

Basic accounting: concepts, techniques and conventions assignment



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Southern New Hampshire University (SNHU) School of Business – Graduate Programs – www.snhu.edu Managerial Accounting – ACC 500 CHAPTER 15 COVERAGE OF LEARNING OBJECTIVES LEARNING OBJECTIVE FUNDAMENTAL ASSIGNMENT MATERIAL ADDITIONAL ASSIGNMENT MATERIALEXCEL, COLLAB. , & INTERNET EXERCISES LO1: Read and interpret the basic financial statements. 19, 20, 25, 30 3643 LO2: Analyze typical business transactions using the balance sheet equation. A1, A2, B1, B222, 23, 26, 27 28, 29, 30, 31 36, 3741, 42 LO3: Distinguish between the accrual basis of accounting and the cash basis of accounting.

A3, B321, 36 LO4: Relate the measurement of expenses to the expiration of assets. 2742 LO5: Explain the nature of dividends and retained earnings. 24, 39, 40 LO6: Select relevant items from a set of data and assemble them into a balance sheet, an income statement, and a statement of retained earnings. A2, B225, 28, 30, 38 39, 4041 LO7: Distinguish between the reporting of corporate owner's equity and the reporting of owner's equity for partnerships and sole proprietorships. LO8: Identify how the measurement conventions of recognition, matching and cost recovery, and stable monetary unit affect financial reporting. 3 CHAPTER 15 Basic Accounting: Concepts, Techniques, and Conventions 15-A1(20-30 min.) 1. $E = 150 - 120 = 30$ $D = 40 + 30 = 70$ $C = 15$ because there were no additional investments by stockholders $A = 85 - 15 - 40 = 30$; or $85 - (15 + 40) = 30$ $B = 95 - 15 - 70 = 10$; or $95 - (15 + 70) = 10$ 2. $K = 20 + 170 = 190$ $J = 50 + 20 - 5 = 65$ $H = 10 + 30 = 40$ $F = 50 + 10 + 100 = 160$ $G = 275 - 65 - 40 = 170$ 3. $P = 300 - 270 = 30$ $Q = 100 + 30 - 110 = 20$ $N = 85 - 35 = 50$ $L = 105 + 50 + 100 = 255$ $M = 95 + 85 + 110 = 290$

This problem was designed for an equation-type solution, but some students may find a different approach more helpful in understanding the solution and its steps. Such an approach can be easily developed on the board as follows, using Case 1 as an example: Given: BeginningEndSteps: LiabilitiesAB1. $A = 85 - (40 + 15) = 30$ Paid-in capital15C2. $E = 150 - 120 = 30$ Retained earnings 40 D3. $D = 40 + 30 - 0 = 70$ Total (equal to total assets) 85954. $C = 15 + 0 = 15$ 5. $B = 95 - (70 + 15) = 10$ Revenues150 Expenses120 Net earnings E 15-A2(40-55 min.) 1. See Exhibit 15-A2 on the following page. 2.

SRINIVAS COMPANY

Income Statement For the Month Ended April 30, 20X1 Sales (revenue)\$100,000 Deduct expenses: Cost of goods sold\$40,000 Wages, salaries and commissions43,000 Rent, 2,000 + 10,00012,000 Depreciation 1,000 Total expenses 96,000 Net income\$ 4,000 EXHIBIT 15-A2 SRINIVAS COMPANY

Analysis of Transactions for April 20X1 (in thousands of dollars) Assets= Equities Mer-Pre-Equip-LiabilitiesStockholders' Equity

Accountschandisepayment and= NoteAccountsPaid-inRetained

DescriptionCash +Receivable +Inventory +Rent +Fixtures= Payable

+Payable +Capital +Earnings a. Incorporation+120=+120 b. Purchased erchandise-35+35= c. Purchased merchandise+25=+25 d1.

Sales+30+70=+100(revenue) d2. Cost of inventory sold-40=- 40(expense)

e. Collections+15-15= f. Disbursements to trade creditors-18=-18 g.

Purchased equipment-12+36=+24 h. Prepaid rent- 6+6= i. Rent expense-

10=- 10(expense) j. Wages, etc. -43=- 43(expense) k. Depreciation- 1=-

1(expense) l. Rent expense -2 = - 2(expense) Balances, April 30,

20X1+41+55+20+4+35=+24+ 7+120+ 4 ? _____?

