1 par value stock.
- b. Collette contributes \$35,000 cash, office furniture with a value of \$5,000, and computer equipment with a value of \$10,000 and receives 15,000 shares of \$1 par value stock. The furniture and equipment is expected to last 5 years and has no salvage value.
- c. On January 2, \$10,000 of painting products are purchased. CC paid \$8,000 cash with the remaining amount on account.
- d. During January, painting products are sold for \$8,000 cash. The cost of the products is \$2,000.
- e. Additional painting products with a value of \$5,000 are sold, with a cost of \$1,500, but the cash is not collected as of January 31st. It is expected that the \$5,000 will be collected in full by February 15th.
- f. Cohen is paid a salary of \$2,000.
- g. CC paid \$1,200 for January and February rent.

Required:

Prepare appropriate accrual basis journal entries.

- a. Cash 75,000
 Common Stock 15,000
 Additional Paid-in Capital 60,000
- b. Cash 35,000
 Furniture 5,000
 Computer Equipment 10,000
 Common Stock 15,000
 Additional Paid-in Capital 35,000
- c. Inventory 10,000
 Cash 8,000
 Accounts Payable 2,000
- d. Cash 8,000
 Sales Revenue 8,000
 Cost of Goods Sold 2,000
 Inventory 2,000
- e. Accounts Receivable 5,000
 Sales Revenue 5,000
 Cost of Goods Sold 1,500
 Inventory 1,500
- f. Salary Expense 2,000
 Cash 2,000
- g. Rent Expense (Jan) 600
 Prepaid Rent (Feb) 600
 Cash 1,200

95. Monmath Corp. started operations in March of Year 3. The following transactions occur during March.

- a. On March 1, Year 3, Monty contributes \$20,000 for 10,000 shares of \$1 par value stock.
 b. On March 1, Year 3, Monmath borrows \$50,000 on a note from the bank to finance the purchase of a building.
 c. Monmath buys \$15,000 of inventory on account (this is the gross price before any possible discounts).
 d. Monmath pays a \$12,000 account payable with cash.
 e. Monmath paid the annual rent of \$11,760.
 f. Monmath pays for one half of the inventory purchased in (c) above. There are no discounts given.
 g. Issued 300 shares of \$1 par value stock in settlement of \$300 accounts payable.
 h. Received \$400 from a customer for merchandise to be delivered on April 15, Year 3.

Required:

Prepare the journal entries for transactions a through h, assuming Monmath uses the accrual basis of accounting.

a.	Cash	20,000	
	Common Stock		10,000
	Additional Paid-in Capital		10,000
b.	Building	50,000	
	Note Payable		50,000
c.	Merchandise Inventory	15,000	
	Accounts Payable		15,000
d.	Accounts Payable	12,000	
	Cash		12,000
e.	Prepaid Rent	11,760	
	Cash		11,760
f.	Accounts Payable	7,500	
	Cash		7,500
g.	Accounts Payable	300	
	Common Stock		300
h.	Cash	400	
	Advances from Customer		400

96. Assets are usually classified in one of following ways:

CA	-current assets
PPE	-property, plant, and equipment
IA	-intangible asset

Using the abbreviations above, indicate the appropriate classification of each of the following items.

- _____ merchandise inventory
- _____ goodwill
- _____ land
- _____ patent
- _____ work-in-process inventory
- _____ marketable equity securities
- _____ trademark
- _____ furniture and fixtures
- _____ cash
- _____ prepaid insurance

- a. CA
- b. IA
- c. PPE
- d. IA
- e. CA
- f. CA
- g. IA
- h. PPE
- i. CA
- j. CA

97. A friend of yours has prepared the following balance sheet for his bicycle shop but it has a problem. He thought his total assets did not reflect the assets available to the firm. He has asked you to take a look at this balance sheet and help him out.

Eric's Bike Shop, Inc.

Balance Sheet

As of December 31, Year 1

Assets

Current Assets:

Cash	\$15,000
Merchandise Inventory	30,000
Merchandise Sold, at cost	37,500
Prepaid Insurance	1,000
Advance from Customer	<u>(1,000)</u>
Total Current Assets	\$82,500

Property, Plant, and Equipment:

Equipment	8,000
Less Note Payable	<u>(5,000)</u>
Total Assets	<u>\$85,500</u>

Liabilities and Shareholders' Equity

Current Liabilities:

Bike Sales	\$55,000
Accounts Payable	2,000
Accumulated Depreciation	700
Rent Payable	<u>1,000</u>
Total Current Liabilities	\$58,700

Shareholders' Equity:

Common Stock 1,000 shares at \$10 par value	\$10,000
Additional Paid-in Capital	7,500
Retained Earnings	<u>9,300</u>
Total Shareholders' Equity	<u>\$26,800</u>

Total Liabilities and Shareholders' Equity \$85,500

Required:

- a. Prepare a corrected balance sheet for Eric's Bike Shop, Inc.
- b. Draft a memo to Eric explaining the errors you corrected. Include your reasons.

a.

