

1. What is accounting?

Accounting is the information system that measures business activities, processes the information into reports, and communicates the results to decision makers. Accounting is the language of business.

2. Briefly describe the two major fields of accounting.

Financial accounting provides information for external decision makers, such as outside investors, lenders, customers, and the federal government. Managerial accounting focuses on information for internal decision makers, such as the company's managers and employees.

3. Describe the various types of individuals who use accounting information and how they use that information to make important decisions.

Individuals use accounting information to help them manage their money, evaluate a new job, and better decide whether they can afford to make a new purchase. Business owners use accounting information to set goals, measure progress toward those goals, and make adjustments when needed. Investors use accounting information to help them decide whether or not a company is a good investment and once they have invested, they use a company's financial statements to analyze how their investment is performing. Creditors use accounting information to decide whether to lend money to a business and to evaluate a company's ability to make the loan payments. Taxing authorities use accounting information to calculate the amount of income tax that a company has to pay.

4. What are two certifications available for accountants? Briefly explain each certification.

Certified Public Accountants (CPAs) are licensed professional accountants who serve the general public. They work for public accounting firms, businesses, government, or educational institutions. To be certified they must meet educational and/or experience requirements and pass an exam. Certified Management Accountants (CMAs) specialize in accounting and financial management knowledge. They work for a single company.

5. What is the role of the Financial Accounting Standards Board (FASB)?

The FASB oversees the creation and governance of accounting standards. They work with governmental regulatory agencies, congressionally created groups, and private groups.

6. Explain the purpose of Generally Accepted Accounting Principles (GAAP), including the organization currently responsible for the creation and governance of these standards.

The guidelines for accounting information are called GAAP. It is the main U.S. accounting rule book and is currently created and governed by the FASB. Investors and lenders must have information that is relevant and has faithful representation in order to make decisions and the GAAP provides the framework for this financial reporting.

7. Describe the similarities and differences among the four different types of business entities discussed in the chapter.

A sole proprietorship has a single owner, terminates upon the owner's death or choice, the owner has personal liability for the business's debts, and it is not a separate tax entity. A partnership has two or more owners, terminates at partner's choice or death, the partners have personal liability, and it is not a separate tax entity. A corporation is a separate legal entity, has one or more owners, has indefinite life, the stockholders are not personally liable for the business's debts, and it is a separate tax entity. A limited-liability company has one or more members and each is only liable for his or her own actions, has an indefinite life, and is not a separate tax entity.

8. A business purchases an acre of land for \$5,000. The current market value is \$5,550 and the land was assessed for property tax purposes at \$5,250. What value should the land be recorded at, and which accounting principle supports your answer?

The land should be recorded at \$5,000. The cost principle states that assets should be recorded at their historical cost.

9. What does the going concern assumption mean for a business?

The going concern assumption assumes that the entity will remain in business for the foreseeable future and long enough to use existing resources for their intended purpose.

10. Which concept states that accounting information should be complete, neutral, and free from material error?

The faithful representation concept states that accounting information should be complete, neutral, and free from material error.

11. Financial statements in the United States are reported in U.S. dollars. What assumption supports this statement?

The monetary unit assumption states that items on the financial statements should be measured in terms of a monetary unit.

12. Explain the role of the International Accounting Standards Board (IASB) in relation to International Financial Reporting Standards (IFRS).

The IASB is the organization that develops and creates IFRS which are a set of global accounting standards that would be used around the world.

13. What is the accounting equation? Briefly explain each of the three parts.

$\text{Assets} = \text{Liabilities} + \text{Equity}$. Assets are economic resources that are expected to benefit the business in the future. They are things of value that a business owns or has control of. Liabilities are debts that are owed to creditors. They are one source of claims against assets. Equity is the other source of claims against assets. Equity is the stockholders' claims against assets and is the amount of assets that is left over after the company has paid its liabilities. It represents the net worth of the corporation.

14. How do retained earnings increase? What are the two ways that retained earnings decreases?

Retained earnings increases with revenues. Retained earnings decreases with expenses and dividends.

15. How is net income calculated? Define revenues and expenses.

Revenues – Expenses = Net Income. Revenues are earnings resulting from delivering goods or services to customers. Expenses are the cost of selling goods or service.
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16. What are the steps used when analyzing a business transaction?

Step 1: Identify the accounts and the account type. Step 2: Decide if each account increases or decreases. Step 3: Determine if the accounting equation is in balance.

17. List the four financial statements. Briefly describe each statement.

Income Statement – Shows the difference between an entity's revenues and expenses and reports the net income or net loss for a specific period.
Statement of Retained Earnings – Shows the changes in retained earnings for a specific period including net income (loss) and dividends.
Balance Sheet – Shows the assets, liabilities, and stockholders' equity of the business as of a specific date.
Statement of Cash Flows – Shows a business's cash receipts and cash payments for a specific period.

18. What is the calculation for return on assets (ROA)? Explain what ROA measures.

Return on Assets = Net income / Average total assets. ROA measures how profitably a company uses its assets.

S1-1

For each user of accounting information, identify if the user would use financial accounting (FA) or managerial accounting (MA).

Solution:

a.	FA
b.	FA
c.	FA
d.	MA
e.	MA
f.	FA
g.	MA
h.	FA

S1-2

Name the organization that governs the majority of the guidelines that the CPA will use to prepare financial statements for Wholly Shirts. What are those guidelines called?

Solution:

The Financial Accounting Standards Board governs the majority of guidelines, called Generally Accepted Accounting Principles (GAAP), that the CPA will use to prepare financial statements for Wholly Shirts.

S1-3

Which type of business organization will meet Chloe's needs best?

Solution:

Chloe's needs will best be met by organizing a corporation since a corporation has an unlimited life and is a separate tax entity. In addition, the owners (stockholders) have limited liability. Chloe could also consider a limited liability company (LLC) as an option.

A LLC meets two of the three criteria. It has an unlimited life and limited liability for the owner. However, a LLC is not a separate tax entity.

S1-4

Identify the advantages and disadvantages of owning a sole proprietorship.

Solution:

Advantages:
1. Easy to organize.
2. Unification of ownership and management.
3. Less government regulation.
4. Owner has more control over business.
Disadvantages:
1. The owner pays taxes since it is not a separate tax entity.
2. No continuous life or transferability of ownership.
3. Unlimited liability of owner.

S1-5

Consider the accounting principles and assumptions discussed in the chapter and identify the principle or assumption that best matches the situation:

Solution:

a.	The economic entity assumption
b.	The cost principle.
c.	The monetary unit assumption.
d.	The going concern assumption.

S1-6

Requirements

1. Use the accounting equation to solve for equity.
2. If next year assets increased by \$3,500 and equity decreased by \$2,580, what

Solution:**Requirement 1**

Kenmore Handyman Services has equity of \$7,720.				
Assets	=	Liabilities	+	Equity
\$ 16,400	=	\$ 8,680	+	?
\$ 16,400	=	\$ 8,680	+	\$ 7,720

Requirement 2

Kenmore Handyman Services has liabilities of \$14,760.				
Assets	=	Liabilities	+	Equity
\$16,400 + \$3,500	=	?	+	\$7,720 – \$2,580
\$ 19,900	=	\$ 14,760	+	\$ 5,140

S1-7

Requirements

1. Use the accounting equation to solve for the missing information.
2. Did Josh's Overhead Doors report net income or net loss?

Solution:

Requirement 1

Assets	=	Liabilities	+	Equity				
				Contributed Capital		Retained Earnings		
			+	Common Stock		Dividends	+	Revenues - Expenses
\$ 42,600	=	\$ 17,220	+	\$ 26,240	-	\$ 8,500	+	\$ 12,080 - ?
\$ 42,600	=	\$ 17,220	+	\$ 26,240	-	\$ 8,500	+	\$ 12,080 - \$ 4,440

Requirement 2

Josh's Overhead Doors reported net income of \$7,640. Net Income = Revenues (\$12,080) – Expenses (\$4,440)

S1-8

Identify each account as Asset (A), Liability (L), or Equity (E).

Solution:

a.	L
b.	A
c.	E
d.	A
e.	E
f.	E
g.	A
h.	E
i.	A
j.	E

S1-9

Indicate the effects of the business transactions on the accounting equation for Tiny Town Kennel.