_____?? _____? _____? 155155 SRINIVAS

COMPANY Balance Sheet April 30, 20X1

Liabilities and Assets
 Stockholders' Equity
 Liabilities: Cash\$ 41, 000
 Note payable\$ 24, 000
 Accounts receivable55, 000
 Accounts payable 7, 000
 Merchandise20, 000
 Total liabilities\$ 31, 000
 Stockholders' equity:
 Prepaid rent4, 000
 Paid-in capital\$120, 000
 Equipment and fixtures 35, 000
 Retained earnings 4, 000
 Total stockholders' equity 124, 000
 Total assets\$155, 000
 Total liabilities and stockholders' equity\$155, 000

3. Most businesses tend to have net losses during their infant months, so Srinivas's ability to show a net income for April is good. Indeed, the rate of return on beginning investment is $\$4,000 \div \$120,000 = 3.33\%$ per month, or 40% per year.

Many points can be raised, including the problem of maintaining an "optimum" cash balance so that creditors can be paid neither too quickly nor too slowly. See the next solution also. 15-A3(5-10 min.) Revenue (cash basis): Cash sales\$30, 000 Cash collected from credit customers 15, 000 Total revenue\$45, 000 The accrual basis provides a more accurate measure of economic performance. As long as the two recognition criteria are met (earned and realized), the \$100, 000 measure of revenue on the accrual basis is preferred to the \$45, 000 measure of revenue on the cash basis.

The \$100, 000 is the more accurate measure of accomplishments for April.

15-B1(10-15 min.) This is straightforward. Computations are in millions of dollars. $A = 8,363.2 - (4,213.5 + 2,921.3) = 1,228.4$ $B = 2,589.0 + 907.0 = 3,496.0$ $C = 2,921.3 - 907.0 - 0.0 + 2.2 = 2,016.5$ $D = 4,213.5 + 136.6 = 4,350.1$ $E = 1,188.8 + 4,350.1 + 2,016.5 = 7,555.4$

Instructors may wish to comment about the \$136.6 million additional
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investments by stockholders; many companies have stock purchase plans for employees and/or stockholders. 15-B2(30-40 min.) 1. See Exhibit 15-B2 on the following page.

EXHIBIT 15-B2 PACCAR Analysis of Transactions for January 2003 (in millions of dollars) Assets= Equities Prepaid Property, Exp. & Liabilities Stockholders' Equity Accounts Inven-Plant, = Accounts Other Paid-in Capital &

Transaction Cash + Receivable + tories + Equip. + Assets = Payable

+ Liabilities Retained Earnings Balances 1/1/03 + 773 + 5,064 + 311 + 1,577 + 978 = +1,275 + 4,827 + 2,601 a1. +155 + 500 = +655 (increase revenue) a2. -390 = -390 (increase expense) b. +500 = +500 c. +300 - 300 = d. -250 + 250 = e. -450 = -450 f. -100 = -100 (increase expense) g. -90 = -90 (increase expense) h. 20 = -20 (increase expense) Balances, 1/31/03 + 428 + 5,264 + 421 + 1,557 + 1,138 = +1,325 + 4,827 + 2,656 ? _____ ? _____ ??

_____ ? _____ ? +8,808 +8,808 2. PACCAR Statement of

Earnings For the Month Ended January 31, 2003 (in millions) Sales \$655

Deduct expenses: Cost of goods sold \$390 Selling and administrative expenses 100 Rent and insurance expense 90 Depreciation 20 Total expenses 600 Net earnings \$ 55 PACCAR Balance Sheet January 31, 2003 (in millions)

Liabilities and Assets Stockholders' Equity Cash \$ 428 Accounts payable \$1,325

Accounts receivable 5,264 Other liabilities 4,827 Inventories 421 Stockholders' equity 2,656 Prepaid expenses & other assets 1,138 Property, plant, and equipment 1,557 Total \$8,808 Total \$8,808 15-B3(5-10 min.) Revenue (cash

basis): Cash sales \$155,000,000 Collections from credit customers 300,000,000 Total revenue \$455,000,000 The accrual basis provides a more

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accurate measure of economic performance. As long as both recognition criteria are met (earned and realized), the \$655 million measure of revenue on the accrual basis is preferred to the \$455 million measure of revenue on the cash basis.