Eric's Bike Shop, Inc.

Balance Sheet

As of December 31, Year 1

Assets

Current Assets:

Cash	\$15,000
Merchandise Inventory	30,000
Prepaid Insurance	<u>1,000</u>
Total Current Assets	\$46,000

Property, Plant, and Equipment:

Equipment	8,000
Less Accumulated Depreciation	<u>(700)</u>

Total Assets

\$53,300

Liabilities and Shareholders' Equity

Current Liabilities:

Accounts Payable	\$2,000
Rent Payable	1,000
Advance from customer	1,000
Note Payable	<u>5,000</u>
Total Current Liabilities	<u>\$ 9,000</u>

Shareholders' Equity:

Common Stock 1,000 shares at \$10 par value	\$10,000
Additional Paid-in Capital	7,500
Retained Earnings	<u>26,800</u>

Total Shareholders' Equity \$44,300

Total Liabilities and Shareholders' Equity

\$53,300

b. Date: March 31, Year 2

To: Eric

From: Me

RE: Corrections to Balance Sheet dated December 31, Year 1

Enclosed please find the corrected version of your Balance Sheet as of December 31, Year 1. The following adjustments have to be made:

- Merchandise Sold and Bike Sales are not balance sheet accounts. Rather, they are the total sales and cost of sales for the accounting period. These accounts need to be closed to Retained Earnings at the end of the period.
- The Advance from Customer is not an asset; it is a liability and represents the amount of goods or service you need to provide the customer in order to earn this revenue.
- The Note Payable should not be shown as a deduction from equipment. Rather, it is an amount the bike shop owes, a liability.
- Accumulated Depreciation is not shown as a liability, it is a contra account to equipment. It shows the amount of the equipment charged to expense from the date the equipment was placed in service.

If you have further questions concerning this financial statement, please do not hesitate to contact me.

98. Prepare journal entries for each of the following unrelated transactions. You may omit explanations for the journal entries.

- A firm issues 5,000 shares of \$2 par value common stock in exchange for \$20,000 cash.
- A firm acquires a building with \$30,000 cash and signs a 15-year note for \$60,000.
- A firm buys inventory for \$980 cash.
- A firm pays \$8,000 to its landlord for annual rent.
- A publisher sells \$3,000 in magazine subscriptions that will be filled over the next 12 months.

a.	Cash	20,000	
	Common Stock		10,000
	Additional Paid-in Capital		10,000
b.	Building	90,000	
	Cash	30,000	
	Note Payable		60,000
c.	Merchandise Inventory	980	
	Cash	980	
d.	Prepaid Rent	8,000	
	Cash	8,000	
e.	Cash	3,000	
	Advances From Customer		3,000

99. You've been asked to review the following balance sheet which has been prepared by a new staff member.

Calvin Springs Outfitters

Balance Sheet

As of December 31, Year 1

Assets

Current Assets:

Cash	\$ 7,500
Accounts Receivable	14,000
Merchandise Inventory	25,000
Land	<u>9,000</u>
Total Current Assets	\$ 46,500

Property, Plant, and Equipment:

Building	<u>\$125,000</u>
Total Assets	<u>\$180,500</u>

Liabilities and Shareholders' Equity

Current Liabilities:

Advance from Customer	\$ 500
Accounts Payable	21,000
Rent Payable	3,600
Utilities Payable	1,200
Salaries Payable	<u>1,800</u>
Total Current Liabilities	\$ 28,100

Shareholders' Equity:

Common Stock 2,000 shares at \$2.50 par value	\$ 5,000
Additional Paid-in Capital	85,000
Retained Earnings	<u>62,400</u>
Total Shareholders' Equity	<u>\$152,400</u>
Total Liabilities and Shareholders' Equity	<u>\$180,500</u>

a. Prepare the journal entries for the following transactions:

