

Key Ratios

10/10

- Working Capital

$$= \text{Current Assets} - \text{Current Liabilities}$$

- Current Ratios

$$= \frac{\text{Current assets}}{\text{Current Liabilities}}$$

- Quick Ratio

$$= \frac{(\text{Current assets} - \text{inventory + prepayments})}{\text{Current Liabilities}}$$

- Debt/Assets

$$= \frac{\text{Total debt}}{\text{Total assets}}$$

- Gross Profit Rate

$$= \frac{\text{gross profit}}{\text{Sales}}$$

- Profit Margin

$$= \frac{\text{Net profits}}{\text{Sales}}$$

② Receivables Turnover
= $\frac{\text{credit sales}}{\text{average accounts receivable}}$

Avg Collection Period
= $\frac{365}{\text{Receivables Turnover}}$

Did not study
-See where I mess up



MIT Sloan School of Management
15.501 Corporate Financial Accounting
Midterm Examination
October 8, 2008

NAME:

10/10 Practice

SECTION: (Circle one)

[A]

or

[B]

Instructions:

- 1) Exam Length: 1 hour and 20 minutes
- 2) This exam is 16 pages long (including the cover page). Please make sure your copy of the exam is not missing any pages.
- 3) A non-programmable calculator may be used during this exam. No other material is to be used during the exam.
- 4) Write your answers in the space provided and show any supporting computations you make. Do not attach additional material.
- 5) The total number of points on this exam is 130.

Manage your time efficiently.

Make sure to look through the entire exam before you start!

Question	Possible Points	Actual Points
1	36	
2	14	
3	24	
4	18	
5	18	
6	20	

Question 1

Instructions: Circle the letter corresponding to your response.

1. If a deterministic or stable selling price exists and a firm does not face substantial marketing or cash collection costs, when is revenue recognition most appropriate?

- a. At the time of sale
- b. At completion of production *right*
- c. At the time of cash collection
- d. At the expiration of returns and warranty periods

2. Trademarks would appear in which balance sheet section?

- a. Intangible assets *- can value + sell ??*
- b. Investments
- c. Property, plant, and equipment
- d. Current assets

3. The best definition of assets is the

- a. cash owned by the company.
- b. collection of resources belonging to the company and the claims on these resources.
- c. owners' investment in the business.
- d. resources belonging to a company that have future benefit to the company.

4. Jenner Corporation began the year with retained earnings of \$155,000. During the year, the company issued \$210,000 of common stock, recorded expenses of \$600,000, and paid dividends of \$40,000. If Jenner's ending retained earnings was \$165,000, what was the company's revenue for the year?

- a. \$610,000
- b. \$650,000
- c. \$820,000
- d. \$860,000

$$\begin{array}{r} 700 + 40 - 155 \\ \hline 640 - 155 \\ \hline 475 ? \end{array}$$

1

confused

$RE = \underline{-600} - 40 = 165$

$\underline{-640} = 165$

$\underline{-} = 805$

- does not add up

5. Which of the following items has no effect on retained earnings?

- a. Expense
- b. Dividends
- c. Land purchase
- d. Revenue

all do?

6. Are advanced receipts from customers treated as revenue at the time of receipt?

Why or why not?

- a. Yes, they are treated as revenue at the time of receipt because the company has access to the cash.
- b. No, the amount of revenue cannot be adequately determined until the company completes the work.
- c. Yes, the intent of the company is to perform the work and the customer is confident that the services will be completed.
- d. No, revenue cannot be recognized until the work is performed.

7. Based on the following data, what is the amount of current assets?

Accounts payable	31,000
Accounts receivable	<u>50,000</u>
Cash	<u>15,000</u>
Intangible assets	50,000
Inventory	<u>69,000</u>
Long-term investments	80,000
Long-term liabilities	100,000
Marketable securities	<u>40,000</u>
Notes payable	28,000
Plant assets	670,000
Prepaid expenses	<u>1,000</u>

also current

- a. \$96,000
- b. \$175,000
- c. \$106,000
- d. \$105,000

Never memorized all the ratios

8. Simpson Corporation has current assets of \$1,250,000 and current liabilities of \$750,000. If they pay \$250,000 of their accounts payable, what will their new current ratio be?

- a. 2.0:1
- b. 1.7:1
- c. 2.5:1
- d. 1.25:1

$$\begin{array}{r} \text{assets} \\ \hline \text{liabilities} \end{array} \quad \begin{array}{r} 1250 \\ 500 \end{array}$$

assets go down too!

$$\frac{1000}{500} = 2$$

- same as before payment

9. Blue Corporation issued a one-year 12% \$200,000 note on April 30, 2007. What was interest expense for the year ended December 31, 2007?

- a. \$24,000
- b. \$18,000
- c. \$16,000
- d. \$14,000

$$\begin{array}{r} 8 \text{ months} \\ (0\% - 20\%) \end{array}$$

$$200,000 \cdot .08$$

10. Employees at B Corporation are paid \$5,000 cash every Friday for working Monday through Friday. The calendar year accounting period ends on Wednesday, December 31. How much salary expense should be recorded two days later on January 2?

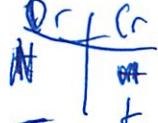
- a. \$5,000
- b. \$3,000
- c. None, matching requires the weekly salary to be accrued on December 31.
- d. \$2,000

11. One might infer from a debit balance in Allowance for Doubtful Accounts that:

- a. A posting error has been made.
- b. More accounts have been written off than had been estimated.
- c. The direct method is being used.
- d. Bad Debt Expense has been overestimated.

need to memorize which side is debt for credit

Use the test to take the test



12. The financial statements of the Colter Manufacturing Company report net sales of \$400,000 and accounts receivable of \$80,000 and \$40,000 at the beginning of the year and end of year, respectively. What is the average collection period for accounts receivable in days?

- a. 40
- b. 80
- c. 54.7
- d. 50

$$\frac{365}{\text{Rec. turn}} = \frac{365}{(\text{Credit sales}) / \text{Avg. AR}}$$

$$\begin{array}{r}
 365 \\
 \hline
 \left(\begin{array}{r}
 400,000 \\
 60,000
 \end{array} \right)
 \end{array}$$

This stuff is slow
- but know the detail!

Question 2

Joan Batenilli decides to open a pizza parlor near the local college campus. Analyze the following transactions for the month of June:

1. Joan Batenilli invests \$25,000 cash in exchange for common stock to start a pizza parlor business on June 1.
2. Purchased baking equipment for \$4,000 on June 2, paying \$2,000 in cash and with the remainder due in 60 days.
3. Purchased cooking supplies for \$1,200 cash on June 2. *Operating - oh COGS*
4. Paid a bill from Campus News for \$200 for advertising in the campus newspaper on June 15. *- I was thinking*
5. Billed the Tiger Football Team \$100 for pizzas ordered on June 30.
6. Joan Batenilli was paid dividends of \$800 on June 30.
7. ~~Incurred~~ utility expenses of \$200 for the month on account. *just incurred*
8. Over the month, cash receipts from customers for pizza sales amounted to \$1,500. *Ovens/investment (PPE)*
not paid
9. Over the month, paid salaries of \$200 to student workers.

Instructions:

Know which statement is which!

(Read carefully)

On the following page, prepare a statement of cash flows for Joan Batenilli's pizza parlor for the month of June.

Operating	$-200 - 200 + 1500 - 200 = 900 - 100$	
Investing	$-2,000 - 1200 =$	$-3,200 - 2000$
Financing	$25,000 - 800 =$	$24,200$
Net		$21900 \ 22100$
Old Cash	<hr/>	0
New Cash	<hr/>	$21900 \ 22100$

Question 3

Taylor Company accumulates the following adjustment data at December 31.

1. Depreciation of \$1,000 on equipment purchased in January.
2. Salaries of \$1,250 are unpaid.
3. Prepaid insurance totaling \$900 has expired.
4. Revenue of \$3,000 collected in advance has been earned.
5. Revenue of \$2,400 has been earned but unbilled.
6. Utility expenses of \$250 are unpaid.
7. Interest of \$500 on a note payable is outstanding for the year but unpaid.

Instructions:

A. Using the table on the following page, for each of the above items, indicate:

- (a.) The type of adjustment (prepaid expense, unearned revenue, accrued revenue, or accrued expense).
- (b.) The account relationship (asset/liability, liability/revenue, etc.)
- (c.) The status of account balances before adjustment (understatement or overstatement).
- (d.) The adjusting entry.
- (e.) The income effect.

B. Assume net income before the adjustments listed above was \$56,700. What is the adjusted net income?

broad cat here
Not just wanted
broad cat here -

narrow cat

Dr/Cr

Type of Adjustment	Account Relationship	Account Balances Before Adjustment (Understatement or Overstatement)	Adjusting Entry	Income Effect
1 Depreciation	Assets/Expenses	Over Under ✓ Depreciation is a found	Assets 1000 Accumulated depreciation 1000	0 -100
2 Accrued expenses	Liability/Expense	Under Under can be both	AP 1250 Salaries payable 1250	-1,250
3 Prepaid expenses	Prepaid Expenses/Asset	Over Under	Prepaid Ins 900 Retained Earnings 900	-900
4 Revenue of \$3,000 collected in advance has been earned.	Unearned Rev/Cash Liability	Under Under	Cash 3000 Unearned Revenue 3000	+3000 0 Revenue 3000

* missed
- had been
collected!

Type of Adjustment	Account Relationship	Account Balances Before Adjustment or Overstatement	Adjusting Entry	Income Effect
5 Revenue of \$2,400 has been earned but unbilled.	AR Accrued Revenue Asset	Retained Earnings Over Under	AR 2,400 Revenue	Retained Earnings 2,400 + 2,400
6 Utility expenses of \$250 are unpaid.	AP Accrued Expenses Liability	Retained Earnings Expense Under	AP 250 Utility Expense	Retained Earnings 250 -250
7 Interest of \$500 on a note payable is outstanding for the year but unpaid.	Accrued Interest Expense Liability	Retained Earnings Expense Under	AP 500 Interest Payable	Retained Earnings 500 -500

Each expense category

Separate

I also lump the payables

break
retained
earning into
Revenue / Expense

Question 4

Selected transactions for the Barkley Company are listed below.

1. Paid monthly utility bill.
2. Purchased new display case for cash.
3. Paid cash for repair work on security system.
4. Billed customers for services performed.
5. Received cash from customers billed in transaction 4.
6. Dividends paid to owners.
7. Incurred advertising expenses on account.
8. Paid monthly rent.
9. Received cash from customers when service was rendered.

Instructions:

Describe the effect of each transaction on assets, liabilities, and stockholders' equity. Provide your responses below.

Example: Made initial cash investment in the business.

Answer: Increase in assets and increase in stockholders' equity.

1. Decrease cash, decreased AP
- depends on when accrued
decrease retained earnings (expense) ✓
(stockholder's equity)
2. ↑ in PPE asset) no net change in assets
↓ in cash ↑ say explicitly here
3. ↓ in cash, ↓ in retained earnings / SE ✓
4. 'already performed' - just accrual here
↑ A P asset ↑ revenue/retained earnings / SE ✓
5. ↓ AP asset ↑ cash asset no net change in assets ✓

#9.