The \$655 million is the more accurate measure of accomplishments for January. 15-1The income statement answers questions about financial performance over a span of time. The balance sheet answers questions about financial status at a point in time. 15-2Assets are economic resources that a company owns and expects to benefit future activities. Liabilities are a company's obligations to nonowners. 15-3The income statement is the main link between two balance sheets. The income statement explains how operations have changed the balance sheet values over a span of time. 5-4This statement is fallacious because it does not take into consideration withdrawals (dividends) or increases in ownership investment, both of which affect the ownership capital account but not net income. 15-5Under the accrual basis, companies recognize revenue as it is earned and realized and expenses in the period when costs expire. In contrast, the cash basis recognizes revenue as cash is collected and most expenses as cash is disbursed. 15-6Adjusting entries differ from routine entries in that they deal with implicit transactions in contrast with the explicit transactions that trigger nearly all the day-to-day routine entries. 5-7The manager acquires goods and services (including advertising), not expenses per se. These goods and services become expenses as they are used in obtaining revenue. 15-8It is preferable to refer to the costs rather than the values of assets such as plants or inventory because the word value has many meanings and is more

vague than the word cost. Cost explicitly recognizes that balance sheet amounts are based on the amounts spent on assets, not their current values. 15-9Yes. Depreciation is simply the allocation of the acquisition cost of assets over the periods that benefit from the asset's use. It is not a measure of the changes in market value of an asset. 15-10Retained earnings is neither an asset nor a preferred claim against cash or any other asset, but it represents a general claim against total assets. In most instances no "pot of gold" exists, as the cash inflow from operations will be largely reinvested in other assets. 15-11Although profitable operations are typically a prerequisite to dividends, dividends are actually a distribution of assets that "liquidate" a portion of the ownership claim. 15-12Congress has delegated the setting of generally accepted accounting principles to the Securities and Exchange Commission (SEC).

In turn, the SEC has delegated the task to the Financial Accounting Standards Board (FASB), which is a private-sector body supported by those with interests in preparing, auditing, and using financial statements. 15-13Accountants create value through the information they supply to decision makers. If users cannot trust the information, it will have little value. Therefore, accountants must be especially careful to adhere to strict ethical guidelines and exhibit the utmost integrity. 15-14Accountants record revenue when the company has both earned and realized the revenue.

This is important because it triggers the recognition not only of the revenue, but also of the related expenses. 15-15The use of the dollar as the principal accounting measure has been criticized because the changing purchasing power of a monetary unit over time is not taken into account. 15-16The <https://assignbuster.com/basic-accounting-concepts-techniques-and-conventions-assignment/>

going-concern concept is a notion that implies that companies will use existing resources to fulfill the general purpose of a continuing concern rather than sell them in tomorrow's real estate or equipment market. 15-17 In the accounting sense, objectivity means freedom from bias or accuracy that can be verified by other independent accountants. 5-18 Economic feasibility sometimes inhibits the adoption of new ways to measure financial performance and position because the apparent benefits may not exceed the obvious costs of gathering and interpreting the information. 15-19 Because land is recorded at its historical cost and is not depreciated, the land purchased in 1910 would still be listed at its purchase price. The market value of that land nearly 100 years later is likely to be substantially more than the amount on the books. The equipment purchased in 1998 would be listed at its purchase price less the depreciation taken on it since 1998.

This may be more or less than the current market price of the equipment. Even though the book value of the equipment may differ from its market price, the difference between the book value and the market price of the equipment is likely to be much less than the difference between the book value of the land and its market price. 15-20 A marketing manager generally focuses on changes in assets, not the general level of the assets. Marketing decisions deal with generating revenues and the costs of those revenues. Such items are recorded on the income statement.

Although the income statement and balance sheet articulate, that is, the income statement explains changes in the balance sheet, the most direct measures of marketing performance are in the income statement. 15-21 A

principle of good performance measures is that they recognize performance
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as close as possible to the time of the performance. If the goal of the sales staff is to close sales, then such staff should be evaluated on the amount of sales closed. Any delay between the closing of the sale and the recognition of sales staff performance weakens the motivational effects of the performance measure.

One potential delay is the time between closing the sale and the time the company receives payment for the goods or services. Accrual accounting does not wait until the receipt of cash before recognizing a sale, whereas cash accounting does. Thus, accrual accounting generally provides a more relevant sales performance measure than does cash-basis accounting.

15-22 We know that stockholders' equity will be \$400,000, and the difference between the amount of assets and the amount of liabilities will also be \$400,000. But we do not know the exact amount of the assets and the liabilities.

5-23 (10-15 min.)