1. Merchandise purchased on account and costing \$5,000 was received but not recorded.
2. Payments by clients for previously billed invoices were found in the receptionist's desk drawer. The checks totaled \$2,100.
3. Written checks totaling \$2,700 for payment of accounts payable, were found in the treasurer's desk drawer. He was going to mail them out next Monday.
4. It was discovered that the company president had hired a new secretary for an annual salary of \$18,250.
5. Upon further investigation, you found that the company had paid but incorrectly recorded next year's fire insurance policy, totaling \$3,600. The payment was recorded as an expense.

b. Prepare a corrected balance sheet.

a.	1. Merchandise Inventory	5,000	
	Accounts Payable		5,000
	2. Cash	2,100	
	Accounts Receivable		2,100
	3. Cash	2,700	
	Accounts Payable		2,700
	4. No effect		
	5. Prepaid Insurance	3,600	
	Insurance Expense		3,600
	(Retained Earnings)		

b.

Calvin Springs Outfitters

Balance Sheet

As of December 31, Year 1

Assets

Current Assets:

Cash	\$ 12,300
Accounts Receivable	11,900
Merchandise Inventory	30,000
Prepaid insurance	<u>3,600</u>
Total Current Assets	\$ 57,800

Property, Plant, and Equipment:

Land	9,000
Building	<u>125,000</u>
Total Assets	<u>\$191,800</u>

Liabilities and Shareholders' Equity

Current Liabilities:

Advance from Customer	\$ 500
Accounts Payable	28,700
Rent Payable	3,600
Utilities Payable	1,200
Salaries Payable	<u>1,800</u>
Total Current Liabilities	\$ 35,800

Shareholders' Equity:

Common Stock 2,000 shares at \$2.50 par value	\$ 5,000
Additional Paid-in Capital	85,000
Retained Earnings	<u>66,000</u>
Total Shareholders' Equity	<u>\$156,000</u>
Total Liabilities and Shareholders' Equity	<u>\$191,800</u>

100. Express the following transactions of Forman's Store, Inc., in journal entry form. If an entry is not required, indicate the reason. You may omit explanations for the journal entries.

The store:

- (1) Receives \$35,000 from John Forman in return for 1,000 shares of the firm's \$35 par value common stock.
- (2) Gives a 60-day, 8% note to a bank and receives \$8,000 cash from the bank.
- (3) Rents a building and pays the annual rental of \$11,000 in advance.
- (4) Acquires display equipment costing \$7,000 and issues a check in full payment.
- (5) Acquires merchandise inventory costing \$22,000. The firm issues a check for \$12,000, with the remainder payable in 30 days.
- (6) Signs a contract with a nearby restaurant under which the restaurant agrees to purchase \$1,500 of groceries each week. The firm receives a check for the first two weeks' orders in advance.
- (7) Obtains a fire insurance policy providing \$50,000 coverage beginning next month. It pays the one-year premium of \$1,440.
- (8) Pays \$625 for advertisements that will appear in newspapers next month.
- (9) Places an order with suppliers for \$43,500 of merchandise to be delivered next month.

(1) Cash.....	35,000	
Common Stock		35,000
(2) Cash.....	8,000	
Notes Payable		8,000
(3) Prepaid Rent	11,000	
Cash.....		11,000
(4) Equipment.....	7,000	
Cash.....		7,000
(5) Merchandise Inventory	22,000	
Cash.....		12,000
Accounts Payable		10,000
(6) Cash.....	3,000	
Advances from Customers.....		3,000
(7) Prepaid Insurance	1,440	
Cash.....		1,440
(8) Prepaid Advertising.....	625	
Cash.....		625

(9) The placing of an order does not give rise to a journal entry because it represents a mutually unexecuted contract.

101. Assume that a firm uses the accrual basis of accounting. Indicate the amount of expense the firm recognizes during the month of November for each independent transaction.

- a. Rent of \$3,600 is paid on November 1 for the months November through January.
- b. Inventory costing \$2,500 is ordered on account. The invoice is received on November 25 and the goods are received on December 5.
- c. Insurance premium of \$900 is paid for a full year of coverage starting November 1.
- d. On December 3, an invoice for November utilities of \$325 is received.
- e. On November 1, supplies costing \$2,200 are purchased. At November 30, \$500 of supplies remained on hand.

- a. \$1,200
- b. \$0
- c. \$75
- d. \$325
- e. \$1,700

102. Describe T-accounts and how they are used.

T-ACCOUNTS

A T-account is a device or convention for organizing and accumulating the accounting entries of transactions that affect an individual account, such as cash, accounts receivable, bonds payable, or additional paid-in capital. As the name implies, the T-account looks like the letter T, with a horizontal line bisected by a vertical line. Conventionally, the name of the specific individual account title appears on the horizontal line. One side of the space formed by the vertical line records increases in the account, and the other side records decreases. Which side records increases and which side records decreases differs depending on whether the T-account represents an asset account or represents a liability or shareholders' equity account.