Solution:

a.	Increase asset (Cash); Increase equity (Service Revenue)
b.	Decrease asset (Cash); Decrease equity (Salaries Expense)
c.	Increase asset (Cash); Increase Equity (Common Stock)
d.	Increase asset (Accounts Receivable); Increase equity (Service Revenue)
e.	Increase liability (Accounts Payable); Decrease equity (Utility Expense)
f.	Decrease asset (Cash); Decrease equity (Dividends)

S1-10

Indicate the effects of the business transactions on the accounting equation for Elaine's Inflatables.

Solution:

a.	Increase asset (Cash); Increase equity (Common Stock)
b.	Increase asset (Equipment); Increase liability (Accounts Payable)
c.	Increase asset (Office Supplies); Decrease asset (Cash)
d.	Increase asset (Cash); Increase equity (Service Revenue)
e.	Decrease asset (Cash); Decrease equity (Wages Expense)
f.	Decrease asset (Cash); Decrease equity (Dividends)
g.	Increase asset (Accounts Receivable); Increase equity (Service Revenue)
h.	Decrease asset (Cash); Decrease equity (Rent Expense)
i.	Increase liability (Accounts Payable); Decrease equity (Utilities Expense)

S1-11

Identify the financial statement (or statements) that each account would appear on. Use I for Income Statement, RE for Statement of Retained Earnings, and B for Balance Sheet.

Solution:

a.	B
b.	B
c.	B
d.	B
e.	I
f.	I
g.	B
h.	RE
i.	B
j.	I

S1-12

Prepare the income statement of Decorating Arrangements for the year ended December 31, 2016.

Solution:

DECORATING ARRANGEMENTS		
Income Statement		
Year Ended December 31, 2016		
Revenue:		
Service Revenue		\$ 80,000
Expenses:		
Salaries Expense	\$ 37,000	
Rent Expense	11,000	
Insurance Expense	2,000	
Utilities Expense	500	
Total Expenses		50,500
Net Income		<u>\$ 29,500</u>

S1-13

Prepare the statement of retained earnings of Decorating Arrangements for the year ending December 31, 2016

Solution:

DECORATING ARRANGEMENTS	
Statement of Retained Earnings	
Year Ended December 31, 2016	
Retained Earnings, January 1, 2016	\$4,800
Net income for the year	29,500
	34,300
Dividends	(4,500)
Retained Earnings, December 31, 2016	\$ 29,800

S1-14

Prepare the balance sheet of Decorating Arrangements as of December 31, 2016.

Solution:

DECORATING ARRANGEMENTS			
Balance Sheet			
December 31, 2016			
Assets		Liabilities	
Cash	\$ 7,000	Accounts Payable	\$ 4,300
Accounts Receivable	7,500		
Office Supplies	1,500	Stockholders' Equity	
Equipment	26,600	Common Stock	8,500
		Retained Earnings	29,800
		Total Stockholders' Equity	38,300
Total Assets	<u>\$ 42,600</u>	Total Liabilities and Stockholders' Equity	<u>\$ 42,600</u>

S1-15

Prepare the statement of cash flows for Pushing Daisies Homes for the month ended July 31, 2016.

Solution:

PUSHING DAISIES HOMES		
Statement of Cash Flows		
Month Ended July 31, 2016		
Cash flows from operating activities:		
Receipts:		
Collections from customers		\$ 24,000
Payments:		
For rent	\$ (3,000)	
For salaries	(1,600)	
For utilities	(900)	(5,500)
Net cash provided by operating activities		18,500
Cash flows from investing activities:		
Purchase of equipment	(18,000)	
Net cash used by investing activities		(18,000)
Cash flows from financing activities:		
Issued common stock	12,000	
Payment of cash dividend	(3,500)	
Net cash provided by financing activities		8,500
Net increase in cash		9,000
Cash balance, July 1, 2014		11,000
Cash balance, July 31, 2014		<u>\$ 20,000</u>

S1-16

Calculate Refined Water Services' return on assets (ROA) for the month of October.

Solution:

Return on assets =	Net income / Average total assets
	= \$74,000 / ((\$350,000 + \$390,000) / 2)
	= \$74,000 / \$370,000
	= 20%

E1-17

For each of the users of accounting information, identify whether the user is an external decision maker (E) or an internal decision maker (I):

Solution:

a.	E
b.	I
c.	E
d.	E
e.	E
f.	I
g.	I
h.	E

E1-18

Match the accounting terms to the definition:

Solution:

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

E1-19

Match the accounting terms to the definition:

Solution:

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

E1-20

Compute the missing amount in the accounting equation for each entity from the financial information presented:

Solution:

	Assets	Liabilities	Equity
Newton Gas	\$ 144,000	\$ 64,000	\$ 80,000
Megas Video Rentals	65,000	40,000	25,000
Cline's Grocery	\$ 200,000	\$ 43,000	\$ 157,000

E1-21

For each of the following situations with regard to common stock and dividends of a corporation compute the amount of net income or net loss during June 2016.

- The company issued \$7,500 of common stock and paid no dividends.
- The company issued no common stock. It paid cash dividends of \$13,000.
- The company issued \$20,000 of common stock and paid cash dividends of \$18,000.

Solution:

	a.	b.	c.
Stockholders' equity, May 31, 2016 (\$188,000 – \$122,000)	\$ 66,000	\$ 66,000	\$ 66,000
Issuance of common stock	7,500	0	20,000
Net income for the month	82,500	103,000	88,000
	156,000	169,000	174,000
Dividends	0	(13,000)	(18,000)
Stockholders' equity, June 30, 2016 (\$244,000 – \$88,000)	\$156,000	\$156,000	\$156,000

E1-22

Requirements

1. Did the stockholders' equity of Star Nursery increase or decrease during 2016? By how much?
2. Identify the four possible reasons that stockholders' equity can change.

Solution:**Requirement 1**

	Assets	=	Liabilities	+	Equity
Beginning of 2016	\$ 24,000	=	\$ 5,000	+	?
	\$ 24,000	=	\$ 5,000	+	\$ 19,000
End of 2016	\$ 18,000	=	\$ 1,000	+	?
	\$ 18,000	=	\$ 1,000	+	\$ 17,000
Stockholders' equity increased in 2016 by \$2,000 (\$17,000 – \$19,000).					

Requirement 2

a. Increase through issuance of common stock.
b. Increase through net income.
c. Decrease through dividend payment.
d. Decrease through net loss.

E1-23

Requirements

- 1. Compute Peaceful River Spa’s net income for 2016.
- 2. Did Peaceful River Spa’s stockholders’ equity increase or decrease during 2016? By how much?

Solution:

Requirement 1

Revenues	–	Expenses	=	Net Income
\$ 40,000	–	\$ 35,000	=	\$ 5,000

Requirement 2

Peaceful River Spa’s equity increased by \$5,000 (\$14,000 - \$9,000) or the amount of the net income.				
	Assets	=	Liabilities	+ Equity
Beginning of 2016	\$ 18,000	=	\$ 9,000	+ ?
	\$ 18,000	=	\$ 9,000	+ \$ 9,000
Ending of 2016	\$ 23,000	=	\$ 9,000	+ ?
	\$ 23,000	=	\$ 9,000	+ \$ 14,000

E1-24

Requirements

1. Compute the missing amount for Meehan Company. You will need to determine Retained Earnings, December 31, 2016, and total stockholders' equity.
2. Did Meehan earn a net income or suffer a net loss for the year? Compute the amount.

Solution:

Requirement 1

	Assets	–	Liabilities	=	Equity
Beginning of 2016	\$ 64,000	–	\$ 44,000	=	\$ 20,000
Ending of 2016	\$ 54,000	–	\$ 39,000	=	\$ 15,000

Retained Earnings:	
Retained Earnings, Jan. 1, 2016	\$ 7,000
Plus: Revenues	257,000
Less: Expenses	(258,000)
Less: Dividends	(4,000)
Retained Earnings, Dec. 31, 2016	\$ 2,000
Stockholders' Equity:	
Common Stock	\$ 13,000
Retained Earnings	2,000
Total Stockholders' Equity	\$ 15,000

Requirement 2

Revenues	–	Expenses	=	Income (Loss)
\$ 257,000	–	\$ 258,000	=	\$ (1,000)
Felix Company earned net income of \$20,000.				