1. False. Accounts receivable should be classified as an asset.
2. False. Retained earnings should be accounted for as a stockholders' equity item.
3. False. Machinery used in the business should be recorded at original cost less accumulated depreciation.
4. False. A large retained earnings balance is the best evidence of previous profitable operations.
5. True
6. False. From a single balance sheet, you can find stockholders' equity for a specific day.

15-24 (15-20 min.)

The theme of this solution is that retained income is not a pot of cash awaiting distribution to stockholders.

Cash	\$1,500	Paid-in capital	\$1,500
Inventory	600	Total assets	\$1,500

Note in both Requirements 1 and 2 that the ownership equity is fundamentally a claim against the total assets (in the aggregate). For example, 60% of the shareholders do not have a specific

claim on cash, and 40% of the shareholders do not have a specific claim on inventory. Instead, they have an undivided claim against (or interest in) all of the assets. 3. Cash\$1, 750Paid-in capital\$1, 500 Retained earnings 250 Total liabilities and stockholders' equity\$1, 750

Retained earnings is part of the stockholders' equity. Even though cash and retained earnings have increased by identical amounts, the retained earnings is fundamentally a general interest in total assets (just as paid-in capital is a general interest in total assets). Retained earnings is the net rise in ownership claim attributable to profitable operations. However, the assets themselves should not be confused with the claims against the assets. 4. Cash\$ 600Paid-in capital\$1, 500 (\$1, 750-\$400-\$750)Retained earnings250 Inventory400 Equipment 750Total liabilities and

Total assets\$1, 750 stockholders' equity\$1, 750 The same explanation applies here as in Requirement 3. However, Transaction 4 should clarify the lack of a specific link between retained earnings (and paid-in capital) and any particular assets. The ownership claims are general, not specific. 5. Cash\$ 600Accounts payable\$ 350 InventoryPaid-in capital1, 500 (\$400+\$350)750Retained earnings 250 Equipment 750Total liabilities and Total assets\$2, 100 stockholders' equity\$2, 100 The meaning of retained earnings was explained in answer 3.

Purchases on "open account" usually create a general liability; that is, the trade creditors usually hold only general claims against the total assets, not specific claims against particular assets (as created by mortgages on buildings). In sum, both the creditors and the owners hold general claims

against the assets. Of course, if the corporation is liquidated (all assets converted to cash to be distributed to claimants), the creditors' general claims must be satisfied before the owners get one dollar. Thus, the stockholders are said to have residual claim or residual interest. 15-25(10-15 min.) 1.

The name of the statement is antiquated. This statement is ordinarily either a statement of profit or a statement of loss, not profit and loss. It is usually titled income statement or statement of earnings or sometimes a statement of operations.. 2. The line with the date should not be for an instant of time but for an indicated span of time. 3. Companies do not usually recognize increases in market values when using historical cost accounting. 4.

Dividends are not expenses, and companies do not deduct them when calculating net profit. 5. The appropriate deduction is the cost of goods sold, not purchased. . The bottom line is more often titled net income or net earnings, although net profit is acceptable. 7. Although this is not the major point of the problem, the income statement has apparently omitted some expenses. For example, neither rent nor depreciation is shown; at a minimum, one or the other would ordinarily be included. 8. " Cash received from loan" should not be listed on the income statement. 15-26(10 min.)

SonyUnited Airlines $A = L + SE$ $A = L + SE$ PrepaidUnearned

TravelTravelSalesSales CashExpenseExpenseCash= RevenueRevenue 1.

Dec. payment-70, 000+70, 000=+70, 000=+70, 000 2. Feb. ravel-70, 000=-70, 000=-70, 000+70, 000 15-27(10-15 min.) Winsted Hardware,

TenantHutchinson, Landlord $A = L + SE$ $A = L + SE$ Unearned

PrepaidRentRentRent CashRentExpenseCashRevenueRevenue 1. -6, 000+6,

000=+6, 000=+6, 000 2. -2, 000=-2, 000=-2, 000+2, 000 3. -2, 000=-2, 000=-2, 000+2, 000 4. -2, 000=-2, 000=-2, 000+2, 000 15-28(15-20 min.)

Assets - Liabilities= Stockholders' equity Dec. 31: B125, 000 - B55, 000= B70, 000 Jan. 1: B100, 000 - B40, 000= B60, 000 Change: B 25, 000 - B15, 000= B10, 000 1. As above, B60, 000. This is the easiest computation. 2.