6. ↓ cash asset ↓ retained earnings /SE ↓

7. \uparrow AP (liability) \uparrow expenses / \downarrow re/SE \checkmark

8. 'I called now'
- same as 1, ✓

9. ∇cash $\nabla \text{Revenue/PRF/SE}$ ✓

just say stuff explicitly!

Question 5

Oh this is the Friday one

The Dolton Sign Company uses the allowance method in accounting for uncollectible accounts. Past experience indicates that 6% of accounts receivable will eventually be uncollectible. Selected account balances at December 31, 2006, and December 31, 2007, appear below:

	12/31/2006	12/31/2007
Net Credit Sales	\$400,000	\$500,000
Accounts Receivable	\$80,000	\$100,000
Allowance for Doubtful Accounts	\$4,000	?

Instructions:

A. Record the following events in 2007.

Aug 10 Determined that the account of Jack Dune for \$700 is uncollectible.

Allowance for Db. Accts	AR
700	700 V

Sept 21 Determined that the account of Lori Lyons for \$3,000 is uncollectible.

3000	3000 V
------	---

Oct 10 Received a check for \$400 as payment on account for Jack Dune, whose account had previously been written off as uncollectible.

AR 400	XA 1400 and 400	Cash 400	AR 400 400 always other side X
-----------	-----------------------	-------------	---

B. Prepare the adjusting journal entry to record the bad debt provision for the year ended December 31, 2007.

Allowance for Db. accounts	
2000	5,300
5,300	6000
6000	11

at this
pt XA
= \$1,300
700
- I was
not keeping track

Bad Debt Provision 8000	Bad Debt Expense 5,300
5,300	\$ 4,68,000
\$ 4,68,000	? Sub of retained earnings

write off
- but it's the
opposite of
a write off
- confused

AR
400 |

C. What is the balance of Allowance for Doubtful Accounts at December 31, 2007?

6000 ✓

D. What is the receivables turnover ratio for 2007?

$$\frac{\text{Sales}}{\text{Avg AR}} = \frac{500,000}{\cancel{40,000} \cancel{85000}} = \frac{50}{9} \quad \text{Since } \frac{80,000 - 4,000}{(80,000 - 6,000)} \text{ avg}$$

~~9) 50
45 5
45 0~~ C Wrong way of doing long division

- What am I thinking!

5.55

* remove allowance of doubtful accounts when calculating turnover ratio

Question 6

The following items are taken from the financial statements of Sutch Company for 2007:

Accounts payable	\$15,000
Accounts receivable	11,000
Accumulated Depreciation – Video Equipment	28,000
Advertising Expense	21,000
Cash	24,000
Common Stock	90,000
Depreciation Expense	12,000
Dividends	15,000
Insurance Expense	3,000
Note Payable (due 2010)	70,000
Prepaid Insurance	6,000
Rent Expense	17,000
Retained Earnings (beginning)	12,000
Salaries Expense	34,000
Salaries Payable	3,000
Service Revenue	145,000
Supplies	4,000
Supplies Expense	6,000
Video Equipment	210,000

Instructions:

A. On the following two pages, prepare an income statement and a classified balance sheet for Sutch Company for the period ending December 31, 2007. (Assume the note payable is a long-term liability.)

Income Statement

Revenue

Operating Expenses (list each out)

Other Expenses

~~Profit~~

~~Net
income~~

Balance Sheet

Stk Cash

:

Stk Asset

:

Lg Term Asset

etc

B. Compute the current ratio, debt to total assets ratio, and profit margin.

Ratio	Calculation	Answer
Current Ratio	$\frac{\text{Current Assets}}{\text{Liabilities}}$ ✓	
Debt/Assets Ratio	$\frac{\text{Total Liabilities}}{\text{Total Assets}}$ ✓ be more explicit	
Profit Margin	$\frac{\text{Revenue}}{\text{Net Income}}$ P	

Should be
fraction

 MIT Sloan School of Management 15.501 Corporate Financial Accounting Midterm Examination October 8, 2008	
NAME: _____	
SECTION: (Circle one)	
[A] or [B]	
<p>Instructions:</p> <p>1) Exam Length: 1 hour and 20 minutes This exam is 16 pages long (including the cover page). Please make sure your copy of the exam is not missing any pages.</p> <p>2) A non-programmable calculator may be used during this exam. No other material is to be used during the exam.</p> <p>3) Write your answers in the space provided and show any supporting computations you make. Do not attach additional material.</p> <p>4) The total number of points on this exam is 130.</p> <p><i>Manage your time efficiently.</i></p> <p><i>Make sure to look through the entire exam before you start!</i></p>	

Question 1

Instructions: Circle the letter corresponding to your response.

1. If a deterministic or stable selling price exists and a firm does not face substantial marketing or cash collection costs, when is revenue recognition most appropriate?
 - a. At the time of sale
 - b. At completion of production
 - c. At the time of cash collection
 - d. At the expiration of returns and warranty periods

2. Trademarks would appear in which balance sheet section?
 - a. Intangible assets
 - b. Investments
 - c. Property, plant, and equipment
 - d. Current assets

3. The best definition of assets is the
 - a. cash owned by the company.
 - b. collection of resources belonging to the company and the claims on these resources.
 - c. owners' investment in the business.
 - d. resources belonging to a company that have future benefit to the company.

4. Jenner Corporation began the year with retained earnings of \$155,000. During the year, the company issued \$210,000 of common stock, recorded expenses of \$600,000, and paid dividends of \$40,000. If Jenner's ending retained earnings was \$165,000, what was the company's revenue for the year?
 - a. \$610,000
 - b. \$650,000
 - c. \$820,000
 - d. \$860,000

Question	Possible Points	Actual Points
1	36	
2	14	
3	24	
4	18	
5	18	
6	20	

5. Which of the following items has no effect on retained earnings?

- Expense
- Dividends
- Land purchase
- Revenue

6. Are advanced receipts from customers treated as revenue at the time of receipt? Why or why not?

- Yes, they are treated as revenue at the time of receipt because the company has access to the cash.
- No, the amount of revenue cannot be adequately determined until the company completes the work.
- Yes, the intent of the company is to perform the work and the customer is confident that the services will be completed.
- No, revenue cannot be recognized until the work is performed.

7. Based on the following data, what is the amount of current assets?

Accounts payable	31,000
Accounts receivable	50,000
Cash	15,000
Intangible assets	50,000
Inventory	69,000
Long-term investments	80,000
Long-term liabilities	100,000
Marketable securities	40,000
Notes payable	28,000
Plant assets	670,000
Prepaid expenses	1,000

8. Simpson Corporation has current assets of \$1,250,000 and current liabilities of \$750,000. If they pay \$250,000 of their accounts payable, what will their new current ratio be?

- 2.0:1
- 1.7:1
- 2.5:1
- 1.25:1

9. Blue Corporation issued a one-year 12% \$200,000 note on April 30, 2007. What was interest expense for the year ended December 31, 2007?

- \$24,000
- \$18,000
- \$16,000
- \$14,000

10. Employees at B Corporation are paid \$5,000 cash every Friday for working Monday through Friday. The calendar year accounting period ends on Wednesday, December 31. How much salary expense should be recorded two days later on January 2?

- \$5,000
- \$3,000
- None, matching requires the weekly salary to be accrued on December 31.
- \$2,000

11. One might infer from a debit balance in Allowance for Doubtful Accounts that:

- A posting error has been made.
- More accounts have been written off than had been estimated.
- The direct method is being used.
- Bad Debt Expense has been overestimated.

12. The financial statements of the Colter Manufacturing Company report net sales of \$400,000 and accounts receivable of \$80,000 and \$40,000 at the beginning of the year and end of year, respectively. What is the average collection period for accounts receivable in days?

- a. 40
- b. 80
- c. 54.7
- d. 50

Question 2

Joan Batenilli decides to open a pizza parlor near the local college campus. Analyze the following transactions for the month of June:

1. Joan Batenilli invests \$25,000 cash in exchange for common stock to start a pizza parlor business on June 1.
2. Purchased baking equipment for \$4,000 on June 2, paying \$2,000 in cash and with the remainder due in 60 days.
3. Purchased cooking supplies for \$1,200 cash on June 2.
4. Paid a bill from Campus News for \$200 for advertising in the campus newspaper on June 15.
5. Billed the Tiger Football Team \$100 for pizzas ordered on June 30.
6. Joan Batenilli was paid dividends of \$800 on June 30.
7. Incurred utility expenses of \$200 for the month on account.
8. Over the month, cash receipts from customers for pizza sales amounted to \$1,500.
9. Over the month, paid salaries of \$200 to student workers.

Instructions:

On the following page, prepare a statement of cash flows for Joan Batenilli's pizza parlor for the month of June.

Joan Batenilli's Pizza Parlor

Statement of Cash Flows

For the month of June

OPERATING ACTIVITIES

Additions:

Receipts from customers, 1,500

Subtractions:

Payment for cooking supplies, (1,200)

Payment for advertising, (200)

Payment for salaries, (200)

Net cash provided by operating activities: (100)

INVESTING ACTIVITIES

Payment for baking equipment, (2,000)

Net cash provided by investing activities: (2,000)

FINANCING ACTIVITIES

Issuance of common stock, 25,000

Payment of dividend, (800)

Net cash provided by financing activities: 24,200

Net increase in cash: 22,100

Question 3

Taylor Company accumulates the following adjustment data at December 31.

1. Depreciation of \$1,000 on equipment purchased in January.
2. Salaries of \$1,250 are unpaid.
3. Prepaid insurance totaling \$900 has expired.
4. Revenue of \$3,000 collected in advance has been earned.
5. Revenue of \$2,400 has been earned but unbilled.
6. Utility expenses of \$250 are unpaid.
7. Interest of \$500 on a note payable is outstanding for the year but unpaid.

Instructions:

A. Using the table on the following page, for each of the above items, indicate:

- (a.) The type of adjustment (prepaid expense, unearned revenue, accrued revenue, or accrued expense).
- (b.) The account relationship (asset/liability, liability/revenue, etc.)
- (c.) The status of account balances before adjustment (understatement or overstatement).
- (d.) The adjusting entry.
- (e.) The income effect.

B. Assume net income before the adjustments listed above was \$56,700. What is the adjusted net income?

			Account Balances (Understatement or Overstatement)		
	Type of Adjustment	Account Relationship		Adjusting Entry	Income Effect
1	Depreciation of \$1,000 on equipment purchased in January	Prepaid expense	Assets: Overstated	Debit Depreciation Expense 1,000 Credit Accumulated Depreciation 1,000	(1,000)
2	Salaries of \$1,250 are unpaid.	Accrued expense	Liability/Expense Understated	Debit Wage Expense 1,250 Credit Salaries Payable 1,250	(1,250)
3	Prepaid insurance totalling \$900 has expired.	Prepaid expense	Assets: Overstated	Debit Insurance Expense 900 Credit Prepaid Insurance 900	(900)
4	Revenue of \$3,000 collected in advance has been earned.	Unearned revenue	Liability/Revenue Overstated	Debit Unearned Revenue 3,000 Credit Revenue 3,000	+3,000

			Account Balances (Understatement or Overstatement)		
	Type of Adjustment	Account Relationship		Adjusting Entry	Income Effect
5	Revenue of \$2,400 has been earned but unearned.	Accrued revenue	Assets: Understated	Debit Accounts Receivable 2,400 Credit Revenue 2,400	+2,400
6	Utility expenses of \$250 are unpaid.	Accrued expense	Liability/Expense Understated	Debit Utility Expense 250 Credit Accounts Payable 250	(250)
7	Interest of \$50 on a note payable is outstanding for the year but unpaid.	Accrued expense	Liability/Expense Understated	Debit Interest Expense 50 Credit Interest Payable 50	(50)

ADJUSTED NET INCOME:

$$56,700 - 1,000 - 1,250 - 900 + 3,000 + 2,400 - 250 - 50 = \$58,200$$

Question 4

Selected transactions for the Barkley Company are listed below.