E1-25

Give an example of a transaction that has each of the following effects on the accounting equation:

- a. Increase one asset and decrease another asset.
- b. Decrease an asset and decrease equity.
- c. Decrease an asset and decrease a liability.
- d. Increase an asset and increase equity.
- e. Increase an asset and increase a liability.

Solution:

Student responses will vary. Examples include:
a. Cash purchase of office supplies.
b. Cash dividends paid to stockholders.
c. Paid cash on accounts payable.
d. Received cash for services provided.
e. Borrowed cash from the bank.

E1-26

Indicate the effects of business transactions on the accounting equation of Vivian's Online Video store.

Solution:

a.	Increase asset (Cash); Increase equity (Common Stock)
b.	Increase asset (Accounts Receivable); Increase equity (Rental Revenue)
c.	Increase asset (Office Furniture); Increase liability (Accounts Payable)
d.	Increase asset (Cash); Decrease asset (Accounts Receivable)
e.	Decrease asset (Cash); Decrease liability (Accounts Payable)
f.	Increase asset (Cash); Increase equity (Rental Revenue)
g.	Decrease asset (Cash); Decrease equity (Office Rent Expense)
h.	Decrease asset (Cash); Increase asset (Office Supplies)

E1-27

Indicate the effects of business transactions on the accounting equation for Sam's Snack Foods, a supplier of snack foods.

Solution:

a.	Increase asset (Cash); Increase equity (Common Stock)
b.	Increase asset (Land); Decrease asset (Cash)
c.	Decrease asset (Cash); Decrease liability (Accounts Payable)
d.	Increase asset (Equipment); Increase liability (Notes Payable)
e.	Increase asset (Accounts Receivable); Increase equity (Service Revenue)
f.	Increase liability (Salaries Payable); Decrease equity (Salaries Expense)
g.	Increase asset (Cash); Decrease asset (Accounts Receivable)
h.	Increase asset (Cash); Increase liability (Notes Payable)
i.	Decrease asset (Cash); Decrease equity (Dividends)
j.	Increase liability (Accounts Payable); Decrease equity (Utility Expense)

E1-28

Describe each transaction.

Solution:

Transaction Descriptions:	
1.	Issuance of common stock to stockholders
2.	Earned revenue on account
3.	Purchased equipment on account
4.	Collected cash on account
5.	Cash purchase of equipment
6.	Paid cash on account
7.	Earned revenue and received cash
8.	Paid cash for salaries expense

E1-29

Analyze the effects on the accounting equation of the medical practice of Samantha Stamford, M.D.

Solution:

	Assets			=	Liabilities		+	Equity				
								Contributed + Capital	Retained Earnings			
Date	Cash	+ Medical Supplies	+ Land	=	Accounts Payable	+ Common Stock	- Dividends	+ Service Revenue	- Salaries Expense	- Rent Expense	- Utilities Expense	
Jul-06	65,000					65,000						
Bal.	\$ 65,000			=		+ \$ 65,000						
9	(52,000)		52,000	=								
Bal.	\$ 13,000		+ \$52,000	=		+ \$ 65,000						
12		+ 1,600		=	1,600							
Bal.	\$ 13,000	+ \$ 1,600	+ \$52,000	=	\$ 1,600	+ \$ 65,000						
15												
Bal.	\$ 13,000	+ \$ 1,600	+ \$52,000	=	\$ 1,600	+ \$ 65,000						
20	(3,150)			=					(1,500)	(1,300)	(350)	
Bal.	\$ 9,850	+ \$ 1,600	+ \$52,000	=	\$ 1,600	+ \$ 65,000			- \$ 1,500	- \$ 1,300	- \$ 350	
31	8,000			=				+8,000				
Bal.	\$ 17,850	+ \$ 1,600	+ \$52,000	=	\$ 1,600	+ \$ 65,000		+ +8,000	- \$ 1,500	- \$ 1,300	- \$ 350	
31	(800)			=	(800)							
Bal.	\$ 17,050	+ \$ 1,600	+ \$52,000	=	\$ 800	+ \$ 65,000		+ +8,000	- \$ 1,500	- \$ 1,300	- \$ 350	

E1-30

Requirements

1. What are the four financial statements that business will need to prepare?
2. Is there a specific order in which the financial statements must be prepared?
3. Explain how to prepare each statement.

Solution:**Requirement 1**

- | |
|-----------------------------------|
| a. Income statement |
| b. Statement of retained earnings |
| c. Balance sheet |
| d. Statement of cash flows |
| |

Requirement 2

Yes, the financial statements should be prepared in the order listed above in Requirement 1.
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Requirement 3

- | |
|--|
| Income Statement: |
| a. The header includes the name of the business, the title of the statement, and the time period. An income statement always represents a period of time, for example, a month or a year. |
| b. The revenue accounts are always listed first and then subtotaled if necessary. |
| c. Each expense account is listed separately from largest to smallest and then subtotaled if necessary. |
| d. Net income is calculated as total revenues minus total expenses. |
| |
| Statement of Retained Earnings: |
| a. The header includes the name of the business, the title of the statement, and the time period. A statement of retained earnings always represents a period of time, for example, a month or a year. |
| b. The beginning retained earnings is listed first and will always be the ending retained earnings from the previous time period. |
| c. The net income is added to the beginning retained earnings. |
| d. The dividends are subtracted from retained earnings. If there had been a net loss, this would also be subtracted. |

Balance Sheet:

- a. The header includes the name of the business and the title of the statement date is different. The balance sheet shows the date as a specific date and not a period of time.
- b. Each asset account is listed separately and then totaled. Cash is always listed first.
- c. Liabilities are listed separately and then totaled. Liabilities that are to be paid first are listed first.
- d. The stockholders' equity section includes common stock and ending retained earnings from the statement of retained earnings.
- e. The balance sheet must always balance: $\text{Assets} = \text{Liabilities} + \text{Equity}$.

Statement of Cash Flows:

- a. The header includes the name of the business, the title of the statement, and the time period. A statement of cash flows always represents a period of time, for example, a month or a year.
- b. Each dollar amount is calculated by evaluating the cash column on the transaction detail.
- c. Operating activities involve cash receipts for services provided and cash payments for expenses paid.
- d. Investing activities include the purchase and sale of land and equipment for cash.
- e. Financing activities include cash from the issuance of common stock and payment of cash dividends.
- f. The ending cash balance must match the cash balance on the balance sheet.

E1-31

Requirements

1. Prepare the income statement for Wilford Towing Service for the month ending June 30, 2016.
2. What does the income statement report?

Solution:**Requirement 1**

WILFORD TOWING SERVICE Income Statement Month Ended June 30, 2016	
Revenue:	
Service Revenue	\$ 13,000
Expenses:	
Salaries Expense	\$ 1,900
Rent Expense	800
Total Expenses	2,700
Net Income	<u>\$ 10,300</u>

Requirement 2

The income statement reports revenues and expenses for a period of time.
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E1-32

Requirements

1. Prepare the statement of retained earnings for Wilford Towing Service for the month ending June 30, 2016.
2. What does the statement of retained earnings report?

Solution:

WILFORD TOWING SERVICE Statement of Retained Earnings Month Ended June 30, 2016	
Retained Earnings, June 1, 2014	\$ 3,700
Net income for the month	10,300
	14,000
Dividends	(2,000)
Retained Earnings, June 30, 2014	<u>\$ 12,000</u>

Requirement 2

The statement of retained earnings reports the changes in net income (loss) and dividends for a corporation during a time period.

E1-33

Requirements

1. Prepare the balance sheet for Wilford Towing Service as of June 30, 2016.
2. What does the balance sheet report?

Solution:

WILFORD TOWING SERVICE Balance Sheet June 30, 2016			
Assets		Liabilities	
Cash	\$ 1,900	Accounts Payable	\$ 6,000
Accounts Receivable	8,200	Notes Payable	6,900
Office Supplies	1,300	Total Liabilities	12,900
Equipment	17,500		
		Stockholders' Equity	
		Common Stock	4,000
		Retained Earnings	12,000
		Total Stockholders' Equity	16,000
Total Assets		Total Liabilities and Stockholders' Equity	
	<u>\$ 28,900</u>		<u>\$ 28,900</u>

Requirement 2

The balance sheet reports an entity's assets, liabilities, and stockholders' equity as of a specific date.

