**ANSWERS TO QUESTIONS - CHAPTER 2**

**1. Accrual accounting attempts to record the effects of accounting events in the period when such events occur, regardless of when cash is received or paid. The goal is to match expenses with the revenues that they produce.**

**2. Recognition is the act of recording an event in the financial statements. When accruals are used, events are recognized before the associated cash is paid or collected.**

**3. If cash is collected in advance for services, the revenue is recognized when the services are rendered.**

**4. The issue of common stock, which is capital acquired from owners, increases business assets (usually cash) and equity (common stock).**

**5. The recognition of revenue on account increases the corresponding revenue account on the income statement, but does not affect the statement of cash flows. The cash flow statement is affected when the account is collected.**

**6. Revenue is recognized under accrual accounting when a revenue-producing event occurs, i.e., when the revenue is *earned*, even if no cash is collected at the time of the transaction.**

**7. The recognition of expenses affects the accounting equation by either decreasing assets or increasing liabilities (payables) and by decreasing stockholders’ equity (retained earnings).**

**8. A claims exchange transaction is one where the claims of creditors (liabilities) increase and the claims of stockholders (retained earnings) decrease, or vice versa. The total amount of claims is unchanged.**

**9. Expenses are recognized under accrual accounting at the time the expense is incurred or resources are consumed, regardless of when cash payment is made.**

**10. Net cash flows from operations on the cash flow statement may be different from net income because of the application of accrual accounting. Revenues and expenses reported on the income statement may be recognized before or after the actual collection or payment of cash that is reported on the cash flow statement.**

**11. Net income increases stockholders' claims on business assets by increasing retained earnings.**

**12. An expense is a decrease in assets or an increase in liabilities that occurs in the process of generating revenue.**

**13. The purpose of the statement of changes in stockholders’ equity is to display the effects of business operations and stock issued to owners and dividends paid to stockholders. It identifies the ways that an entity's equity increased and decreased as a result of its operations and transactions with its stockholders.**

**14. The purpose of the balance sheet is to provide information about an entity's assets, liabilities, and stockholders’ equity and their relationships to each other at a particular point in time. It provides a list of the economic resources that the enterprise has available for its operating activities and the claims to those resources.**

**15. The balance sheet is dated as of a specific date because it shows information about an entity's assets, liabilities, and stockholders’ equity as of that date, not measured over a time period. The statement of changes in stockholders’ equity, the income statement, and the statement of cash flows reflect transactions that occur over a period of time.**

**16. The statement of cash flows explains the change in cash from one accounting period to the next. It is prepared by analyzing the cash account and summarizing where cash came from and how it was used.**

**17. Period costs are costs that are recognized in an accounting period. Examples of period costs include rent expense, utilities expense, and salaries expense.**

**18. Salary of the tax return preparer could be directly matched with the revenue that it produces.**