1. Paid monthly utility bill.
2. Purchased new display case for cash.
3. Paid cash for repair work on security system.
4. Billed customers for services performed.
5. Received cash from customers billed in transaction 4.
6. Dividends paid to owners.
7. Incurred advertising expenses on account.
8. Paid monthly rent.
9. Received cash from customers when service was rendered.

Instructions:

Describe the effect of each transaction on assets, liabilities, and stockholders' equity. Provide your responses below.

Example: Made initial cash investment in the business.

Answer: Increase in assets and increase in stockholders' equity.

1. Decrease in assets and decrease in stockholders' equity.

2. No net change in assets.

3. Decrease in assets and decrease in stockholders' equity.

4. Increase in assets and increase in stockholders' equity.

5. No net change in assets.

6. Decrease in assets and decrease in stockholders' equity.

7. Increase in liabilities and decrease in stockholders' equity.

8. Decrease in assets and decrease in stockholders' equity.

9. Increase in assets and increase in stockholders' equity.

Question 5

The Dolton Sign Company uses the allowance method in accounting for uncollectible accounts. Past experience indicates that 6% of accounts receivable will eventually be uncollectible. Selected account balances at December 31, 2006, and December 31, 2007, appear below:

	12/31/2006	12/31/2007
Net Credit Sales	\$400,000	\$500,000
Accounts Receivable	\$80,000	\$100,000
Allowance for Doubtful Accounts	\$4,000	?

Instructions:

- A. Record the following events in 2007.

Aug 10 Determined that the account of Jack Dune for \$700 is uncollectible.

Dr Allowance for Doubtful Accounts 700

Cr Accounts Receivable – Jack Dune 700

Sept 21 Determined that the account of Lori Lyons for \$3,000 is uncollectible.

Dr Allowance for Doubtful Accounts 3,000

Cr Accounts Receivable – Lori Lyons 3,000

Oct 10 Received a check for \$400 as payment on account for Jack Dune, whose account had previously been written off as uncollectible.

Dr Accounts Receivable – Jack Dune 400

Cr Allowance for Doubtful Accounts 400

Dr Cash 400

Cr Accounts Receivable – Jack Dune 400

B. Prepare the adjusting journal entry to record the bad debt provision for the year ended December 31, 2007.

Question 6
The following items are taken from the financial statements of Sutch Company for 2007:

Accounts payable	\$15,000
Accounts receivable	11,000
Accumulated Depreciation – Video Equipment	28,000
Advertising Expense	21,000
Cash	24,000
Common Stock	90,000
Depreciation Expense	12,000
Dividends	15,000
Insurance Expense	3,000
Note Payable (due 2010)	70,000
Prepaid Insurance	6,000
Rent Expense	17,000
Retained Earnings (beginning)	12,000
Salaries Expense	34,000
Salaries Payable	3,000
Service Revenue	145,000
Supplies	4,000
Supplies Expense	6,000
Video Equipment	210,000

Instructions:

D. What is the receivables turnover ratio for 2007?

The receivables turnover ratio is Net Credit Sales / Average Net Receivables

From above, Net Credit Sales for 2007 is 500,000

Average Net Receivables is $\frac{1}{2} \times [(80,000 - 4,000) + (100,000 - 6,000)]$, which is 85,000

So $500,000 / 85,000 = 5.88$

SUTCH COMPANY
INCOME STATEMENT FOR THE PERIOD ENDING DECEMBER 31, 2007

Service Revenue	\$145,000
Less:	
Insurance Expense	(3,000)
Supplies Expense	(6,000)
Rent Expense	(17,000)
Advertising Expense	(21,000)
Salaries Expense	(34,000)
Depreciation Expense	(12,000)
Net Income:	\$52,000

B. Compute the current ratio, debt to total assets ratio, and profit margin.

Ratio	Calculation	Answer
Current Ratio	Current Assets / Current Liabilities 45,000 / 18,000	2.5
Debt/Assets Ratio	Total Liabilities / Total Assets 88,000 / 227,000	38.8%
Profit Margin	Net Income / Total Sales 52,000 / 145,000	35.9%

SUTCH COMPANY
BALANCE SHEET FOR DECEMBER 31, 2007

ASSETS		LIABILITIES AND STOCKHOLDERS' EQUITY	
<u>Current Assets</u>		<u>Current Liabilities</u>	
Cash	24,000	Accounts payable	15,000
Accounts receivable	11,000	Salaries payable	3,000
Prepaid Insurance	6,000	Total Current Liabilities	18,000
Supplies	4,000	<u>Non-current Liabilities</u>	
		Note Payable (due 2010)	70,000
<u>Total current assets</u>	45,000	Total Non-current Liabilities	70,000
<u>Non-current assets</u>			
Video Equipment	210,000	<u>Total Liabilities:</u>	88,000
(Accumulated Depreciation ... Video Equipment)	(28,000)		
		<u>Stockholders' Equity</u>	
<i>Total non-current assets</i>	<i>182,000</i>	Common Stock	50,000
		Retained Earnings	49,000
Total:	227,000	Total Stockholders' Equity:	139,000



MIT Sloan School of Management
15.501 Corporate Financial Accounting
Midterm Examination
October 14, 2009

NAME:

SECTION: (Circle one)

[A]

or

[B]

10/11 Practice

Instructions:

- 1) Exam Length: 1 hour and 20 minutes
- 2) This exam is 16 pages long (including the cover page). Please make sure your copy of the exam is not missing any pages.
- 3) A non-programmable calculator may be used during this exam. No other material is to be used during the exam.
- 4) Write your answers in the space provided and show any supporting computations you make. Do not attach additional material.
- 5) The total number of points on this exam is 80.

Manage your time efficiently.

Make sure to look through the entire exam before you start!

Question	Possible Points	Actual Points
1	8	
2	10	
3	13	
4	9	
5	10	
6	12	
7	18	

Question 1 (8 points)

Instructions: Circle the letter corresponding to your response.

1. Manuel's Tune-Up Shop follows the revenue recognition principle. Javier services a car on August 31. The customer picks up the vehicle on September 1 and mails the payment to Manuel on September 5. Manuel receives the check in the mail on September 6. When should Manuel show that the revenue was earned?
 - a. August 31
 - b. August 1
 - c. September 5
 - d. September 6
2. A furniture factory's employees work overtime to finish an order that is sold on January 31. The office sends a statement to the customer in early February and payment is received by mid-February. The overtime wages should be expensed in:
 - a. January.
 - b. February.
 - c. the period when the workers receive their checks.
 - d. either January or February depending on when the pay period ends.
3. Which of the following reflect the balances of prepayment accounts prior to adjustment?
 - a. Balance sheet accounts are understated and income statement accounts are under-stated.
 - b. Balance sheet accounts are overstated and income statement accounts are over-stated.
 - c. Balance sheet accounts are overstated and income statement accounts are under-stated.
 - d. Balance sheet accounts are understated and income statement accounts are over-stated.

income over
'I don't really get it'
'it has to be paid'
oh prior to adjustment

does not make sense
or
income
- balance sheet

4. The general term employed to indicate an expense that has not been paid or revenue that has not been received and has not yet been recognized in the accounts is:

- a. contra asset.
- b. prepayment.
- c. asset.
- d. accrual.

5. Waterfalls Corporation purchased a one-year insurance policy in January 2009 for \$60,000. The insurance policy is in effect from March 2009 through February 2010. If the company neglects to make the proper year-end adjustment for the expired insurance:

- a. net income and assets will be understated by \$50,000
- b. net income and assets will be overstated by \$50,000
- c. net income and assets will be understated by \$10,000
- d. net income and assets will be overstated by \$10,000

6. After aging the accounts receivable for recording bad debts expense, estimated uncollectible accounts are \$25,000. If the balance of the Allowance for Doubtful Accounts is \$8,000 debit before adjustment what is the balance after adjustment?

- a. \$25,000
- b. \$8,000
- c. \$33,000
- d. \$17,000

a. \$25,000	Bal 80 00	Dr Cr
	<u> </u>	<u> </u>
	33,000	

7. Henson Company began the year with retained earnings of \$175,000. During the year, the company recorded revenues of \$250,000, expenses of \$190,000, and paid dividends of \$20,000. What was Henson's retained earnings at the end of the year?

- a. \$255,000
- b. \$215,000
- c. \$405,000
- d. \$235,000

$$\begin{aligned}175 + 250 - 190 - 20 &= \\175 + 60 - 20 &= \\175 + 40 &= \\215 &= \end{aligned}$$

Current assets

8. Use the following data to determine the total amount of working capital.

Koonce Office Supplies			
Balance Sheet			
31-Dec-10			
Cash	\$65,000	Accounts Payable	\$70,000
Prepaid Insurance	30,000	Salaries Payable	10,000
Accounts Receivable	50,000	Mortgage Payable	<u>80,000</u>
Inventory	70,000	Total Liabilities	\$160,000
Trademark	70,000		
Land held for Investment	75,000	Common Stock	\$120,000
Land	90,000	Retained Earnings	<u>250,000</u>
Building	80,000		
		Total Stockholders' Equity	<u>\$370,000</u>
		Total Liabilities and Stockholders' Equity	\$530,000
Total Assets	\$530,000		

a. \$135,000.

b. \$295,000. ✓

c. \$205,000.

d. \$125,000.

65 + 30 + 50 + 70

180 ~~24~~

215

'1 or no ins',
or - liabilities?
current

215 - 80

208 - 65

4 158 - 15
135

Question 2 (10 points)

Instructions: Match the items below in the space provided.

A. Aging the accounts receivable	F. Accrued revenues
B. Dividends	G. Direct write-off method
C. Revenue recognition principle	H. Assets
D. Prepaid expenses	I. Accrued expenses
E. Matching principle	J. Working capital

✓ <u>J</u>	1. The excess of current assets over current liabilities.
✓ <u>D</u>	2. Expenses paid before they are incurred
✓ <u>G</u>	3. Bad debt losses are not estimated and no allowance account is used.
✓ <u>H</u>	4. Future economic benefits.
✓ <u>AE</u>	5. Efforts are related to accomplishments <i>match expenses to revenue</i>
✓ <u>A</u>	6. Analysis of customer account balances by length of time they have been unpaid.
✓ <u>CF</u>	7. Revenue is recognized when earned
✓ <u>F</u>	8. Revenues earned but not yet received
✓ <u>I</u>	9. Expenses incurred but not yet paid
✓ <u>B</u>	10. Distributions of cash from a corporation to its stock holders.