E1-34

Prepare the income statement for Drought Design Studio for the year ending December 31, 2016.

Solution:

DROUGHT DESIGN STUDIO Income Statement Year Ended December 31, 2016		
Revenue:		
Service Revenue		\$ 159,200
Expenses:		
Salaries Expense	\$ 62,000	
Rent Expense	22,000	
Utilities Expense	6,500	
Miscellaneous Expense	4,000	
Property Tax Expense	1,200	
Total Expenses		95,700
Net Income		<u>\$ 63,500</u>

E1-35

Prepare the statement of retained earnings for Drought Design Studio for the year ending December 31, 2016.

Solution:

DROUGHT DESIGN STUDIO	
Statement of Retained Earnings	
Year Ended December 31, 2016	
Retained Earnings, January 1, 2016	\$ 31,000
Net income for the year	63,500
	94,500
Dividends	(55,000)
Retained Earnings, December 31, 2016	\$ 39,500

E1-36

Prepare the balance sheet for Drought Design Studio as of December 31, 2016.

Solution:

DROUGHT DESIGN STUDIO Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$ 3,100	Accounts Payable	\$ 3,700
Accounts Receivable	10,200	Notes Payable	9,800
Office Supplies	4,500	Total Liabilities	13,500
Office Furniture	55,200	Stockholders' Equity	
		Common Stock	20,000
		Retained Earnings	39,500
		Total Stockholders' Equity	59,500
		Total Liabilities and Stockholders'	
Total Assets	\$ 73,000	Equity	\$ 73,000

E1-37

For each transaction, identify the appropriate section on the statement of cash flows to report the transaction. Choose from: Cash flows from operating activities (O), Cash flows from investing activities (I), Cash flows from financing activities (F), or Is not reported on the statement of cash flows (X). If reported on the statement, decide whether the transaction should be shown as a positive cash flow (+) or a negative cash flow (–):

Solution:

a.	F+
b.	O–
c.	X
d.	F–
e.	O+
f.	I–
g.	O–
h.	X
i.	O–
j.	X

E1-38

Prepare the statement of cash flows of Bean Town Food Equipment Company for the month ended February 29, 2016.

Solution:

BEAN TOWN FOOD EQUIPMENT COMPANY Statement of Cash Flows Month Ended February 29, 2016		
Cash flows from operating activities:		
Receipts:		
Collections from customers		\$ 8,000
Payments:		
For rent	\$ (1,800)	
For salaries	(1,500)	
For utilities	(500)	(3,800)
Net cash provided by operating activities		4,200
Cash flows from investing activities:		
Purchase of land	(18,000)	
Net cash used by investing activities		(18,000)
Cash flows from financing activities:		
Issuance of common stock	7,500	
Payment of cash dividends	(3,000)	
Net cash provided by financing activities		4,500
Net decrease in cash		(9,300)
Cash balance, February 1, 2016		16,400
Cash balance, February 29, 2016		\$ 7,100

E1-39

Calculate the return on assets (ROA) for Alec Appliance Service for the year ending December 31, 2016.

Solution:

Average total assets = (Beginning total assets + ending total assets) / 2
Beginning total assets = \$39,000 + \$20,000 + \$155,000 + \$1,600 + \$22,000
+ \$4,200 = \$241,800
Ending total assets = \$20,200 + \$38,000 + \$155,000 + \$18,400 + \$46,000
+ \$600 = \$278,200
Average total assets = (\$241,800 + \$278,200) / 2 = \$260,000
ROA = Net income / Average total assets
ROA = \$18,200 / \$260,000 = 0.07 = 7%

P1-40A

Analyze the effects of the transactions on the accounting equation of Solid Gold.

Solution:

	Assets										= Liabilities +	Equity							
											Contributed Capital		+	Retained Earnings					
	Cash	+	Accounts Receivable	+	Office Supplies	+	Land	=	Accounts Payable	+	Common Stock	-	Dividends	+	Service Revenue	-	Rent Expense	-	Advertising Expense
Bal.	\$2,400	+	\$2,600			+	\$15,000	=	\$ 3,000	+	\$ 14,400				\$2,600				
(a)	8,000										8,000								
Bal.	\$10,400	+	\$2,600			+	\$15,000	=	\$ 3,000	+	\$ 22,400				\$2,600				
(b)	1300														\$ 1,300				
Bal.	\$11,700	+	\$2,600			+	\$15,000	=	\$ 3,000	+	\$ 22,400				\$ 3,900				
(c)	-3000								-3000										
Bal.	\$8,700	+	\$2,600			+	\$15,000	=	\$ -	+	\$ 22,400			+	\$ 3,900				
(d)					400				400										
Bal.	\$8,700	+	\$2,600	+	\$400	+	\$15,000	=	\$ 400	+	\$ 22,400			+	\$ 3,900				
(e)	2,200		-2200																
Bal.	\$10,900	+	\$400	+	\$400	+	\$15,000	=	\$ 400	+	\$ 22,400			+	\$ 3,900				
(f)	-1800												(1,800)						
Bal.	\$9,100	+	\$400	+	\$400	+	\$15,000	=	\$ 400	+	\$ 22,400	-	1,800	+	\$ 3,900				
(g)			6,500												6,500				
Bal.	\$9,100	+	\$6,900	+	\$400	+	\$15,000	=	\$ 400	+	\$ 22,400	-	1,800	+	\$ 10,400				
(h)	-1750																-1,400		-350
Bal.	\$7,350	+	\$6,900	+	\$400	+	\$15,000	=	\$ 400	+	\$ 22,400	-	1,800	+	\$ 10,400	-	\$1,400	-	\$350

P1-41A

Analyze the effects of the transaction on the accounting equations of Turnbull Gymnastics.

Solution:

Assets				=	Liabilities		+	Equity																					
								Contributed Capital	+	Retained Earnings																			
	Cash	+	Accounts Receivable	+	Office Supplies	=	Accounts Payable	+	Common Stock	–	Dividends	+	Service Revenue	–	Rent Expense	–	Utilities Expense	–	Salaries Expense	–	Advertising Expense								
1	+21,000								21,000																				
2	2,400												2,400																
Bal.	\$23,400						=		+	\$21,000					+	\$2,400													
5	-350								350																				
Bal.	\$23,050							+	\$350				=		+	\$21,000					+	\$2,400							
9									1,500																				
Bal.	\$23,050				+			\$1,500	+				\$350	=		+	\$21,000					+	\$3,900						
10										100																			
Bal.	\$23,050				+			\$1,500	+				\$350	=		\$100	+	\$21,000					+	\$3,900					
15	-300																												
Bal.	\$22,750				+			\$1,500	+				\$350	=		\$100	+	\$21,000					+	\$3,900					
20	-100																												
Bal.	\$22,650				+			\$1,500	+				\$350	=		\$0	+	\$21,000					+	\$3,900					
25	1,500																												
Bal.	\$24,150				+			\$0	+				\$350	=			+	\$21,000					+	\$3,900					
28	-2,800																												
Bal.	\$21,350								+				\$350	=			+	\$21,000					+	\$3,900					
28	-1100																												
Bal.	\$20,250								+				\$350	=			+	\$21,000					+	\$3,900					
30	2,800																												
Bal.	\$23,050								+				\$350	=			+	\$21,000					+	\$6,700					
31	-4500																												
Bal.	\$18,550				+			\$0	+				\$350	=		\$0	+	\$21,000				–		\$4,500	+	\$6,700			

P1-42A

Requirements

1. Prepare Golden City Barbershop's income statement.
2. Prepare the statement of retained earnings.
3. Prepare the balance sheet.