Long-standing custom follows three rules:

1. Increases in assets appear on the left side, and decreases in assets appear on the right side of T-accounts.
2. Increases in liabilities appear on the right side, and decreases in liabilities appear on the left side of T-accounts.
3. Increases in shareholders' equity appear on the right side, and decreases in shareholders' equity appear on the left side of T-accounts.

103. Explain the terms debit and credit. In your discussion, also present the debit and credit rules that are critical for maintaining T-accounts, as well as the equality of the balance sheet.

Accountants use two abbreviations: debit (Dr.) and credit (Cr.). Debit, used as a verb, means “record an entry on the left side of an account.” Used as a noun or an adjective, it means “an entry on the left side of an account.” Credit, used as a verb, means “record an entry on the right side of an account.” Used as a noun or an adjective, it means “an entry on the right side of an account.” These terms combined with the three rules for T-accounts result in the following:

* A debit or charge indicates (1) an increase in an asset, or (2) a decrease in a liability, or (3) a decrease in a shareholders’ equity item.

* A credit indicates (1) a decrease in an asset, or (2) an increase in a liability, or (3) an increase in a shareholders’ equity item.

104. Why does every accounting transaction have two effects?

Accounting is governed by the balance sheet equation, which shows the equality of assets with liabilities plus shareholders’ equity:

$$\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}$$

To maintain this equality, it is necessary to report every event and transaction in a dual manner. If a transaction results in an increase on the left-hand side (Assets), dual transactions recording requires that one of the following must occur to maintain the balance sheet equation: decrease another asset; increase a liability; increase shareholders’ equity. Similarly, if a transaction results in an increase in a Liability account, then one of the following must occur to maintain the balance sheet equation: decrease another liability; decrease shareholders’ equity; increase an asset.

105. What is the relationship between a T-account and a journal entry?

Typically, the accountant records journal entries before transferring the amounts to T-accounts. A T-account is used to record the effects of events and transactions that affect a specific asset, liability, shareholders’ equity, revenue, or expense account (which the text has not yet introduced). It captures both increases and decreases in that specific account, without reference to the effects on other accounts. It also shows the beginning and ending balances of balance sheet accounts. A journal entry shows all the accounts affected by a single event or transaction; each debit and each credit in a journal entry will affect a specific T-account. Journal entries provide a record of transactions, and T-accounts summarize the effects of transactions on specific accounts.

106. Describe the balance sheet equation and the dual effects of transactions.

THE BALANCE SHEET EQUATION AND DUAL EFFECTS OF TRANSACTIONS

The balance sheet equation provides the analytical framework to understand the effects of transactions and events on the financial statements. The balance sheet equation underlies the recording of transactions and events. It captures the financial statement effects of operating, investing, and financing transactions—three key activities of business firms.

The balance sheet equation shows the equality of assets with liabilities plus shareholders' equity. This equation requires that an entity's assets exactly balance, or offset, an equal amount of financing provided by creditors and owners of the corporation. Total liabilities plus shareholders' equity shows the sources of all the firm's financing, and the assets show how the firm holds or has invested those funds. The balance sheet equation maintains this equality by reporting the financial statement effects of each event and transaction in a dual manner, or what are termed the dual effects of transactions. Any single event or transaction will have one of the following four effects or some combination of these effects:

1. It increases an asset and increases either a liability or shareholders' equity.
2. It decreases an asset and decreases either a liability or shareholders' equity.
3. It increases one asset and decreases another asset.
4. It increases one liability or shareholders' equity and decreases another liability or shareholders' equity.

107. Describe a typical balance sheet.

A TYPICAL BALANCE SHEET

The balance sheet groups individual accounts by type (asset, liability, or shareholders' equity) and lists these accounts with their balances as of the balance sheet date. The date of the balance sheet appears at the top of the balance sheet. The asset and liability categories further group individual accounts by the expected timing of cash receipts (for assets) or cash payments (for liabilities). Common terminology describes items whose cash receipts or payments the firm expects will occur within one year as current assets or current liabilities, respectively. If the firm expects to collect or pay more than one year after the balance sheet date, the balance sheet classifies these as noncurrent assets and noncurrent liabilities, respectively. The balance sheet begins with a list of assets and then lists liabilities and shareholders' equity. Both U.S. GAAP and IFRS require firms to report balance sheet accounts for the prior year in addition to the current year. Under U.S. GAAP, assets and liabilities appear in order of decreasing closeness-to-cash; many firms that report under IFRS reverse this ordering.