Question 3 (13 points)

Milius Corporation began operations on January 1, 2009. The firm's cash account revealed the following transactions for the month of January:

Date	Transaction	Amount
<i>Cash Receipts</i>		
Jan. 1	Investment by John Milius for common stock	\$ 35,000
Jan. 1	Loan from Upper Valley Bank, due June 30, 2009, with 6% annual interest	\$ 40,000
Jan. 15	Advance from a customer for merchandise scheduled for delivery in February, 2009	\$ 1,200
Jan. 1-31	Sales to customers	\$ 60,000
<i>Cash Disbursements</i>		
Jan. 1	Rental of retail space at a monthly rental of \$3,000	\$ (6,000)
Jan. 1	Premium on property and liability insurance for coverage from January 1 to December 31, 2009	\$ (1,200)
Jan. 19	Payment of utility bills	\$ (750)
Jan. 23	Payment of salaries	\$ (3,500)
Jan. 1-31	Purchase of merchandise	\$ (44,800)
<i>Balance, January 31, 2009</i>		\$ 79,950

The following information relates to Milius Corporation as of January 31, 2009.

- (1) Customers owe the firm \$9,500 from sales made during January.
- (2) The firm owes suppliers \$3,900 for merchandise purchased during January.
- (3) Unpaid utility bills total \$260, and unpaid salaries total \$1,260.
- (4) Merchandise inventory on hand totals \$5,500.

make SWP
use

Instructions:

- (a) Using the space allotted on the following pages, prepare an income statement for January, assuming that Milius Corporation uses a cash basis of accounting.
- (b) Using the space allotted on the following pages, prepare an income statement for January, assuming that Milius Corporation uses the accrual basis of accounting.

way we learned more

Income Statement (Period)
Revenue

— ; Each expenses

Net Income

Note adjustments

(a)

Revenue 60,000 + 1200

Expenses

Rent 6,000

Insurance 1,200

Utilities 750

Salaries 3,500

COGS 44,800

Total 56,250

~~Net~~ Net Income ~~3,750~~ 4,450

+ adjustments (read carefully)

(b)

Revenue 60,000 + 9,500

Expenses

Loan Interest 200

Rent 3,000

Ins 1,800

Utility 750 + 260

Salaries 3,500 + 1260

COGS 44,800 + 3,900 - 5,580

Total 52160 52070

Net Income 7850 17,230

Question 4 (9 points)

Skynet commences business on September 1, 2000. It pays the one-year insurance premium of \$3,600 for property and liability protection on this date. On September 1, 2001, it renews the insurance policy and pays a \$4,800 one-year insurance premium. Skynet's accounting period ends December 31 of each year. Assuming that Skynet uses the accrual basis of accounting, use T-accounts, journal entries, or the Balance Sheet Equation to show the entries it will record on September 1 and December 31 of both 2000 and 2001.

Sept 1 2000	<u>Prepaid Ins</u>	<u>Cash</u>
	3600	3600
Dec 31 2000		✓ start this for

Ins Expenses	Retained Earnings
1200	1200

for year

Sept 1 2001	<u>Ins Expenses</u>	<u>Retained Earnings</u>
	2400	2400
	Prepaid Ins	Cash
	1800	4800

Dec 31 2001

Ins Expenses	Retained Earnings
2400	2400
1600	1600

Skynet borrows \$250,000 on October 1, 2008. The debt carries an annual interest rate of 6% and is payable in two installments, on April 1 and October 1 of each year. The debt matures on October 1, 2012. Skynet's accounting period ends on December 31 of each year. Assuming that Skynet uses the accrual basis of accounting, use T-accounts, journal entries, or the Balance Sheet Equation to show how it will record the annual interest expense for 2008.

Interest Payable		Interest on Notes Payable	Expense
Liabilities			
15,825		15,825	
↑ always other side	15,825	3,750	
but I thought	15,825	Expense	
Liabilities Dr Cr	-		
+ 3750			
		+ guess I should write both broad + specific categories	

$$\begin{aligned}
 &\cancel{2,500 \text{ / year}} \\
 &\cancel{5,208 \text{ / monthly}} \\
 &\text{duh } 6\% \text{ annual interest} \\
 &\frac{3}{12} \cdot 6\% \\
 &1.5\% \cdot 250,000 \\
 &= 3,750
 \end{aligned}$$

Skynet makes sales on account during 2009 totaling \$126,900. Collections from customers from sales on account during 2009 total \$94,300. Skynet uses the allowance method for uncollectible accounts, and estimates that it will ultimately not collect 4% of sales on account. During 2009, the firm ~~wrote off~~ \$2,200 of accounts receivable as uncollectible. If the Allowance for Uncollectible Accounts has a credit balance of \$1,320 on December 31, 2008, what amount of Bad Debt Expense will Skynet recognize in 2009, and what will be the balance of the Allowance for Uncollectible Accounts on December 31, 2009?

$$4\% = 5,076$$

Allowance for Bad Debt Expense	
	±
2200	1320 Bal
	5,076
	4,196 Bal

Question 5 (10 points)

Instructions: Analyze the transactions described below and indicate their effect on the basic accounting equation. Use a plus sign (+) to indicate an increase and a minus sign (-) to indicate a decrease.

	Assets	=	Liabilities	+	Stockholders' Equity	
1. Received cash for services rendered.	+ 0		- 0		+ 0	$\bigcirc = \text{no change}$
2. Purchased office equipment on credit.	+ 0		+ 0		0	
3. Paid employees' salaries.	- 0		0		- 0	✓
4. Received cash from customer in payment on account.	+/- 0		0		0	
5. Paid telephone bill for the month.	- 0		0		- 0	✓
6. Paid for office equipment purchased in transaction 2.	- 0		+ 0	- 0	0	
7. Purchased office supplies on credit.	+ 0		- 0	+ 0	0	
8. Dividends were paid.	- 0		0		- 0	
9. Obtained a loan from the bank.	+ 0		+ 0		0	
10. Billed customers for services rendered.	+ 0		+ 0		+ 0	can both be +?

Services accrued here!

So for most part I know
 - its just what assumption are they making
 and read everything
 One real mistake \rightarrow D.

Question 6 (12 points)

here we go again
on this!

The financial statements of Omni Consumer Products reveal the following for four recent years (amounts in millions):

	2005	2006	2007	2008	
Credit sales	5181	6137	6713	7292	
Total Sales	\$8,330	\$9,456	\$10,035	\$10,615	
Credit Sales/Total Sales	62.2%	64.9%	66.9%	68.7%	
Bad Debt Expense	\$57	\$64	\$82	\$96	
	2004	2005	2006	2007	2008
Accounts Receivable, Gross	\$1,592	\$2,099	\$2,223	\$2,456	\$2,607
Less Allowance for Uncollectible Accounts	(\$47)	(\$61)	(\$66)	(\$84)	(\$99)
Accounts Receivable, Net	\$1,545	\$2,038	\$2,157	\$2,372	\$2,508

Instructions:

- Compute the amount of accounts written off as uncollectible during 2005, 2006, 2007, and 2008 and enter it in the space below. (Use the space on the following page to show your work.)
- Compute the amount of cash collections from credit customers during 2005, 2006, 2007, and 2008 and enter it in the space below. (Use the space on the following page to show your work.)
- Calculate the accounts receivable turnover ratio for 2005, 2006, 2007, and 2008 and enter it in the space below. (Use the space on the following page to show your work.)

	2005	2006	2007	2008
<i>Write-offs</i>	43 ✓	59 ✓	64 ✓	81 ✓
<i>Cash collections</i>				
<i>Accounts receivable turnover ratio</i>	1.35 1.30	1.35	1.34	1.34

Credit Sales
A.A.R

Should avg
start + end

Allowance = $\frac{\text{last year's allowance}}{\text{A.A.R}}$ + bad debt expense

- Write off

I shall do
a f system!

$$\text{Writeoffs} = \left(\begin{array}{l} \text{last year} \\ \text{allowance} \end{array} \right) + \text{bad debt} - \text{current allowance}$$

+
-
+
-

~~flip signs~~

$$\text{Writeoff} = -\text{last years} - \text{bad debt} + \text{current allowance}$$

allowance expense

- - 47 - 57 + 61

= 51

$$= -\text{last year} + \text{bad debt} + \text{current}$$

-- + + -

$$= 47 + 57 - 61 \quad \text{✓}$$

= 43

Q1 Cash collection

$$\text{last years AR} + \text{current years sales} - \text{writeoff} + \text{end of year AR}$$

total credit

This page is intentionally left blank

↑
why not
total sales

- says from credit
customers

Avg AQ I did wrong

~~both down side~~

~~credit~~

oh I flipped
in calculator

even though I wrote
correct answer on
paper

- I like this basic
calc I have
to use

Question 7 (18 points)

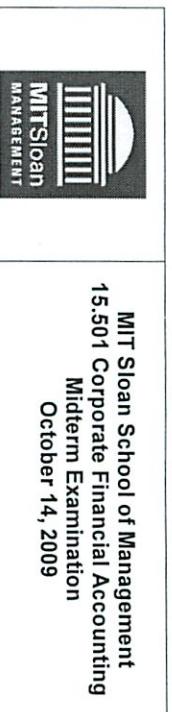
Tyrell Corporation begins operations on January 1, 2008. That same day, Rick Deckard invests \$50,000 for common stock of the firm, and the firm borrows \$40,000 from a local bank. The firm must repay the loan with interest for both 2008 and 2009 on December 31, 2009. The interest rate is 10% per year. The firm purchases a building for \$60,000 cash for its operations. On March 31, the firm decides to launch a marketing campaign and prepays \$36,000 for 12 months of advertising (beginning immediately).

During 2008, the firm makes cash sales to clients totaling \$52,900 and sales on account totaling \$116,100. Of the sales on account, the firm collects \$54,800 by December 31, 2008. The firm incurs and pays other costs as follows: salaries, \$34,200; utilities, \$2,600. It has unpaid bills at the end of 2008 as follows: salaries, \$2,400; utilities, \$180. Ignore taxes.

Instructions:

- (a) Using the space allotted on the following pages, prepare an income statement for Tyrell Corporation for 2008, assuming that the firm uses the accrual basis of accounting and recognizes revenue at the time of sale.
- (b) Using the space allotted on the following pages, prepare a balance sheet for Tyrell Corporation as of December 31, 2008. Show supporting computations for each balance sheet item.

just know what goes under each entry
& read carefully!



NAME: _____

SUGGESTED SOLUTIONS

SECTION: (Circle one)

[A] or [B]

Instructions:

- 1) Exam length: 1 hour and 20 minutes
- 2) This exam is 16 pages long (including the cover page). Please make sure your copy of the exam is not missing any pages.
- 3) A non-programmable calculator may be used during this exam. No other material is to be used during the exam.
- 4) Write your answers in the space provided and show any supporting computations you make. Do not attach additional material.
- 5) The total number of points on this exam is 80.

Manage your time efficiently.

Make sure to look through the entire exam before you start!

Question	Possible Points	Actual Points
1	8	
2	10	
3	13	
4	9	
5	10	
6	12	
7	18	

Question 1 (8 points)

Instructions: Circle the letter corresponding to your response.