Solution:**Requirement 1**

GOLDEN CITY BARBERSHOP Income Statement Year Ended December 31, 2016	
Revenue:	
Service Revenue	\$ 195,000
Expenses:	
Salaries Expense	\$ 61,000
Advertising Expense	13,000
Rent Expense	11,000
Interest Expense	7,000
Property Tax Expense	2,700
Insurance Expense	2,500
Total Expenses	97,200
Net Income	<u>\$ 97,800</u>

Requirement 2

GOLDEN CITY BARBERSHOP Statement of Retained Earnings Year Ended December 31, 2016	
Retained Earnings, January 1, 2016	\$ 49,000
Net income for the year	97,800
	146,800
Dividends	(32,000)
Retained Earnings, December 31, 2016	<u>\$ 114,800</u>

Requirement 3

GOLDEN CITY BARBERSHOP Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$ 3,800	Accounts Payable	\$ 17,000
Accounts Receivable	900	Notes Payable	37,000
Office Supplies	9,000	Salaries Payable	900
Equipment	19,000	Total Liabilities	54,900
Building	157,000		
Land	5,000	Stockholders' Equity	
		Common Stock	25,000
		Retained Earnings	114,800
		Total Stockholders' Equity	139,800
		Total Liabilities and Stockholders'	
Total Assets	\$ 194,700	Equity	\$ 194,700

P1-43A

Prepare the following financial statements for Click a Pix Photography for the year ended December 31, 2016:

- a. Income statement
- b. Statement of retained earnings.
- c. Balance sheet

Solution:**Part a.**

CLICK A PIX PHOTOGRAPHY Income Statement Year Ended December 31, 2016		
Revenue:		
Service Revenue		\$ 95,000
Expenses:		
Salaries Expense	20,000	
Insurance Expense	11,000	
Advertising Expense	3,200	
Total Expenses		34,200
Net Income		<u>\$ 60,800</u>

Part b.

CLICK A PIX PHOTOGRAPHY Statement of Retained Earnings Year Ended December 31, 2016		
Retained Earnings, January 1, 2016		
		\$ 26,000
Net income for the year		60,800
		<u>86,800</u>
Dividends		(10,000)
Retained Earnings, December 31, 2016		<u>\$ 76,800</u>

Part c.

CLICK A PIX PHOTOGRAPHY Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$ 40,000	Accounts Payable	\$ 6,000
Accounts Receivable	12,000	Notes Payable	<u>9,000</u>
Equipment	73,800	Total Liabilities	15,000
		Stockholders' Equity	
		Common Stock	34,000
		Retained Earnings	<u>76,800</u>
		Total Stockholders' Equity	110,800
		Total Liabilities and Stockholders'	
Total Assets	<u>\$ 125,800</u>	Equity	<u>\$ 125,800</u>

P1-44A

Prepare a corrected balance sheet.

Solution:

LONE STAR LANDSCAPING Balance Sheet November 30, 2016			
Assets		Liabilities	
Cash	\$ 4,900	Accounts Payable	\$ 2,800
Accounts Receivable	2,100	Notes Payable	<u>24,200</u>
Office Supplies	300	Total Liabilities	27,000
Office Furniture	6,000		
Land	33,800	Stockholders' Equity	
		Common Stock	12,000
		Retained Earnings	<u>8,100</u>
		Total Stockholders' Equity	20,100
		Total Liabilities and Stockholders'	
Total assets	<u>\$ 47,100</u>	Equity	<u>\$ 47,100</u>

P1-45A**Requirements**

1. Analyze the effects of the events on the accounting equation of Alfonso Sheen, CPA.
2. Prepare the following financial statements:
 - a. Income statement
 - b. Statement of retained earnings.
 - c. Balance sheet

Solution:

Requirement 1

Assets						=	Liabilities			+	Equity								
										Contributed Capital	+	Retained Earnings							
Cash	+	Accounts Receivable	+	Office Supplies	+	Furniture	=	Accounts Payable	+	Common Stock	–	Dividends	+	Service Revenue	–	Rent Expense	–	Utilities Expense	
5	70,000									70,000									
6	-350			350															
Bal.	\$69,650		+	\$350			=		+	\$70,000									
7						7,000		7,000											
Bal.	\$69,650		+	\$350	+	\$7,000	=	\$7,000	+	\$70,000									
10	1,800													1,800					
Bal.	\$71,450		+	\$350	+	\$7,000	=	\$7,000	+	\$70,000			+	\$1,800					
11	-400																	-400	
Bal.	\$71,050		+	\$350	+	\$7,000	=	\$7,000	+	\$70,000			+	\$1,800			–	\$400	
12		11,000												11,000					
Bal.	\$71,050	+	\$11,000	+	\$350	+	\$7,000	=	\$7,000	+	\$70,000		+	\$12,800			–	\$400	
18	-1,000																	-1,000	
Bal.	\$70,050	+	\$11,000	+	\$350	+	\$7,000	=	\$7,000	+	\$70,000		+	\$12,800	–	\$1,000	–	\$400	
25	11,000	-11,000																	
Bal.	\$81,050	\$0	+	\$350	+	\$7,000	=	\$7,000	+	\$70,000			+	\$12,800	–	\$1,000	–	\$400	
27	-7,000							-7,000											
Bal.	\$74,050		+	\$350	+	\$7,000	=	\$0	+	\$70,000			+	\$12,800	–	\$1,000	–	\$400	
	-4,500											-4,500							
Bal.	\$69,550	+	\$0	+	\$350	+	\$7,000	=	\$0	+	\$70,000	–	\$4,500	+	\$12,800	–	\$1,000	–	\$400

Requirement 2a

ALFONSO SHEEN, CPA Income Statement Month Ended Febraury 29, 2016	
Revenue:	
Service Revenue	\$12,800
Expenses:	
Rent Expense	\$1,000
Utilities Expense	\$400
Total Expenses	\$1,400
Net Income	<u>\$11,400</u>

Requirement 2b

ALFONSO SHEEN, CPA Statement of Retained Earnings Month Ended Febraury 29, 2016	
Retained Earnings, February 1, 2016	\$ 0
Net income for the month	\$11,400
	11,400
Dividends	\$ (4,500)
Retained Earnings, February 29, 2016	<u>\$ 6,900</u>

Requirement 2c

ALFONSO SHEEN, CPA Balance Sheet February 29, 2016			
Assets		Liabilities	
Cash	\$ 69,550		
Office Supplies	350		
Furniture	7,000	Stockholders' Equity	
		Common Stock	\$ 70,000
		Retained Earnings	<u>6,900</u>
		Total Stockholders' Equity	<u>76,900</u>
		Total Liabilities and Stockholders'	
Total Assets	<u>\$ 76,900</u>	Equity	<u>\$ 76,900</u>

P1-46A**Requirements**

1. Analyze the effects of the preceding events on the accounting equation of the Angela Petrillo, Attorney.
2. Prepare the following financial statements:
 - a. Income statement
 - b. Statement of retained earnings.
 - c. Balance sheet

Solution:

Requirement 1

	Assets				=	Liabilities	+	Equity				
								Contributed Capital	+	Retained Earnings		
	Cash	+ Accounts Receivable	+ Office Supplies	+ Computer	=	Accounts Payable	+ Common Stock	- Dividends	+ Service Revenue	- Utilities Expense	- Misc. Expense	
3	72,000						72,000					
5	-350		350									
Bal.	\$71,650		\$350		=		\$72,000					
7				5,500		5,500						
Bal.	\$71,650		\$350	\$5,500	=	\$5,500	\$72,000					
9	2,500								2,500			
Bal.	\$74,150		\$350	\$5,500	=	\$5,500	\$72,000		\$2,500			
15						340						-340
Bal.	\$74,150		\$350	\$5,500	=	\$5,840	\$72,000		\$2,500			\$340
23		18,000							18,000			
Bal.	\$74,150	\$18,000	\$350	\$5,500	=	\$5,840	\$72,000		\$20,500			\$340
28	-340					-340						
Bal.	\$73,810	\$18,000	\$350	\$5,500	=	\$5,500	\$72,000		\$20,500			\$340
30	-1,300											-1,300
Bal.	\$72,510	\$18,000	\$350	\$5,500	=	\$5,500	\$72,000		\$20,500	\$1,300		\$340
31	1,800	-1,800										
Bal.	\$74,310	\$16,200	\$350	\$5,500	=	\$5,500	\$72,000		\$20,500	\$1,300		\$340
31	-2,000							-2,000				
Bal.	\$72,310	\$16,200	\$350	\$5,500	=	\$5,500	\$72,000	\$2,000	\$20,500	\$1,300		\$340