Change in stockholders' equity + Cash dividends= Net income

B10, 000 + B16, 000= B26, 000 3. Let X = Cost of goods sold Sales - Cost of goods sold - Operating expenses = Net income B265, 000 - X - B50, 000= B26, 000 -X= B26, 000 - B265, 000 + B50, 000 X= B189, 000 15-29(20-30 min.)

Case 1234567 X\$10, 000\$3, 000\$9, 000\$14, 000\$7, 500\$ 8, 000\$ 4, 200 Y6, 0006, 0002, 0003, 600 Z2, 0002, 0009, 000(200) Loss A4, 5004, 800

B16, 50015, 200 Computations: 1: X = \$ 9, 000 + \$ 3, 000 - \$ 2, 000 = \$ 10, 000 2: X = \$ 9, 000 - \$ 6, 000 = \$ 3, 000 : Y = \$ 11, 000 - \$ 5, 000 = \$ 6, 000 : Z = \$ 5, 000 - \$ 3, 000 = \$ 2, 000 3: X = \$ 6, 000 + \$ 10, 000 - \$ 7, 000 = \$ 9, 000 : Y = \$ 15, 000 - \$ 9, 000 = \$ 6, 000 Z = \$ 6, 000 - \$ 4, 000 = \$ 2, 000 4: X = \$ 8, 000 + \$ 12, 000 - \$ 6, 000 = \$ 14, 000 5: X = \$ 3, 000 + \$ 4, 500 = \$ 7, 500 6: X = \$ 14, 000 - \$ 6, 000 = \$ 8, 000 : Y = \$ 6, 000 - \$ 4, 000 = \$ 2, 000 : Z = \$ 8, 000 + \$ 7, 000 - \$ 6, 000 = \$ 9, 000 : A = \$ 10, 000 - \$ 2, 000 + \$ 1, 500 - \$ 5, 000 = \$ 4, 500 : B = \$ 4, 500 + \$ 12, 000 = \$ 16, 500 7: X = \$ 8, 200 - \$ 4, 000 = \$ 4, 200 : Y = \$ 9, 600 - \$ 6, 000 = \$ 3, 600 : Z = \$ 3, 600 + \$ 400 - \$ 4, 200 = \$ (200) : A = \$ (200) + \$ 5, 000 = \$ 4, 800 : B = \$ 20, 000 - \$ 4, 800 = \$ 15, 200 Note: The formula for cost of goods sold is not discussed in the chapter, but it is given in the problem.

The following framework may help on cases 6 and 7: Stockholders' equity:

Case 6 Case 7 Beginning \$? = 4, 500 \$ 8, 200 - 4, 000 = 4, 200 Additional
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investments +5,000 Net profit $Y = 6,000 - 4,000 = +2,000$? = -200

Dividends -1,500 -400 End \$10,000 \$9,600 - 6,000 = 3,600 Then $A = L +$

$SE = 12,000 + 4,500 = 16,500$ In case 6, the \$4,500 is the beginning

balance, $\$10,000 - (\$5,000 + \$2,000 - \$1,500) = \$4,500$. In case 7, the

net loss of \$200 is $\$4,200 - (\$3,600 + \$400) = \200 . 15-30 (45-75 min.) 1.

See Exhibit 15-30 on the following page. 2. UNIVERSITY WIRELESS Statement

of Income For the Month Ended October 31, 20X1

Sales \$60,000 Cost of goods sold 30,000 Gross profit \$30,000 Operating

expenses: Rent \$500 Depreciation 50 Advertising 9,000 Wages and

salaries 11,000 Miscellaneous 1,510 22,060 Operating income \$7,940

Interest expense 40 Net income \$7,900 EXHIBIT 15-30 Assets = Equities Pre-

Fixtures Liabilities Stockholders' Equity Accounts paid and Equip-

Accounts Notes Accr. Accr. Paid-in Retained Trans. Cash + Receivable

+ Inventory + Rent + ment = Payable + Payable + Wages + Int. + Capital

+ Earnings a. +36,000 = +36,000 b. -20,000 +40,000 = +20,000 c1. -1,

000 +1,000 = c2. *-500 = -500 (E) d1. = +3,000 -3,000 (E) 2. -6,000 = -6,

000 (E) e1. +10,000 +50,000 = +60,000 (R) e2. -30,000 = -30,000 (E) f1. -

5,000 = -5,000 (E) f2. = +6,000 -6,000 (E) g. -1,510 = -1,510 (E) h. -1,

000 +6,000 = +5,000 i. = +40** -40 (E) j. -50 = -50 (E) k. -6,000 = -6,000

(D) Balance 10/30 + 5,490 +50,000 +10,000 + 500 +5,950 = +23,000 +5,

000 +6,000 +40 +36,000 + 1,900 *This and other adjustments could be

made at the end of this series of entries. **. $0.96 \times \$5,000 \times 1/12 = \40