1. Manuel's Tune-Up Shop follows the revenue recognition principle. Javier services a car on August 31. The customer picks up the vehicle on September 1 and mails the payment to Manuel on September 5. Manuel receives the check in the mail on September 6. When should Manuel show that the revenue was earned?
 - a. August 31
 - b. August 1
 - c. September 5
 - d. September 6
2. A furniture factory's employees work overtime to finish an order that is sold on January 31. The office sends a statement to the customer in early February and payment is received by mid-February. The overtime wages should be expensed in:
 - a. January.
 - b. February.
 - c. the period when the workers receive their checks.
 - d. either January or February depending on when the pay period ends.
3. Which of the following reflect the balances of prepayment accounts prior to adjustment?
 - a. Balance sheet accounts are understated and income statement accounts are under-stated.
 - b. Balance sheet accounts are overstated and income statement accounts are over-stated.
 - c. Balance sheet accounts are overstated and income statement accounts are under-stated.
 - d. Balance sheet accounts are understated and income statement accounts are over-stated.

4.

The general term employed to indicate an expense that has not been paid or revenue that has not been received and has not yet been recognized in the accounts is:

- a. contra asset.
- b. prepayment.
- c. asset.
- d. accrual.

5.

Waterfalls Corporation purchased a one-year insurance policy in January 2009 for \$60,000. The insurance policy is in effect from March 2009 through February 2010. If the company neglects to make the proper year-end adjustment for the expired insurance:

- a. net income and assets will be understated by \$50,000
- b. net income and assets will be overstated by \$50,000
- c. net income and assets will be understated by \$10,000
- d. net income and assets will be overstated by \$10,000

6.

After aging the accounts receivable for recording bad debts expense, estimated uncollectible accounts are \$25,000. If the balance of the Allowance for Doubtful Accounts is \$8,000 debit before adjustment what is the balance after adjustment?

- a. \$25,000
- b. \$8,000
- c. \$33,000
- d. \$17,000

7. Henson Company began the year with retained earnings of \$175,000. During the year, the company recorded revenues of \$250,000, expenses of \$190,000, and paid dividends of \$20,000. What was Henson's retained earnings at the end of the year?

- a. \$255,000
- b. \$215,000
- c. \$405,000
- d. \$235,000

8.

Use the following data to determine the total amount of working capital.

Koounce Office Supplies		
Balance Sheet		
31-Dec-10		
Cash	\$65,000	Accounts Payable
Prepaid Insurance	30,000	Salaries Payable
Accounts Receivable	50,000	Mortgage Payable
Inventory	70,000	Total Liabilities
Trademark	70,000	\$80,000
Land held for Investment	75,000	Common Stock
Land	90,000	Retained Earnings
Building	80,000	Total Stockholders' Equity
		\$250,000
		\$370,000
Total Assets	\$530,000	Total Liabilities and Stockholders' Equity
		\$530,000

Question 2 (10 points)

Instructions: Match the items below in the space provided.

A.	Aging the accounts receivable	F.	Accrued revenues
B.	Dividends	G.	Direct write-off method
C.	Revenue recognition principle	H.	Assets
D.	Prepaid expenses	I.	Accrued expenses
E.	Matching principle	J.	Working capital
J.	1.	The excess of current assets over current liabilities.	
D.	2.	Expenses paid before they are incurred	
G.	3.	Bad debt losses are not estimated and no allowance account is used.	
H.	4.	Future economic benefits.	
E.	5.	Efforts are related to accomplishments	
A.	6.	Analysis of customer account balances by length of time they have been unpaid.	
C.	7.	Revenue is recognized when earned	
F.	8.	Revenues earned but not yet received	
I.	9.	Expenses incurred but not yet paid	
B.	10.	Distributions of cash from a corporation to its stock holders.	

Question 3 (13 points)

Millius Corporation began operations on January 1, 2009. The firm's cash account revealed the following transactions for the month of January:

Date	Transaction	Amount
<i>Cash Receipts</i>		
Jan. 1	Investment by John Millius, for common stock	\$ 35,000
Jan. 1	Loan from Upper Valley Bank, due June 30, 2009, with 6% annual interest	\$ 40,000
Jan. 15	Advance from a customer for merchandise scheduled for delivery in February, 2009	\$ 1,200
Jan. 1-31	Sales to customers	\$ 60,000
<i>Cash Disbursements</i>		
Jan. 1	Rental of retail space at a monthly rental of \$3,000	\$ (6,000)
Jan. 1	Premium on property and liability insurance for coverage from January 1 to December 31, 2009	\$ (1,200)
Jan. 19	Payment of utility bills	\$ (750)
Jan. 23	Payment of salaries	\$ (3,500)
Jan. 31	Purchase of merchandise	\$ (44,800)
<i>Balance, January 31, 2009</i>		\$ 79,950

The following information relates to Millius Corporation as of January 31, 2009:

- (1) Customers owe the firm \$9,500 from sales made during January.
- (2) The firm owes suppliers \$3,900 for merchandise purchased during January.
- (3) Unpaid utility bills total \$260, and unpaid salaries total \$1,260.
- (4) Merchandise inventory on hand totals \$5,500.

Instructions:

- (a) Using the space allotted on the following pages, prepare an income statement for January, assuming that Millius Corporation uses a cash basis of accounting.
- (b) Using the space allotted on the following pages, prepare an income statement for January, assuming that Millius Corporation uses the accrual basis of accounting.

Question 4 (9 points)

SkyNet commences business on September 1, 2000. It pays the one-year insurance premium of \$3,600 for property and liability protection on this date. On September 1, 2001, it renews the insurance policy and pays a \$4,800 one-year insurance premium. SkyNet's accounting period ends December 31 of each year. Assuming that SkyNet uses the accrual basis of accounting, use T-accounts, journal entries, or the Balance Sheet Equation to show the entries it will record on September 1 and December 31 of both 2000 and 2001.

September 1, 2000:

Dr Prepaid Insurance, \$3,600
Cr Cash, \$3,600

December 31, 2000:

Dr Insurance Expense, \$1,200 (4 mths @ \$300/mth)
Cr Prepaid Insurance, \$1,200

September 1, 2001:

Dr Prepaid Insurance, \$4,800
Cr Cash, \$4,800

December 31, 2001:

Dr Insurance Expense, \$4,000 (8 mths @ \$300/mth, 4 mths @ \$400/mth)
Cr Prepaid Insurance, \$4,000

SkyNet borrows \$250,000 on October 1, 2008. The debt carries an annual interest rate of 6% and is payable in two installments, on April 1 and October 1 of each year. The debt matures on October 1, 2012. SkyNet's accounting period ends on December 31 of each year. Assuming that SkyNet uses the accrual basis of accounting, use T-accounts, journal entries, or the Balance Sheet Equation to show how it will record the annual interest expense for 2008.

$$\$250,000 \times 6\% \times 3/12 = \$3,750$$

Dr Interest Expense, \$3,750
Cr Interest Payable, \$3,750

SkyNet makes sales on account during 2009 totaling \$125,900. Collections from customers from sales on account during 2009 total \$94,300. SkyNet uses the allowance method for uncollectible accounts and estimates that it will ultimately not collect 4% of sales on account. During 2009, the firm wrote off \$2,200 of accounts receivable as uncollectible. If the Allowance for Uncollectible Accounts has a credit balance of \$1,320 on December 31, 2008, what amount of Bad Debt Expense will SkyNet recognize in 2009, and what will be the balance of the Allowance for Uncollectible Accounts on December 31, 2009?

SkyNet will have a bad debt expense of $4\% \times 125,900 = \$5,076$

To get the ending balance of the Allowance for Uncollectible Accounts:
Beginning Balance + Bad Debt Expense - Write-offs = Ending Balance
 $\$1,320 + \$5,076 - \$2,200 = \$4,196$

	(a.) Cash Basis	(b.) Accrual Basis
Sales Revenue	\$64,200 ^a	\$69,500 ^b
Less Expenses:		
Cost of Merchandise Sold	(\$44,800)	(\$43,200) ^c
Payments on Merchandise Purchased	(\$750)	(\$1,010) ^d
Utilities Expense	(\$3,500)	(\$4,760) ^e
Salaries Expense	(\$5,000)	(\$3,000)
Rent Expense	(\$1,200)	(\$100) ^f
Insurance Expense	(\$56,250)	(\$52,270)
Interest Expense	(\$52,270)	(\$52,270)
Total Expenses	\$4,950	\$17,230
Net Income (Loss)	\$4,950	\$17,230

Question 5 (10 points)

Instructions: Analyze the transactions described below and indicate their effect on the basic accounting equation. Use a plus sign (+) to indicate an increase and a minus sign (-) to indicate a decrease.

	Assets	Liabilities	Shareholders' Equity					
1	Received cash for services rendered.	(+)	(+)					
2	Purchased office equipment on credit.	(+)	(+)					
3	Paid employees' salaries.	(-)	(-)					
4	Received cash from customer in payment on account.	(+)/(+)	(-)					
5	Paid telephone bill for the month.	(-)	(-)					
6	Paid for office equipment purchased in transaction 2.	(-)	(-)					
7	Purchased office supplies on credit.	(+)	(+)					
8	Dividends were paid.	(-)	(-)					
9	Obtained a loan from the bank.	(+)	(+)					
10	Billed customers for services rendered.	(+)	(+)					

Question 6 (12 points)

The financial statements of Omni Consumer Products reveal the following for four recent years (amounts in millions):

	2005	2006	2007	2008
Total Sales	\$8,330	\$9,456	\$10,035	\$10,615
Credit Sales/Total Sales	62.2%	64.9%	66.9%	68.7%
Bad Debt Expense	\$57	\$64	\$82	\$96
	2004	2005	2006	2007
Accounts Receivable, Gross	\$1,592	\$2,099	\$2,223	\$2,456
Less Allowance for Uncollectible Accounts	(\$47)	(\$61)	(\$66)	(\$84)
Accounts Receivable, Net	\$1,545	\$2,038	\$2,157	\$2,372
				\$2,508

Instructions:

- Compute the amount of accounts written off as uncollectible during 2005, 2006, 2007, and 2008 and enter it in the space below. (Use the space on the following page to show your work.)
- Compute the amount of cash collections from credit customers during 2005, 2006, 2007, and 2008 and enter it in the space below. (Use the space on the following page to show your work.)
- Calculate the accounts receivable turnover ratio for 2005, 2006, 2007, and 2008 and enter it in the space below. (Use the space on the following page to show your work.)

	2005	2006	2007	2008
Write-offs	\$43	\$59	\$64	\$81
Cash collections	\$4,631	\$5,954	\$6,416	\$7,061
Accounts receivable turnover ratio	2.89	2.93	2.96	2.99

Write-Offs = Beginning ADA + Bad Debt Expense – Ending ADA

$$2005: 47 + 57 - 61 = 43$$

$$2006: 61 + 64 - 65 = 59$$

$$2007: 66 + 82 - 84 = 64$$

$$2008: 84 + 96 - 99 = 81$$

Cash collections = Beginning A/R (Gross) – Write-Offs + Credit Sales

– Ending A/R (Gross)

$$2005: 1,592 - 43 + 5,181 - 2,099 = 4,631$$

$$2006: 2,099 - 59 + 6,137 - 2,223 = 5,954$$

$$2007: 2,223 - 64 + 6,713 - 2,456 = 6,416$$

$$2008: 2,456 - 81 + 7,293 - 2,607 = 7,061$$

Accounts Receivable Turnover Ratio is “computed by dividing net credit sales (net sales less cash sales) by the average net accounts receivables during the year” (Kimmel, Weygandt, and Kieso, p. 388)

$$2005: 5,181 / [0.5 * (1,545 + 2,038)] = 2.89$$

$$2006: 6,137 / [0.5 * (2,038 + 2,157)] = 2.93$$

$$2007: 6,713 / [0.5 * (2,157 + 2,372)] = 2.96$$

$$2008: 7,293 / [0.5 * (2,372 + 2,508)] = 2.99$$

Ignore taxes.