Requirement 2a

ANGELA PETRILLO, ATTORNEY Income Statement Month Ended March 31, 2016		
Revenue:		
Service Revenue		\$20,500
Expenses:		
Utilities Expense	\$1,300	
Miscellaneous Expense	\$340	
Total Expenses		\$1,640
Net Income		\$18,860

Requirement 2b

ANGELA PETRILLO, ATTORNEY Statement of Retained Earnings Month Ended March 31, 2016		
Retained Earnings, March 1, 2016		
	\$	0
Net income for the month		\$18,860
		18,860
Dividends		(2,000)
Retained Earnings, March 31, 2016	\$	16,860

Requirement 2c

ANGELA PETRILLO, ATTORNEY Balance Sheet March 31, 2016			
Assets		Liabilities	
Cash	\$72,310	Accounts Payable	\$5,500
Office Supplies	\$16,200		
Furniture	\$350	Stockholders' Equity	
	\$5,500		
		Common Stock	72,000
		Retained Earnings	<u>16,860</u>
		Total Stockholders' Equity	88,860
		Total Liabilities and Stockholders'	
Total Assets	<u>\$94,360</u>	Equity	<u>\$94,360</u>

P1-47B

Analyze the effects of the transactions on the accounting equation of Dance Fever.

Solution:

	Assets				= Liabilities+		Equity				
							Contributed Capital	+ Retained Earnings			
	Cash	+ Accounts Receivable	+ Office Supplies	+ Land	= Accounts Payable	+ Common Stock	- Dividends	+ Service Revenue	- Rent Expense	- Advertising Expense	
Bal.	\$ 2,100	+ \$ 2,500	+ \$ 11,000	= \$ 6,000	+ \$ 7,100			2,500			
(a)	13,000					13,000					
Bal.	\$15,100	+ \$ 2,500	+ \$ 11,000	= \$ 6,000	+ \$ 20,100			2,500			
(b)	1,200							1,200			
Bal.	\$16,300	+ \$ 2,500	+ \$ 11,000	= \$ 6,000	+ \$ 20,100			+ 3,700			
(c)	-6,000				-6,000						
Bal.	\$10,300	+ \$ 2,500	+ \$ 11,000	= \$ 0	+ \$ 20,100			+ 3,700			
(d)			1,000		1,000						
Bal.	\$10,300	+ \$ 2,500	+ \$ 1,000	+ \$ 11,000	= \$ 1,000	+ \$ 20,100		+ 3,700			
(e)	1,500	-1,500									
Bal.	\$11,800	+ \$ 1,000	+ \$ 1,000	+ \$ 11,000	= \$ 1,000	+ \$ 20,100		+ 3,700			
(f)	-1,900						-1,900				
Bal.	\$ 9,900	+ \$ 1,000	+ \$ 1,000	+ \$ 11,000	= \$ 1,000	+ \$ 20,100	- \$ 1,900	+ 3,700			
(g)		6,000						6,000			
Bal.	\$ 9,900	+ \$ 7,000	+ \$ 1,000	+ \$ 11,000	= \$ 1,000	+ \$ 20,100	- \$ 1,900	+ 9,700			
(h)	-1,750								-1,400	-350	
Bal.	\$ 8,150	+ \$ 7,000	+ \$ 1,000	+ \$ 11,000	= \$ 1,000	+ \$ 20,100	- \$ 1,900	+ 9,700	- \$ 1,400	- \$ 350	

P1-48B

Analyze the effects of the transactions on the accounting equation of Timmins Gymnastics.

Solution:

	Assets			=	Liabilities		+	Equity				
								Contributed Capital		Retained Earnings		
	Cash	+ Accounts Receivable	+ Office Supplies	=	Accounts Payable	+ Common Stock	- Dividends	+ Service Revenue	- Rent Expense	- Utilities Expense	- Salaries Expense	- Advertising Expense
1	20,000					20,000						
2	2,200							2,200				
Bal.	\$22,200			=		\$20,000		+	\$2,200			
5	-350		350									
Bal.	\$21,850		+ \$350	=		\$20,000		+	\$2,200			
9		4,500							4,500			
Bal.	\$21,850	+	\$4,500	+	\$350	=	+	\$20,000	+	\$6,700		
10					100					-100		
Bal.	\$21,850	+	\$4,500	+	\$350	=	\$100	+	\$20,000	+	\$6,700	- \$100
15	-475											-475
Bal.	\$21,375	+	\$4,500	+	\$350	=	\$100	+	\$20,000	+	\$6,700	- \$100 - \$475
20	-100				-100							
Bal.	\$21,275	+	\$4,500	+	\$350	=	\$0	+	\$20,000	+	\$6,700	- \$100 - \$475
25	4,500	-4,500										
Bal.	\$25,775	+	\$0	+	\$350	=	+	\$20,000	+	\$6,700	- \$100	- \$475
28	-3,000								-3,000			
Bal.	\$22,775		+ \$350	=		\$20,000		+	\$6,700	- \$3,000	- \$100	- \$475
28	-1,500										-1,500	
Bal.	\$21,275		+ \$350	=		\$20,000		+	\$6,700	- \$3,000	- \$100	- \$1,500 - \$475
30	2,000							2,000				
Bal.	\$ 23,275		+ \$350	=		\$20,000		+	\$8,700	- \$3,000	- \$100	- \$1,500 - \$475
31	-3500						-3500					
Bal.	\$ 19,775	+	\$0	+	\$350	=	\$0	+	\$20,000	- \$3,500	+	\$8,700 - \$3,000 - \$100 - \$1,500 - \$475

P1-49B

Requirements

1. Prepare Town and Country Realty's income statement.
2. Prepare the statement of retained earnings.
3. Prepare the balance sheet.

Solution:

Requirement 1

TOWN AND COUNTRY REALTY Income Statement Year Ended December 31, 2016	
Revenues:	
Service Revenue	\$ 180,000
Expenses:	
Salaries Expense	\$ 69,000
Advertising Expense	14,000
Rent Expense	10,000
Interest Expense	6,500
Property Tax Expense	3,400
Insurance Expense	2,200
Total Expenses	105,100
Net Income	\$ 74,900

Requirement 2

TOWN AND COUNTRY REALTY Statement of Retained Earnings Year Ended December 31, 2016	
Retained Earnings, January 1, 2016	\$ 57,000
Net income for the year	74,900
	131,900
Dividends	(32,000)
Retained Earnings, December 31, 2016	\$ 99,900

Requirement 3

TOWN AND COUNTRY REALTY Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$ 3,800	Accounts Payable	\$ 14,000
Accounts Receivable	1,000	Notes Payable	36,000
Office Supplies	12,000	Salaries Payable	1,500
Equipment	13,000	Total Liabilities	51,500
Building	144,600		
Land	5,000	Stockholders' Equity	
		Common Stock	28,000
		Retained Earnings	99,900
		Total Stockholders' Equity	127,900
		Total Liabilities and Stockholders'	
Total Assets	<u>\$ 179,400</u>	Equity	<u>\$ 179,400</u>

P1-50B

Prepare the following financial statements for Precision Pics for the year ended December 31, 2016:

- a. Income statement
- b. Statement of retained earnings.
- c. Balance sheet

Solution:**Requirement a**

PRECISION PICS Income Statement Year Ended December 31, 2016	
Revenues:	
Service Revenue	\$ 110,000
Expenses:	
Salaries Expense	\$ 21,000
Insurance Expense	14,000
Advertising Expense	3,500
Total Expenses	38,500
Net Income	<u>\$ 71,500</u>

Requirement b

PRECISION PICS Statement of Retained Earnings Year Ended December 31, 2016	
Retained Earnings, January 1, 2016	\$ 26,000
Net income for the year	71,500
	<u>97,500</u>
Dividends	(11,000)
Retained Earnings, December 31, 2016	<u>\$ 86,500</u>

Requirement c

PRECISION PICS Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$ 38,000	Accounts Payable	\$ 13,000
Accounts Receivable	7,000	Notes Payable	9,000
Equipment	96,500	Total Liabilities	22,000
		Stockholders' Equity	
		Common Stock	33,000
		Retained Earnings	86,500
		Total Stockholders' Equity	119,500
		Total Liabilities And Stockholders'	
Total Assets	<u>\$ 141,500</u>	Equity	<u>\$ 141,500</u>

P1-51B

Prepare a corrected balance sheet.