UNIVERSITY WIRELESS Balance Sheet October 31, 20X1

Assets Equities Liabilities: Cash \$5,490 Accounts payable \$23,000 Accounts

receivable 50,000 Notes payable 5,000 Inventory 10,000 Accrued wages and

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Prepaid rent 500 salaries payable 6,000 Fixtures and equipment 5,950 Accrued interest payable 40 Total Liabilities \$34,040 Stockholders' equity: Paid-in capital \$36,000 Retained earnings 1,900 37,900 Total assets \$71,940 Total equities \$71,940 UNIVERSITY WIRELESS Statement of Retained Earnings For the Month Ended October 31, 20X1 Retained earnings, October 1, 20X1 \$ 0 Add: Net income for October 7,900 Total \$7,900 Deduct: Cash dividends 6,000

Retained earnings, October 31, 20X1 \$1,900 3. The picture in this set of financial statements is not unusual for new businesses. Some of the liabilities are very current: accounts payable, \$23,000 and accrued wages, \$6,000. Yet there is a small amount of cash. Unless much of the accounts receivable can either be collected or discounted (sold to a bank or other lender) the company may be unable to meet its payroll and pay its bills on time. Moreover, the inventory badly needs replenishment if sales are to continue at their current pace. Payment of a \$4,000 dividend may not have been wise.

Many new businesses can show a respectable net income but nevertheless be at the brink of financial disaster because they are "under-capitalized." That is, there is insufficient long-term investment capital to sustain a smooth growth. Too often, creditors and employees need cash far in advance of when customers provide the cash to the business. This may be such a case, unless customers pay promptly. 15-31(5 min.) 1. Cr. 2. Cr. 3. Cr. 4. Dr. 5. Cr. 6. Cr. 7. Cr. 15-32(10 min.) The following statements are true: 4, 5, 8, 9. Explanations for the false statements follow: 1. The first sentence is correct.

However, credit entries always must be on the right. 2. Amounts borrowed are debited to Cash and credited to Notes Payable. 3. Decreases in assets are shown on the credit side, but decreases in liabilities and stockholders' equity are shown on the debit side. 6. All credits are on the right. 7. Payments on mortgages are credited to cash and debited to Mortgage Payable. 10. Purchases of inventory should be debited to Inventory and credited to Accounts Payable. 11. Decreases in liability accounts should be on the left (or decreases in asset accounts should be on the right). 15-33(10-15 min.) 1 and 2.

CashDues ReceivableAccounts Receivable a. 300a. 300b. 200d. 200 b. 150 d. 200 EquipmentAccounts Payable c. 120b. 350c. 120 15-34(20-30 min.) See Exhibit 15-34. 15-35(20-40 min.) See Exhibit 15-35. EXHIBIT 15-34Amounts are in thousands of dollars. CashNote PayablePaid-in Capital (a)120(b)35(g)24(a)120 (d1)30(f)18 (e)15(g)12 (h)6 (i)10Accounts PayableRetained Earnings (j)43(f)18(c)25Net Inc. 4 Bal. 41 Accounts Receivable (d1)70(e)15Cost of Goods SoldSales (d2)40(d1)100 Merchandise Inventory (b)35(d2)40Rent ExpenseWages, Sal. , & Comm. (c)25(i)10(j)43 (l)2 Prepaid Rent (h)6(l)2Depreciation Expense (k)1

Equipment and Fixtures (g)36(k)1*Details of the revenue and expense accounts appear in the income statement. Their net income effect appears in Retained Earnings in the balance sheet. Note: Ending balances should be drawn for each account, but they are not shown here because they can be computed mentally. EXHIBIT 15-35 CashNote PayableAccr. Interest Payable (a)36, 000(b)20, 000(h)5, 000(i)40 (e1)10, 000(c1)1, 000 (d2)6, 000Accounts PayablePaid-in Capital (f1)5, 000(b)20, 000(a)36, 000 (g)1, 510(d1)3, 000
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(h)1, 000 (k)6, 000 Accrued Wages & Sal. Retained Earnings Bal. 5, 490 (f)2)6, 000 (k)6, 000 Inc. 7, 900 Accounts Receivable e)1)50, 000 Cost of Goods Sold Sales (e)2)30, 000 (e)1)60, 000 Rent Expense Inventory (c)2)500 (b)40, 000 (e)2)30, 000 Depreciation Expense Advertising Expense (j)50 (d)1)3, 000 (d)2)6, 000 Interest Expense Prepaid Rent (i)40 (c)1)1, 000 (c)2)500 Wages & Sal. Expense (f)1)5, 000 Miscellaneous Expense (f)2)6, 000 (g)1, 510 Fixtures and Equipment (h)6, 000 (j)50 Note: Ending balances should be drawn for each account, but they are not shown here because they can be computed mentally. 15-36(30 min.) 1. DR. VERONICA BRIDGE, DENTIST Income Statement For the Year Ended December 31, 20X1 Cash Accrual Basis Basis Fee revenue \$81, 000 \$99, 000 1