108. What is the purpose of using contra accounts? What is the alternative to using them?

Contra accounts provide disaggregated information concerning the net amount of an asset, liability, or shareholders' equity item. For example, the account Property, Plant, and Equipment Net of Accumulated Depreciation does not indicate separately the acquisition cost of fixed assets and the portion of that acquisition cost written off as depreciation since acquisition. If the firm used a contra account, it would have such information.

The alternative to using contra accounts is to debit or credit directly the principal account involved (for example, Property, Plant, and Equipment). This alternative procedure, however, does not permit computation of disaggregated information about the net balance in the account. Note that the use of contra accounts does not affect the total of assets, or liabilities, or shareholders' equity, but only the balances in various accounts that comprise the totals for these items.

109. What distinguishes noncurrent assets from current assets?

The distinction is based on time. Current assets are expected to be converted to cash or used within a year. Noncurrent assets are expected to be converted to cash over longer periods.

110. Explain the difference between inventories for a retailer versus a manufacturer.

Merchandise Inventory reflects goods on hand purchased for resale for the retailer, where as , manufacturer may have raw materials inventory including materials as yet unused for manufacturing products; work-in-process inventory, which includes partially completed manufactured products; and finished goods inventory which is completed but unsold manufactured products.

111. What is goodwill and how is it classified in terms of the accounting equation?

When one firm acquires another firm, it measures the identifiable assets acquired and liabilities assumed at their current fair values. If the purchase price exceeds the sum of the fair values of the identifiable assets less the identifiable liabilities, the excess is goodwill.

Goodwill is an asset that includes intangibles that the acquiring firm cannot separately identify, such as customer loyalty. These desirable attributes cause the buyer to pay more for the acquired firm than the sum of the fair values of all the other assets, less liabilities, identified in the acquisition

112. Explain the order of assets and liabilities in the balance sheet under U.S. GAAP and IFRS.

Under U.S. GAAP, assets and liabilities appear in order of decreasing closeness-to-cash; many firms that report under IFRS reverse this ordering.

113. Explain how tenants record rent paid in advance for an office building and how a landlord or owner of the property rented records the receipt of the advance payment. Show journal entries as part of your answer.

Tenant: Rent paid in advance for the future use of an office building is recorded as an asset called Prepaid Rent.

Journal entry:

Prepaid Rent	XX
Cash	XX

Landlord or Office Building Owner: Rent received in advance shows up as a liability for the owner or landlord. The owner of the office space cannot include in income the amounts paid by the tenant for future months until the owner provides the rental services. So, the advance payment results in a liability payable in services for the use of the building and is commonly called Advances from Tenants, or Rent Received in Advance.

Journal entry:

Cash	XX	
Rent Received in Advance		XX

114. Many firms, especially in their first years of operation and growth, face a variety of challenges obtaining funds to finance their growth.

Required:

Discuss how a small, young manufacturing firm that has a relatively unpredictable revenue stream might approach financing a new manufacturing line.

A manufacturing firm would have significant investments in property, plant, and equipment (PPE). It will require funds to make such investments, with potential sources including short-term liabilities, long-term liabilities, issuing additional shares of stock. When choosing these financing sources, the firm will not want to significantly add to the uncertainty and risk it already faces. Such risks exist in its unpredictable revenue stream. Using short-term liabilities as a potential source may not yield sufficient funds for the new manufacturing line, nor may operating cash flows thus freed be available. Taking on long-term debt may expose the firm to too much risk in its ability to pay the periodic interest and ultimately the balance of the long-term debt. Issuing additional shares of stock may bring in sufficient funds. In addition, a young organization is not expected to declare and pay periodic dividends early in its life. Thus, the need to cover these types of cash flows is lessened.

115. Several actions that an organization may take are not recognized or entered in the accounting records. While not entered into the formal accounting system, several such actions are exceedingly important to the organization.

Required:

Comment on the current and future implications that the hiring of a new president may have on the organization's accounting records.

The hiring of a new president would not be recorded in the accounting records, as it does not immediately affect recorded assets, liabilities, or stockholders' equity. The hiring does not carry a historical cost that is easily quantified for accounting purposes. Information about the hiring, including the president's name, address, etc. would be entered into the organization's information systems (such as personnel and payroll). Subsequent periods in which the president earned his/her salary may record a debit to Salaries Expense and a credit to Cash (or Salaries Payable). Such a transaction does have an objectively determined value per the employment contract.