Solution:

BEAUTIFUL WORLD LANDSCAPING			
Balance Sheet			
July 31, 2016			
Assets		Liabilities	
Cash	\$ 5,500	Accounts Payable	\$ 2,400
Accounts Receivable	1,900	Notes Payable	24,600
Office Supplies	300	Total Liabilities	27,000
Office Furniture	5,600		
Land	34,100	Stockholders' Equity	
		Common Stock	6,000
		Retained Earnings	14,400
		Total Stockholders' Equity	20,400
		Total Liabilities and Stockholders'	
Total Assets	<u>\$ 47,400</u>	Equity	<u>\$ 47,400</u>

P1-52B**Requirements**

1. Analyze the effects of the events on the accounting equation of the Andre Simmon, CPA.
2. Prepare the following financial statements:
 - a. Income statement
 - b. Statement of retained earnings.
 - c. Balance sheet

Solution:

Requirement 1

	Assets				=	Liabilities	+	Equity				
	Cash	+ Accounts Receivable	+ Office Supplies	+ Office Furniture	=	Accounts Payable	+ Common Stock	- Dividends	+ Service Revenue	- Rent Expense	- Utilities Expense	
5	65,000						65,000					
Bal.	\$65,000				=		+ \$65,000					
6	-300		300									
Bal.	\$64,700		+ \$300		=		+ \$65,000					
7				6,800		6,800						
Bal.	\$64,700		+ \$300	+ \$6,800	=	\$6,800	+ \$65,000					
10	3,300									3,300		
Bal.	\$68,000		+ \$300	+ \$6,800	=	\$6,800	+ \$65,000		+ \$3,300			
11	-100											-100
Bal.	\$67,900		+ \$300	+ \$6,800	=	\$6,800	+ \$65,000		+ \$3,300		- \$ (100)	
12		12,500								12,500		
Bal.	\$67,900	+ \$12,500	+ \$300	+ \$6,800	=	\$6,800	+ \$65,000		+ \$15,800		- \$ 100	
18	-1,000											-1,000
Bal.	\$66,900	+ \$12,500	+ \$300	+ \$6,800	=	\$6,800	+ \$65,000		+ \$15,800	- \$ 1,000	- \$100	
25	12,500	-12,500										
Bal.	\$79,400	0	+ \$300	+ \$6,800	=	\$6,800	+ \$65,000		+ \$15,800	- \$ 1,000	- \$100	
27	-6,800					-6,800						
Bal.	\$72,600		+ \$300	+ \$6,800	=	\$0	+ \$65,000		+ \$15,800	- \$ 1,000	- \$100	
28	-3,000							-3,000				
Bal.	\$69,600	+ 0	+ \$300	+ \$6,800	=	\$0	+ \$65,000	- \$3,000	+ \$15,800	- \$ 1,000	- \$100	

Requirement 2a

ANDRE SIMMON, CPA Income Statement Month Ended Febraury 29, 2016		
Revenue:		
Service Revenue		\$15,800
Expenses:		
Rent Expense	\$ 1,000	
Utilities Expense	\$100	
Total Expenses		1,100
Net Income		<u>\$14,700</u>

Requirement 2b

ANDRE SIMMON, CPA Statement of Retained Earnings Month Ended Febraury 29, 2016	
Retained Earnings, February 1, 2016	\$ 0
Net income for the month	\$14,700
	14,700
Dividends	(3,000)
Retained Earnings, February 29, 2016	<u>\$11,700</u>

Requirement 2c

ANDRE SIMMON, CPA Balance Sheet February 29, 2016			
Assets		Liabilities	
Cash	\$69,600		
Office Supplies	300		
Furniture	6,800	Stockholders' Equity	
		Common Stock	\$65,000
		Retained Earnings	11,700
		Total Stockholders' Equity	76,700
		Total Liabilities and Stockholders'	
Total Assets	<u>\$76,700</u>	Equity	<u>\$76,700</u>

P1-53B**Requirements**

1. Analyze the effects of the preceding events on the accounting equation of Ariana Peterson, Attorney.
2. Prepare the following financial statements:
 - a. Income statement
 - b. Statement of retained earnings.
 - c. Balance sheet

Solution:

Requirement 1

	Assets				=	Liabilities	+	Equity				
								Contributed Capital	+	Retained Earnings		
	Cash	+ Accounts Receivable	+ Office Supplies	+ Computer	=	Accounts Payable	+ Common Stock	- Dividends	+ Service Revenue	- Utility Expense	- Misc. Expense	
3	65,000						65,000					
5	-400		400									
Bal.	\$64,600		\$400		=		\$65,000					
7				6,800		6,800						
Bal.	\$64,600		\$400	\$6,800	=	\$6,800	\$65,000					
9	2,900								2,900			
Bal.	\$67,500		\$400	\$6,800	=	\$6,800	\$65,000		\$2,900			
15						300						-300
Bal.	\$67,500		\$400	\$6,800	=	\$7,100	\$65,000		\$2,900			\$300
23		18,000							18,000			
Bal.	\$67,500	\$18,000	\$400	\$6,800	=	\$7,100	\$65,000		\$20,900			\$300
28	-300					-300						
Bal.	\$67,200	\$18,000	\$400	\$6,800	=	\$6,800	\$65,000		\$20,900			\$300
30	-840											-840
Bal.	\$66,360	\$18,000	\$400	\$6,800	=	\$6,800	\$65,000		\$20,900	\$840		\$300
31	2,800	-2,800										
Bal.	\$69,160	\$15,200	\$400	\$6,800	=	\$6,800	\$65,000		\$20,900	\$840		\$300
31	-2,500							-2,500				
Bal.	\$66,660	\$15,200	\$400	\$6,800	=	\$6,800	\$65,000	\$2,500	\$20,900	\$840		\$300

Requirement 2a

ARIANA PETERSON, ATTORNEY Income Statement Month Ended December 31, 2016	
Revenues:	
Service Revenue	\$20,900
Expenses:	
Utility Expense	\$840
Miscellaneous Expense	\$300
Total Expenses	\$1,140
Net Income	<u>\$19,760</u>

Requirement 2b

ARIANA PETERSON, ATTORNEY Statement of Retained Earnings Month Ended December 31, 2016	
Retained Earnings, December 1, 2016	\$ 0
Net income for the month	\$19,760
	<u>19,760</u>
Dividends	(2,500)
Retained Earnings, December 31, 2016	<u>\$ 17,260</u>

Requirement 2c

ARIANA PETERSON, ATTORNEY Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$66,660	Accounts Payable	\$6,800
Accounts Receivable	15,200		
Office Supplies	400	Stockholders' Equity	
Computer	6,800	Common Stock	65,000
		Retained Earnings	17,260
		Total Stockholders' Equity	82,260
		Total Liabilities and Stockholders'	
Total Assets	<u>\$89,060</u>	Equity	<u>\$89,060</u>

P1-54

Requirements

1. Analyze the effects of Daniels Consulting's transactions on the accounting equation. Use the format of Exhibit 1-5, and include these headings: Cash; Accounts Receivable; Office Supplies; Equipment; Furniture; Accounts Payable; Unearned Revenue; Common Stock; Dividends; Service Revenue; Rent Expense; and Utilities Expense.
2. Prepare the income statement of Daniels Consulting for the month ended December 31, 2016.
3. Prepare the statement of retained earnings for the month ended December 31, 2016.
4. Prepare the balance sheet as of December 31, 2016.
5. Calculate the return on assets for Daniel Consulting.