Expenses: Rent \$7, 500 \$6, 000 2 Utilities 600 700 3 Salaries 16, 000 17, 000 4 Depreciation 12, 000 5 Total expenses \$24, 100 \$35, 700 Operating income \$56, 900 \$63, 300 1 \$81, 000 collected - \$2, 000 unearned + \$20, 000 receivable 2 \$7, 500 - \$1, 500 applicable to the first quarter of 20X2 3 \$600 + \$100 owed 4 \$16, 000 + \$1, 000 owed 5 \$72, 000 ? 6 = \$12, 000 The term " cash basis" is ambiguous. A strict interpretation of cash basis would permit deducting the full \$72, 000 paid for equipment as an expense in 20X1. Operating income would be \$56, 900 - \$72, 000 paid for equipment = a loss of \$15, 100. 2.

The accrual basis provides a better measure of economic performance because it encompasses all assets and liabilities arising from operations rather than their immediate cash effects alone. For example, the \$2, 000 advance payment has not yet been earned and therefore represents an obligation of Dr. Bridge. However, the \$20, 000 fees billed have been earned <https://assignbuster.com/basic-accounting-concepts-techniques-and-conventions-assignment/>

and represent a legitimate economic resource of that magnitude (unless their full collectibility is in doubt). The government permits the cash basis primarily to ease the cash demands on taxpayers and to ease the record keeping tasks of small businesses.

In short, if you extend credit to your customers, the government does not feel it equitable to demand payment for taxes if you have not yet received your cash. Remember, therefore, that income measurement may legitimately differ for different purposes. In this case, the cash basis may be the preferable way to measure income for tax purposes. But to measure her own economic performance as a dentist, Dr. Bridge would probably prefer the accrual basis. This is a major point—there is nothing inherently evil about having “ two sets of books. ” 15-37(10-15 min.) 1.

The bank’s assets (cash) and liabilities (deposits) would each increase by \$1,000. Personal assets would change, but liabilities and owners’ equity would not, assuming that the cash on hand had already been recorded as, say, cash on hand (asset) and personal capital (owners’ equity). If the latter recording had been made, the deposit would merely represent the transforming of one asset (cash on hand) into another (cash in bank); no liabilities or owners’ equities would be affected. 2. The bank’s total assets and liabilities would be unaffected. The only change would be in the form of assets.

Cash would decrease by \$800,000, and notes receivable would increase by the same amount. 3. Personal cash (asset) would increase, and personal liabilities (note payable) would increase. 15-38(20 min.) KELLOGG COMPANY

Balance Sheet March 29, 2003 (in millions of dollars)

Assets	Liabilities and Stockholders' Equity*
Cash and equivalents	\$ 138.8
Accounts payable	\$ 583.3
Receivables	811.1
Accrued liabilities	1,227.9
Inventory	594.2
Long-term liabilities	5,830.5
Property, plant, & equip.	2,776.2
Other liabilities	1,707.3
Other assets	5,937.7
Total liabilities	9,349.0
Common stock	\$ 148.4
Retained earnings	760.6
Total stockholders' equity	909.0
Total assets	\$10,258.0
Total liab. and stk. equity	\$10,258.0

** *This is the heading used in most actual annual reports. **Same amount as total assets. (a) \$10,258.0 - \$138.8 - \$811.1 - \$2,776.2 - \$5,937.7 = \$594.2. (b) \$148.4 + \$760.6 = \$909.0 (c) \$10,258.0 - \$909.0 = \$9,349.0 or \$583.3 + \$1,227.9 + \$5,830.5 + \$1,707.3 = \$9,349.0 Note that net sales is not a balance sheet account. 15-39(20-25 min.) The following statements follow the general format used by Disney. Obviously, various alternatives are possible: 1.