During 2008, the firm makes cash sales to clients totaling \$2,900 and sales on account totaling \$116,100. Of the sales on account, the firm collects \$54,800 by December 31, 2008. The firm incurs and pays other costs as follows: salaries, \$34,200; utilities, \$2,600. It has unpaid bills at the end of 2008 as follows: salaries, \$2,400; utilities, \$180.

Ignore taxes.

Instructions:

- (a) Using the space allotted on the following pages, prepare an income statement for Tyrell Corporation for 2008, assuming that the firm uses the accrual basis of accounting and recognizes revenue at the time of sale.
- (b) Using the space allotted on the following pages, prepare a balance sheet for Tyrell Corporation as of December 31, 2008. Show supporting computations for each balance sheet item.

Question 7 (18 points)

Tyrell Corporation begins operations on January 1, 2008. That same day, Rick Deckard invests \$50,000 for common stock of the firm, and the firm borrows \$40,000 from a local bank. The firm must repay the loan with interest for both 2008 and 2009 on December 31, 2009. The interest rate is 10% per year. The firm purchases a building for \$60,000 cash for its operations. On March 31, the firm decides to launch a marketing campaign and prepays \$36,000 for 12 months of advertising (beginning immediately).

(a)

Tyrell Corporation Income Statement for the Year Ending 12/31/2008	
Sales Revenue	\$169,000
Less Expenses:	
Interest Expense	(\$4,000)
Advertising Expense	(\$27,000)
Salaries Expense	(\$36,600)
Utilities Expense	(\$2,780)
Total Expenses	(\$70,380)
Net Income	\$58,620

(b)

Tyrell Corporation Balance Sheet as of 12/31/2008	
Current Assets	
Cash	\$64,900
Accounts receivable	\$61,300
Prepaid advertising	\$9,000
Noncurrent Assets	
P&E	\$60,000
Total Assets	\$195,200
Current Liabilities	
Note payable	\$40,000
Interest payable	\$4,000
Salaries payable	\$2,400
Utilities payable	\$180
Shareholders' Equity	
Common stock	\$50,000
Retained earnings	\$93,620
Total Equities	\$195,200



MIT Sloan School of Management
15.501 Corporate Financial Accounting
Midterm Examination
October 13, 2010

NAME: Michael Plasencia

SECTION: (Circle one)

[A] (1:00pm-2:30pm)

or

[B] (2:30pm-4:00pm)

Instructions:

- 1) Exam Length: 1 hour and 20 minutes
- 2) This exam is 10 pages long (including the cover page). Please make sure your copy of the exam is not missing any pages.
- 3) A non-programmable calculator may be used during this exam. No other material is to be used during the exam.
- 4) Write your answers in the space provided and show any supporting computations you make. Do not attach additional material.
- 5) The last two pages can be detached if convenient.
- 6) The total number of points on this exam is 100.

Manage your time efficiently.

Make sure to look through the entire exam before you start!

Question	Possible Points	Actual Points
1	18	12
2	15	11
3	20	20
4	30	28
5	7	7
6	10	7

85

Question 1 (18 points)

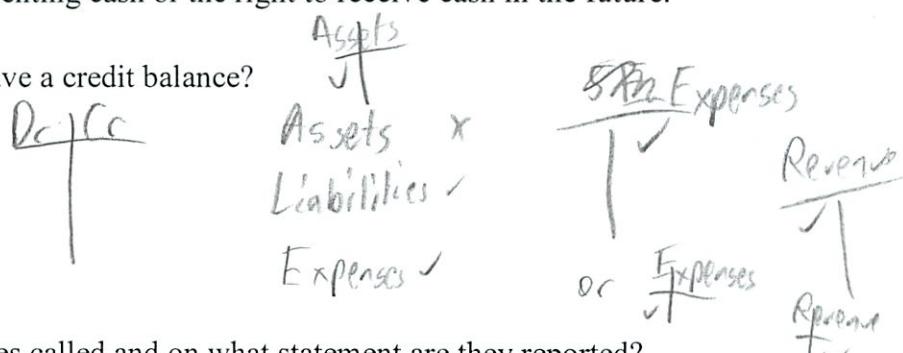
Required: Circle the letter corresponding to your response.

1. The nature of an asset is best described as:

- a. a resource owned by the company that is expected to provide the company future economic benefits.
- b. something with physical form that is valued at cost in the accounting records.
- c. something owned by a business that has a ready market value.
- d. an economic resource representing cash or the right to receive cash in the future.

2. Which account types normally have a credit balance?

- a. Revenues
- b. Liabilities
- c. Expenses
- d. Both a and b

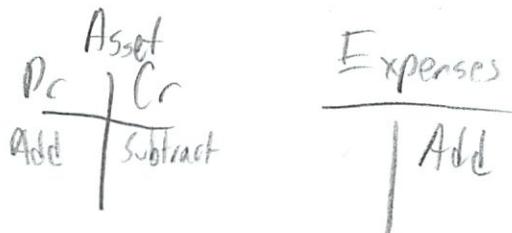


3. What are probable future sacrifices called and on what statement are they reported?

- a. Losses on the income statement $Current$
- b. Stockholders' equity on the balance sheet
- c. Dividends on the statement of stockholders' equity
- d. Liabilities on the balance sheet $Must$

4. Details, Inc., purchased supplies for \$1,300 during 2010. At year end Details had \$800 of supplies left. The adjusting entry should

- a. debit Supplies \$800
- b. credit Supplies \$800 $both in 1$
- c. debit Supplies \$500 1
- d. debit Supplies expense \$500 1



5. Harrigan Company, a small consulting firm, charges all of its operating expenses on Accounts Payable. On January 1, 2010, Harrigan's Accounts Payable balance was \$3,000 and, during the year, \$27,000 of additional operating expenses was charged on account. The ending Accounts Payable balance was \$9,000. What is the amount of cash paid for expenses during 2010?

- a. \$33,000
- b. \$30,000
- c. \$21,000
- d. \$18,000

$$\begin{aligned} 3 + 27 - x &= 9 \\ 30 - x &= 9 \\ -x &= -21 \end{aligned}$$

6. Assets are recorded in the balance sheet in order of

- a. Market value
- b. Historic value
- c. Liquidity
- d. Maturity

7. From the following list of accounts, calculate the quick ratio. (Rounded to nearest tenth.)

Cash.....	\$6,000	Accounts payable.....	\$10,000
Marketable securities.....	3,000	Salary payable.....	4,000
Accounts receivable.....	9,000	Notes payable (due in two years)....	13,000
Inventory.....	11,000		
Prepaid insurance.....	1,000		

- a. 1.3
- b. 2.1
- c. 1.1
- d. 1.8

Current Assets - Inventory - Prepaid
Current Liability

$6+3+9$
10+4

Only Ratio qv

8. The following ratios are available for Leer Inc. and Stable Inc.

	Current Ratio	Debt to Assets Ratio	Earnings per Share
Leer Inc.	2	75%	\$3.50
Stable Inc	1.5	40%	\$2.75

Compared to Stable Inc., Leer Inc. has:

- a. Higher liquidity, higher solvency, and higher profitability.
- b. Lower liquidity, higher solvency, and higher profitability.
- c. Higher liquidity, lower solvency, and higher profitability.
- d. Higher liquidity and lower solvency, but profitability cannot be compared based on information provided.

9. Maxwell Industries recorded and paid \$900 advertising for the current month. Which occurred?

- a. Current assets increase.
- b. Gross profit decreases.
- c. Operating income decreases.
- d. Retained earnings increases.

Question 2 (15 points)

B - for investment purposes ?
C - for operational purposes?

Instructions: In the blank space beside each numbered balance sheet item, enter the letter of its balance sheet classification.

A. Current assets	E. Current liabilities
B. Long-term investments	F. Long-term liabilities
C. Long-term assets	G. Equity
D. Intangible assets	H. Should not appear on the balance sheet

C 1. Machine

A 2. Inventory

C 3. Land *for operations* B - land for investment

G 4. Common stock

C 5. Building *for operations* B - building for operations

E 6. Income taxes payable in 30 days

E 7. Utilities payable

A 8. Note receivable due in 30 days *like if they loaned they will collect*

~~E~~ 9. Wages expense *wages accrued* *come out of Shareholder's equity* G

~~E~~ 10. Security deposit *prepaid revenue* *can't book*

~~E~~ 11. Value of company logo *revenue - so owe the company the money*

A 12. Cash

~~E~~ 13. Value of land in excess of cost *- depends on manager's policy*

F 14. Mortgage payable *far in the future*

A 15. Accounts receivable

Question 3 (20 points)

Period = quarter 4 2011

After accounting for bad debt expense and write-offs for the first three quarters, Image Communications' September 30, 2011, records show these account balances:

Accounts Receivable.....	\$260,000
Allowance for Doubtful Accounts.....	(8,100)

During the year, Image Communications estimates doubtful-account expense at 0.5% of credit sales. Credit sales in the final quarter (October through December) amount to \$340,000.

At year-end, the company ages its receivables and adjusts the balance in Allowance for Doubtful Accounts to correspond to the aging schedule. This schedule is as follows:

Accounts Receivable	Age of Accounts			
	1-30 Days	31-60 Days	61-90 Days	Over 90 Days
\$230,000	\$160,000	\$35,000	\$14,000	\$21,000
Estimated percent uncollectible	0.2%	1%	5%	30%

During the last quarter of 2011, the company completed the following selected transactions:

28-Dec Wrote off as uncollectible the \$1,500 account receivable from Blue Carpets and the \$400 account receivable from Show-N-Tell Antiques

31-Dec Adjusted the Allowance for Doubtful Accounts and recorded doubtful-account expense at year-end, based on the aging of receivables.

Required:

1. Record the December 28 and December 31 transactions using journal entries.
2. Prepare a T-account for Allowance for Doubtful Accounts and post to that account.

Asset	Revenue	Expense
+	+	+
XA	11	11
+		

Question 3 (20 points)

Required: Write your answer in the space below.

Dec 31 Qu Allowances

Cr Allowance for Doubtful Accts
\$1,700

Dr Bad Debt Expense
\$1,700

Dec 28 Write off

Dr 1,900 Allowance Doubtful
Accts

Cr 1,900 Accounts Receivable

Dec 31 Adjustments

Dr Allowance for Doubtful Accts
\$230

Cr Bad Debt Expens
\$230

Guess could do both Dec 31
at once

Dr Cr

Allowance for Doubtful Accounts XA	
1,900	8,100 Bal
	1,700
adjustment 230	7900 Bal
	7670

Accounts Receivable A

Bal 260,000	1,900
340,000	Collection?
Bal 598,100	

Bad Debt Expense A4

Bal 0	230
1,700	
Bal 1470	

3. Did not really memorize
had to reconstruct
took a while

Question 4 (30 points)

Mark Davis formed a lawn service company as a summer job. To start the business on May 1, he deposited \$2,000 in a new bank account in the name of the corporation. The \$2,000 consisted of a \$1,600 loan from his father and \$400 of his own money. The corporation issued 200 shares of common stock to Davis.