(a) WALT DISNEY COMPANY Income Statement

For Fiscal Year 2002 (in millions)

Revenues	\$25,329
Operating Costs and expenses	22,924
Operating income	2,405
Other income, net	137
Net interest expense	(453)
Income before taxes*	2,089
Income taxes*	853
Net income	\$1,236

*This is the nomenclature used by Disney. Note how the title of this income statement uses "income," whereas the title of the retained income statement uses "retained earnings." (b) WALT DISNEY COMPANY Statement of Retained Earnings For Fiscal Year 2002 (in thousands of dollars)

Balance at beginning of year	\$12,171
Net income for the year	1,236
Dividends paid	(428)*

Balance at end of year \$12,979 * \$12,171 + \$1,236 - Dividends = \$12,979

Dividends = \$428 2. The cash dividend is \$428 ? \$1,236 = 35% of net
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income. This is a relatively large dividend for Disney. Generally their cash dividends have been less than 20% of net income because the company financed much of its growth from profits reinvested in the business. Part of the reason for the dividend in recent years being high is that net income was lower than it had been in previous years. To maintain reasonable dividend payouts, Disney had to pay cash dividends that were a high proportion of its net income. 5-40(15-25 min.) The following is a reproduction of Procter & Gamble's statements. Students may use other acceptable formats. Accounts payable and cash are irrelevant. 1. PROCTER & GAMBLE COMPANY

Statement of Earnings Year Ended June 30, 2002 (in millions) Net sales and other income\$40, 238 Costs and expenses: Cost of products sold20, 989 Marketing, research, and administrative expenses12, 571 Interest and other expenses 295 (No label given) 33, 855 Earnings before income taxes6, 383 Income taxes 2, 031 Net earnings\$ 4, 352 2. PROCTER & GAMBLE COMPANY
Statement of Retained Earnings

Year Ended June 30, 2002 (in millions) Balance at beginning of year\$10, 451 Net earnings4, 352 Dividends to shareholders(1, 971) Other decreases in retained earnings (852) Balance at end of year\$11, 980 15-41(45-60 min.)

For the solution, see the Prentice Hall Web site, www.prenhall.com/ 15-42(20 - 30 min.) The purpose of this game is to help students identify different types of implicit transactions. Usually implicit transactions are harder for students to understand than explicit transactions, and this game makes students identify and classify a large number of implicit transactions.

The game has an element of chance because of the roll of the die, and there is competition both within groups and between groups. The game will <https://assignbuster.com/basic-accounting-concepts-techniques-and-conventions-assignment/>

become more interesting and more challenging when the examples in the text have all been used and students must come up with their own examples. Students with experience in business will have an advantage in the competition, but it is also a good chance for students without such experience to learn from those with it. 15-43 (15-25 min.) NOTE TO INSTRUCTOR. This solution is based on the web site as it was in early 2004.

Be sure to examine the current web site before assigning this problem, as the information there may have changed. 1. McDonalds' largest asset is property and equipment, comprising about 78% of the company's assets. This and other assets such as inventories and prepaid expenses are unexpired costs. Accruals of unrecorded expenses include accrued interest, accrued restructuring and restaurant closing costs, and accrued payroll. 2. One measure of the size of a company is its total assets. McDonalds' total assets grew about 7%, from \$22. 5 billion to \$24. 0 billion. This is shown on the balance sheet. 3. McDonalds' sales grew about 3%, from \$14. billion to \$15. 4 billion. Meanwhile, net income fell from \$1. 6 billion to \$. 9 billion. It is not a good sign that income falls despite an increase in revenues. 4. Each of the basic financial statements includes clues that McDonalds is a corporation. Most obvious is that each statement is labeled " consolidated. " The Income Statement shows information about the earnings and dividends per share and the number of shares outstanding. The balance sheet reports Shareholder's Equity. The Statement of Shareholders' Equity shows why the amounts in the various shareholders' investment accounts on the balance sheet changed.

Finally, the Statement of Cash Flows reports treasury stock purchases and common stock dividends under the Financing Activities section. 5. Both the “Report of Independent Auditors” and the “Management Report” indicate that McDonalds’ financial statements comply with GAAP. The notes to the financial statements also make many references to GAAP standards. 6. McDonalds uses accrual accounting. This is evident from the inclusion of accounts such as prepaid expenses and accrued liabilities on the balance sheet.