Davis rented lawn equipment, purchased supplies, and hired high school students to mow and trim his customers' lawns. At the end of each month, Davis mailed bills to his customers. On August 31, Davis was ready to dissolve the business and return to the local university. Because he had been so busy, he had kept few records other than his checkbook and a list of accounts owed by customers.

At August 31, Davis' checkbook shows a balance of \$2,040, and his customers still owe him \$600. During the summer, he collected \$5,600 from customers. His checkbook lists payments for supplies totaling \$400, and he still has gasoline, gardening gloves, and other supplies that cost a total of \$50. He paid his employees wages of \$1,900, and he still owes them \$200 for the final week of the summer.

Davis rented some equipment from Ludwig Tool Company. On May 1, he signed a six-month lease on mowers and paid \$600 for the full lease period. Ludwig will refund the unused portion of the prepayment if the equipment is in good shape. To get the refund, Davis has kept the mowers in excellent condition. In fact, he had to pay \$300 to repair a mower that ran over a hidden tree stump. He has not yet returned the mowers, however.

To transport employees and equipment to jobs, Davis used a trailer that he bought for \$300. He figures that the summer's work used up one-third of the trailer's service potential. The business checkbook lists dividends paid to Davis during the summer of \$460. Also, Davis paid his father back during the summer.

do not need to fully journalize

Required:

1. Prepare the income statement of Davis Lawn Service, Inc., for the four months May through August. The business is not subject to income tax.
2. Prepare the classified balance sheet of Davis Law Service, Inc., at August 31.

\$400 SE - 200 shares

\$1600 Loan

Aug 31 Cash - \$2040
AR = 600

Revenue = \$600 + ~~2000~~ + 600 - 2000

GOEs = 400 expense

Inventory = \$50 asset

Wages - 1900 + 200

200 - Salaries payable

Mowers expense \$400

Mowers prepay \$200

Repairs \$300

Trailer \$300

- Depreciation \$100

Repay loan \$1,600

Dividends \$460

Take rusty

out as
much practice
as record
as value
- depreciation

Question 4 (30 points)

Required: Write your answer in the space below.

Income Statement May - Aug

Revenue	\$ 6200
Expenses	
COGS	\$ 350
Wages	\$ 2100
Lease Mowers	\$ 400
Repairs	\$ 300
Depreciation	\$ 100
Total	<u>\$ 3350</u>
Net Income	2,950 ✓

Balance Sheet Aug 31

Assets

Cash	\$ 2040
Accounts Receivable	\$ 600
Supplies	\$ 50
Prepaid Lease	\$ 1200
current	<u>\$ 2,890</u>

Trailer \$ 1200
Total Assets \$ 3090

Liabilities

Salaries Payable \$ 200

Shareholders' Equity

Contributed \$ 400

Retained \$ 2950

~~Dividends~~ - \$ 460

Total Liabilities

+ Equity \$ 3090

-2

✓ Balances

Question 5 (7 points)

J&J Snack Foods Corp manufactures and markets foods and frozen beverages to the food service and supermarket industries. The 2009 annual report includes the following information:

15 years
We sell equipment service contracts with terms of coverage ranging between 12 and 60 months. We record deferred income on equipment service contracts which is amortized by the straight-line method over the term of the contracts.

In 2009, J&J Snack Foods Corp sold \$16,745,000 in service contracts related to frozen beverage machines. At September 26, 2009 and September 27, 2008, deferred income on service contracts of \$1,334,000 and \$986,000, respectively, were included in short-term liabilities, and deferred income on service contracts of \$90,000 and \$144,000 were included in other long-term liabilities, respectively.

Required:

What is the amount of service contract income recorded in 2009? Show any supporting calculations, and enter your answer in the box provided below.

$$\text{Income in 09} = 08 \text{ short term} + \left(\frac{09}{08} \text{ Sales} + 08 \text{ Long term} \right) - 09 \text{ short term} \\ - 09 \text{ long term}$$

$$968 + 16,745 + 144 - 1,334 - 98 \quad \checkmark$$

$$16,433,000$$

Answer:

$$16,433,000$$

Seems way too high

08 short \rightarrow 09

08 long \rightarrow 09-14

09 short \rightarrow 10

09 long \rightarrow 11-15

09 Sales \rightarrow 09-14

$$09 \text{ long} - 09 \text{ short} - 08 \text{ long}$$

fairly

Or am I doing this wrong
But what else to do?

Question 6 (10 points)

The following items and amounts are taken from the 2011 financial records of Hopkins Inc.:

Security deposit.....	\$3,200	Salaries payable.....	\$6,000
Equipment.....	29,000	Common stock.....	10,500
Salaries expense.....	42,000	Supplies expense.....	4,700
Utilities expense.....	1,100	Retained earnings, Jan. 1, 2011.....	12,000
Dividends.....	7,600 5,800	Insurance expense.....	2,200
Accounts payable.....	7,600	Service revenue.....	75,000
Cash.....	9,900	Repair expense.....	4,500
✓ Accounts receivable.....	9,500		

Instructions:

Prepare a balance sheet for Hopkins Inc. for the year ending December 31, 2011.

Assets

Cash	9,900) Short term
Accounts Receivable	9,500	
Equipment	29,000	long term
Security Deposit	3,200	
Total Assets	51,600	

Salaries Payable	6,000	✓
Accounts Payable	7,600	
Total	13,600	

Shareholders' Equity

Contributed	10,500
-------------	--------

Earned



Retained Earnings

Carryover \$112,000

Revenue 75,000

Expenses

Salaries 42,000

Supplies 4,700

Repair 4,900

Insurance 2,200

Utilities 1,100

Total Expenses 54,500

Total Retained Earnings \$32,500

Dividends - \$5,000

Total Equity 38,000

Total Liabilities + Equity = 51,600

✓ Matches

-3



MIT Sloan School of Management
15.501 Corporate Financial Accounting
Midterm Examination
October 13, 2010

SUGGESTED SOLUTIONS

NAME: _____

SECTION: (Circle one)

[A] (1:00pm-2:30pm)

or

[B] (2:30pm-4:00pm)

Instructions:

- 1) Exam Length: 1 hour and 20 minutes
- 2) This exam is 10 pages long (including the cover page). Please make sure your copy of the exam is not missing any pages.
- 3) A non-programmable calculator may be used during this exam. No other material is to be used during the exam.
- 4) Write your answers in the space provided *and show any supporting computations you make*. Do not attach additional material.
- 5) The last two pages can be detached if convenient.
- 6) The total number of points on this exam is 100.

Manage your time efficiently.

Make sure to look through the entire exam before you start!

Question	Possible Points	Actual Points
1	18	
2	15	
3	20	
4	30	
5	7	
6	10	

Question 1 (18 points)

Required: Circle the letter corresponding to your response.

1. The nature of an asset is best described as:
 - a. a resource owned by the company that is expected to provide the company future economic benefits.
 - b. something with physical form that is valued at cost in the accounting records.
 - c. something owned by a business that has a ready market value.
 - d. an economic resource representing cash or the right to receive cash in the future.

2. Which account types normally have a credit balance?
 - a. Revenues
 - b. Liabilities
 - c. Expenses
 - d. Both a and b

3. What are probable future sacrifices called and on what statement are they reported?
 - a. Losses on the income statement
 - b. Stockholders' equity on the balance sheet
 - c. Dividends on the statement of stockholders' equity
 - d. Liabilities on the balance sheet

4. Details, Inc., purchased supplies for \$1,300 during 2010. At year end Details had \$800 of supplies left. The adjusting entry should
 - a. debit Supplies \$800
 - b. credit Supplies \$800
 - c. debit Supplies \$500
 - d. debit Supplies expense \$500

5. Harrigan Company, a small consulting firm, charges all of its operating expenses on Accounts Payable. On January 1, 2010, Harrigan's Accounts Payable balance was \$3,000 and, during the year, \$27,000 of additional operating expenses was charged on account. The ending Accounts Payable balance was \$9,000. What is the amount of cash paid for expenses during 2010?
 - a. \$33,000
 - b. \$30,000
 - c. \$21,000
 - d. \$18,000

6. Assets are recorded in the balance sheet in order of

- a. Market value
- b. Historic value
- c. Liquidity
- d. Maturity

7. From the following list of accounts, calculate the quick ratio. (Rounded to nearest tenth.)

Cash.....	\$6,000	Accounts payable.....	\$10,000
Marketable securities.....	3,000	Salary payable.....	4,000
Accounts receivable.....	9,000	Notes payable (due in two years)....	13,000
Inventory.....	11,000		
Prepaid insurance.....	1,000		

- a. 1.3
- b. 2.1
- c. 1.1
- d. 1.8

8. The following ratios are available for Leer Inc. and Stable Inc.

	Current Ratio	Debt to Assets Ratio	Earnings per Share
Leer Inc.	2	75%	\$3.50
Stable Inc	1.5	40%	\$2.75

Compared to Stable Inc., Leer Inc. has:

- a. Higher liquidity, higher solvency, and higher profitability.
- b. Lower liquidity, higher solvency, and higher profitability.
- c. Higher liquidity, lower solvency, and higher profitability.
- d. Higher liquidity and lower solvency, but profitability cannot be compared based on information provided.

9. Maxwell Industries recorded and paid \$900 advertising for the current month. Which occurred?

- a. Current assets increase.
- b. Gross profit decreases.
- c. Operating income decreases.
- d. Retained earnings increases.

Question 2 (15 points)

Instructions: In the blank space beside each numbered balance sheet item, enter the letter of its balance sheet classification.

A. Current assets	E. Current liabilities
B. Long-term investments	F. Long-term liabilities
C. Long-term assets	G. Equity
D. Intangible assets	H. Should not appear on the balance sheet

C 1. Machine

A 2. Inventory

C 3. Land

G 4. Common stock

C 5. Building

E 6. Income taxes payable in 30 days

E 7. Utilities payable

A 8. Note receivable due in 30 days

H 9. Wages expense

A 10. Security deposit

H 11. Value of company logo

A 12. Cash

H 13. Value of land in excess of cost

F 14. Mortgage payable

A 15. Accounts receivable

Question 3 (20 points)

After accounting for bad debt expense and write-offs for the first three quarters, Image Communications' September 30, 2011, records show these account balances:

Accounts Receivable.....	\$260,000
Allowance for Doubtful Accounts.....	(8,100)

During the year, Image Communications estimates doubtful-account expense at 0.5% of credit sales. Credit sales in the final quarter (October through December) amount to \$340,000.

At year-end, the company ages its receivables and adjusts the balance in Allowance for Doubtful Accounts to correspond to the aging schedule. This schedule is as follows:

Accounts Receivable	Age of Accounts			
	1-30 Days	31-60 Days	61-90 Days	Over 90 Days
\$230,000	\$160,000	\$35,000	\$14,000	\$21,000
Estimated percent uncollectible	0.2%	1%	5%	30%

During the last quarter of 2011, the company completed the following selected transactions:

28-Dec	Wrote off as uncollectible the \$1,500 account receivable from Blue Carpets and the \$400 account receivable from Show-N-Tell Antiques
31-Dec	Adjusted the Allowance for Doubtful Accounts and recorded doubtful-account expense at year-end, based on the aging of receivables.

Required:

1. Record the December 28 and December 31 transactions using journal entries.

The allowance has a (credit) balance of \$8,100 on October 1st. Image Communications debits bad debt expense \$1,700 and credits the allowance \$1,700 based on 0.5% of credit sales. Before the December 28th write-offs, the (credit) balance is \$9,800.

Dec-28: Dr Allowance for doubtful accounts, \$1,900 Cr Accounts Receivable—Blue Carpets, \$1,500 Cr Accounts Receivable—Show-N-Tell, \$400
--

After these write-offs, the allowance will have a (credit) balance of \$7,900.

The aging of accounts receivable yields the following:

Accounts Receivable	Age of Accounts			
	1-30 Days	31-60 Days	61-90 Days	Over 90 Days
\$230,000	\$160,000	\$35,000	\$14,000	\$21,000
Estimated percent uncollectible	0.2%	1%	5%	30%
Based on aging:	\$320	\$350	\$700	\$6,300

So the ending balance for the allowance should be $\$320 + \$350 + \$700 + \$6,300 = \$7,670$.

The bad debt expense based on percentage of sales on account has been too high. To get the ending (credit) balance in the allowance for doubtful accounts, bad debt expense should be lowered:

**Dec-31: Dr Allowance for doubtful accounts, \$230
Cr Bad debt expense, \$230**

2. Prepare a T-account for Allowance for Doubtful Accounts and post to that account.

Allowance for doubtful accounts		
	\$ 8,100	<i>1-Oct</i>
	1,700	<i>Oct-Dec</i>
<i>28-Dec</i>	<i>\$ 1,500</i>	
<i>28-Dec</i>	<i>400</i>	
<i>31-Dec</i>	<i>230</i>	
	\$ 7,670	<i>Ending</i>

Question 4 (30 points)

Mark Davis formed a lawn service company as a summer job. To start the business on May 1, he deposited \$2,000 in a new bank account in the name of the corporation. The \$2,000 consisted of a \$1,600 loan from his father and \$400 of his own money. The corporation issued 200 shares of common stock to Davis.

Davis rented lawn equipment, purchased supplies, and hired high school students to mow and trim his customers' lawns. At the end of each month, Davis mailed bills to his customers. On August 31, Davis was ready to dissolve the business and return to the local university. Because he had been so busy, he had kept few records other than his checkbook and a list of accounts owed by customers.

At August 31, Davis' checkbook shows a balance of \$2,040, and his customers still owe him \$600. During the summer, he collected \$5,600 from customers. His checkbook lists payments for supplies totaling \$400, and he still has gasoline, gardening gloves, and other supplies that cost a total of \$50. He paid his employees wages of \$1,900, and he still owes them \$200 for the final week of the summer.

Davis rented some equipment from Ludwig Tool Company. On May 1, he signed a six-month lease on mowers and paid \$600 for the full lease period. Ludwig will refund the unused portion of the prepayment if the equipment is in good shape. To get the refund, Davis has kept the mowers in excellent condition. In fact, he had to pay \$300 to repair a mower that ran over a hidden tree stump. He has not yet returned the mowers, however.

To transport employees and equipment to jobs, Davis used a trailer that he bought for \$300. He figures that the summer's work used up one-third of the trailer's service potential. The business checkbook lists dividends paid to Davis during the summer of \$460. Also, Davis paid his father back during the summer.

Required:

1. Prepare the income statement of Davis Lawn Service, Inc., for the four months May through August. The business is not subject to income tax.
2. Prepare the classified balance sheet of Davis Law Service, Inc., at August 31.

To start the business on May 1, he deposited \$2,000 in a new bank account in the name of the corporation. The \$2,000 consisted of a \$1,600 loan from his father and \$400 of his own money.

	Cash	Loan payable	Common stock
[1]	\$2,000	\$1,600 [1]	\$400 [1]

At August 31, Davis' checkbook shows a balance of \$2,040, and his customers still owe him \$600.

Cash		Accounts receivable	
[1]	\$2,000		
[EB]	\$2,040	[EB]	\$600

At the end of each month, Davis mailed bills to his customers. [...] During the summer, he collected \$5,600 from customers.

Cash		Accounts receivable		Revenues	
[1]	\$2,000				
[3]	\$5,600	[2]	\$6,200		
[EB]	\$2,040	[EB]	\$600	\$5,600 [3]	\$6,200 [2]

His checkbook lists payments for supplies totaling \$400, and he still has gasoline, gardening gloves, and other supplies that cost a total of \$50.

Cash		Supplies		Supplies expense	
[1]	\$2,000	[4]	\$400		
[3]	\$5,600			\$350 [5]	
[EB]	\$2,040	\$400 [4]	[EB]	\$50	[5] \$350

He paid his employees wages of \$1,900, and he still owes them \$200 for the final week of the summer.

Cash		Wage expense		Wages payable	
[1]	\$2,000				
[3]	\$5,600	\$400 [4]	[6]	\$2,100	
		\$1,900 [6]			
[EB]	\$2,040				\$200 [EB]

On May 1, he signed a six-month lease on mowers and paid \$600 for the full lease period. Ludwig will refund the unused portion of the prepayment if the equipment is in good shape. To get the refund, Davis has kept the mowers in excellent condition. In fact, he had to pay \$300 to repair a mower that ran over a hidden tree stump. He has not yet returned the mowers, however.

Cash	
[1]	\$2,000
[3]	\$5,600
	\$400 [4]
	\$1,900 [6]
	\$600 [7]
	\$300 [9]
[EB]	\$2,040

Prepaid lease		Lease expense		Repair expense	
[7]	\$600	\$400	[8]	[8]	\$400
[EB]	\$200			[9]	\$300

To transport employees and equipment to jobs, Davis used a trailer that he bought for \$300. He figures that the summer's work used up one-third of the trailer's service potential.

Equipment--Trailer		Trailer expense	
[10]	\$300	[11]	\$100
[EB]	\$200		

Cash	
[1]	\$2,000
[3]	\$5,600
	\$400 [4]
	\$1,900 [6]
	\$600 [7]
	\$300 [9]
	\$300 [10]
[EB]	\$2,040

NOTE: We have not covered depreciation for long-lived assets yet, so I'm treating the trailer as a current asset (like tools, perhaps) instead of PP&E.

The business checkbook lists dividends paid to Davis during the summer of \$460. Also, Davis paid his father back during the summer.

Loan payable		Dividends		
[13]	\$1,600	\$1,600 [1]	[12]	\$460
		\$0 [EB]		

The work thus far can be checked. If you sum the credit entries to the cash account, you find you have credited cash for \$5,560. Since you collected \$5,600 and raised \$2,000 at the outset, the net cash inflow is \$2,040, which is what the checkbook says.

The income statement can be prepared as follows:

Income statement for Davis' Lawn Service Company Summer ended Aug 31 st	
Revenues	<u>\$6,200</u>
Expenses:	
Wage expense	\$2,100
Lease expense	400
Supplies expense	350
Repair expense	300
Trailer expense	100
Total expenses:	<u>\$3,250</u>
Net income	<u>\$2,950</u>

Ending retained earnings will be \$2,950 less dividends of \$460, or \$2,490.

Balance sheet for Davis' Lawn Service Company as of Aug 31 st			
Cash	\$ 2,040	Wages payable	\$ 200
Accounts receivable	600	Total liabilities:	<u>\$ 200</u>
Supplies	50		
Prepaid lease	200	Common stock	\$ 400
Equipment--Trailer	<u>200</u>	Retained earnings	<u>2,490</u>
		Total equity:	<u>\$ 2,890</u>
Total assets:	<u>\$ 3,090</u>	Total liabilities + equity	<u>\$ 3,090</u>

Question 5 (7 points)

J&J Snack Foods Corp manufactures and markets foods and frozen beverages to the food service and supermarket industries. The 2009 annual report includes the following information:

We sell equipment service contracts with terms of coverage ranging between 12 and 60 months. We record deferred income on equipment service contracts which is amortized by the straight-line method over the term of the contracts.

In 2009, J&J Snack Foods Corp sold \$16,745,000 in service contracts related to frozen beverage machines. At September 26, 2009 and September 27, 2008, deferred income on service contracts of \$1,334,000 and \$986,000, respectively, were included in short-term liabilities, and deferred income on service contracts of \$90,000 and \$144,000 were included in other long-term liabilities, respectively.

Required:

What is the amount of service contract income recorded in 2009? Show any supporting calculations, and enter your answer in the box provided below.

Beginning balance for unearned service contract income: $986,000 + 144,000 = \$1,130,000$

Ending balance for unearned service contract income: $1,334,000 + 90,000 = \$1,424,000$

Beginning Balance + Additions – Subtractions = Ending Balance

Entering the data you have:

$$1,130,000 + 16,745,000 - \text{Service contract income} = 1,424,000$$

After arithmetic:

$$\text{Service contract income} = \$16,451,000$$

Answer:

\$16,451,000

Question 6 (10 points)

The following items and amounts are taken from the 2011 financial records of Hopkins Inc.:

Security deposit.....	\$3,200	Salaries payable.....	\$6,000
Equipment.....	29,000	Common stock.....	10,500
Salaries expense.....	42,000	Supplies expense.....	4,700
Utilities expense.....	1,100	Retained earnings, Jan. 1, 2011.....	12,000
Dividends.....	5,000	Insurance expense.....	2,200
Accounts payable.....	7,600	Service revenue.....	75,000
Cash.....	9,900	Repair expense.....	4,500
Accounts receivable.....	9,500		

Instructions:

Prepare a balance sheet for Hopkins Inc. for the year ending December 31, 2011.

First, calculate the net income:

Service revenue.....	<u>\$ 75,000</u>
Salaries expense.....	(42,000)
Repair expense.....	(4,500)
Supplies expense.....	(4,700)
Insurance expense.....	(2,200)
Utilities expense.....	(1,100)
	<u>\$ 20,500</u>

Calculate ending retained earnings balance:

$$\begin{aligned} \text{Beginning balance} + \text{Net income} - \text{Dividends} &= \text{Ending balance} \\ 12,000 + 20,500 - 5,000 &= \$27,500 \end{aligned}$$

Then, prepare the balance sheet:

Hopkins Inc.'s Balance Sheet as of December 31, 2011			
Cash.....	\$ 9,900	Accounts payable.....	\$ 7,600
Accounts receivable.....	9,500	Salaries payable.....	6,000
Security deposit.....	3,200	<i>Total Liabilities</i>	<u>\$ 13,600</u>
<i>Total Current Assets</i>	<u>\$ 22,600</u>		
Equipment.....	29,000	Common stock.....	10,500
<i>Total Noncurrent Assets</i>	<u>\$ 29,000</u>	Retained earnings.....	27,500
		<i>Total Shareholders Equity</i>	<u>\$ 38,000</u>
Total Assets	<u>\$ 51,600</u>	Total Liabilities + Equity	<u>\$ 51,600</u>