Solution:

Requirement 1

Assets						=	Liabilities		+	Equity															
										Contributed Capital	+	Retained Earnings													
	Cash	+	Accounts Receivable	+	Office Supplies	+	Equipment	+	Furniture	=	Accounts Payable	+	Unearned Revenue	+	Common Stock	-	Dividends	+	Service Revenue	-	Rent Expense	-	Utilities Expense		
(1)	20,000														20,000										
(2)	-2,000																					-2,000			
Bal.	\$18,000									=					+	\$20,000					-	\$2,000			
(3)	-3,600						3,600																		
Bal.	\$14,400					+	\$3,600			=					+	\$20,000					-	\$2,000			
(4)									3,000		3,000														
Bal.	\$14,400					+	\$3,600	+	\$3,000	=	\$3,000				+	\$20,000					-	\$2,000			
(5)					800						800														
Bal.	\$14,400			+	\$800	+	\$3,600	+	\$3,000	=	\$3,800				+	\$20,000					-	\$2,000			
(9)			2,500																		2,500				
Bal.	\$14,400	+	\$2,500	+	\$800	+	\$3,600	+	\$3,000	=	\$3,800				+	\$20,000			+	\$2,500		-	\$2,000		
(12)	-150																						-150		
Bal.	\$14,250	+	\$2,500	+	\$800	+	\$3,600	+	\$3,000	=	\$3,800				+	\$20,000			+	\$2,500		-	\$2,000	-	\$150
(18)	2,100																				2,100				
Bal.	\$16,350	+	\$2,500	+	\$800	+	\$3,600	+	\$3,000	=	\$3,800				+	\$20,000			+	\$4,600		-	\$2,000	-	\$150
(21)	2,400												2,400												
Bal.	\$18,750	+	\$2,500	+	\$800	+	\$3,600	+	\$3,000	=	\$3,800	+	\$2,400	+	\$20,000				+	\$4,600		-	\$2,000	-	\$150
(26)	-200										-200														
Bal.	\$18,550	+	\$2,500	+	\$800	+	\$3,600	+	\$3,000	=	\$3,600	+	\$2,400	+	\$20,000				+	\$4,600		-	\$2,000	-	\$150
(28)	400	-400																							
Bal.	\$18,950	+	\$2,100	+	\$800	+	\$3,600	+	\$3,000	=	\$3,600	+	\$2,400	+	\$20,000				+	\$4,600		-	\$2,000	-	\$150
(30)	-1,000																				-1,000				
Bal.	\$17,950	+	\$2,100	+	\$800	+	\$3,600	+	\$3,000	=	\$3,600	+	\$2,400	+	\$20,000		-	1,000	+	\$4,600		-	\$2,000	-	\$150

Requirement 2

DANIELS CONSULTING Income Statement Month Ended December 31, 2016		
Revenue:		
Service Revenue		\$4,600
Expenses:		
Rent Expense	\$2,000	
Utilities Expense	\$150	
Total Expense		\$2,150
Net Income		<u>\$2,450</u>

Requirement 3

DANIELS CONSULTING Statement of Retained Earnings Month Ended December 31, 2016		
Retained Earnings, December 1, 2016		
	\$	0
Net income for the month		<u>\$2,450</u>
		2,450
Dividends		(1,000)
Retained Earnings, December 31, 2016	\$	<u>1,450</u>

Requirement 4

DANIELS CONSULTING Balance Sheet December 31, 2016			
Assets		Liabilities	
Cash	\$17,950	Accounts Payable	\$3,600
Accounts Receivable	2,100	Unearned Revenue	2,400
Office Supplies	800	Total Liabilities	6,000
Equipment	3,600	Stockholders' Equity	
Furniture	3,000	Common Stock	20,000
		Retained Earnings	1,450
		Total Stockholder's Equity	21,450
		Total Liabilities and Stockholders'	
Total Assets	<u>\$27,450</u>	Equity	<u>\$ 27,450</u>

Requirement 5

Average total assets = $(\$0 + \$27,450) / 2 = \$13,725$
Return on assets = $\text{Net income} / \text{Average total assets} = \$2,450 / \$13,725 = 0.147 = 17.9\%$

Decision Case 1-1**Requirements**

1. Which business has more assets?
2. Which business owes more to creditors?
3. Which business has more stockholders' equity at the end of the year?
4. Which business brought in more revenue?
5. Which business is more profitable?
6. Which of the foregoing questions do you think is most important for evaluating these two businesses? Why?
7. Which business looks better from a financial standpoint?

Solution:**Requirement 1**

Greg's Tunes has more assets.
Sal's \$23,000, Greg's \$25,000 (\$10,000 + \$6,000 + \$9,000)

Requirement 2

Greg's Tunes owes more to creditors.
Sal's \$2,000 (\$23,000 – (\$8,000 + \$35,000 – \$22,000)), Greg's \$10,000

Requirement 3

Sal's Silly Songs has more stockholders' equity
Sal's \$21,000 (\$8,000 + \$35,000 – \$22,000) Greg's \$15,000 (\$6,000 + \$9,000)

Requirement 4

Greg's Tunes earned more revenue.
Sal's \$35,000, Greg's \$53,000 (\$9,000 + \$44,000)

Requirement 5

Sal's Silly Songs is more profitable.
Sal's \$13,000 ($\$35,000 - \$22,000$), Greg's \$9,000

Requirement 6

This question is opinion based. More profit is good, which means
Sal's has the advantage. Greg's also owes more to creditors which is risky.
Sal's has much more equity, which minimizes risk.

Requirement 7

Sal's looks financially better, because Sal earned more net income on less total <input type="checkbox"/>
revenue. Sal also owes less to creditors and has more equity.

Ethical Issue 1-1

Requirements

- 1. Suppose you are the chief financial officer (CFO) responsible for the financial statements of Philip Morris. What ethical issue would you face as you consider what to report in your company’s annual report about the cash payments? What is the ethical course of action for you to take in this situation?
- 2. What are some of the negative consequences to Philip Morris for not telling the truth? What are some of the negative consequences to Philip Morris for telling the truth?

Solution:

Requirement 1

The chief financial officer (CFO) of Philip Morris would be torn between addressing the fact that the payments are related to illnesses caused by the company’s products, or alternatively, omitting or concealing this fact. The ethical course of action for the CFO is to be open, honest and forthcoming about the reasons for the payments.

Requirement 2

Negative consequences of not telling the truth are as follows: If users of the financial statements feel they are only getting part of the truth, or that the reports are distorting the information, which will damage the credibility of the company, and damage the company’s reputation.
Negative consequences of telling the truth include painting so bleak a picture effects of smoking that investors will view Philip Morris as too risky and stop buying the company’s stock. Another negative consequence would be to create the impression that the company is engaged in unethical behavior by selling a product that damages people’s health.

Fraud Case 1-1**Requirements**

1. How would this action affect the year-end income statement? How would it affect the year-end balance sheet?
2. If you were one of the company's creditors, how would this fraudulent action affect you?

Solution:**Requirement 1**

The proposed action would increase net income by increasing revenues.
It would distort the balance sheet by understating liabilities and overstating equity.

Requirement 2

By making the company's financial situation look better than it actually was, the company's creditors would likely be more willing to extend credit to the company, and offer the credit at a lower interest rate.

Financial Statement Case 1-1**Requirements**

1. How much in cash (including cash equivalents) did Starbucks Corporation have on September 29, 2013?
2. What were the company's total assets at September 29, 2013? At September 30, 2012?
3. Write the company's accounting equation at September 29, 2013.
4. Identify total net sales (revenues) for the year ended September 29, 2013. How much did total revenue increase or decrease from 2012 to 2013?
5. How much net income (net earnings) or net loss did Starbucks earn for 2013 and for 2012? Based on net income, was 2013 better or worse than 2012?
6. Calculate Starbucks Corporation's return on assets for year ending
7. How did Starbucks Corporation's return on assets compare to Green Mountain Coffee Roasters, Inc.'s return on assets?

Solution:**Requirement 1**

\$2,575.7 (in millions)

Requirement 2

\$11,516.7 (in millions) at September 29, 2013;
\$8,219.2 (in millions) at September 30, 2012

Requirement 3

Assets	=	Liabilities	+	Equity
\$11,516.7	=	\$7,034.4	+	\$4,482.30
(shown in millions)				

Requirement 4

\$14,892.2 (in millions) for year ended September 29, 2013
This is an increase of \$1,592.7 (in millions) over 2012. ($\$14,892.2 - \$13,299.5$)

Requirement 5

\$8.3 (in millions) in 2013
\$1,383.8 (in millions) in 2012
2012 was better than 2013.

Requirement 6

Average total assets = $(\$8,219.2 + \$11,516.7) / 2 = \$9,867.95$ (rounded)
Return on assets = $\$8.3 / \$9,867.95 = 0.0008 = 0.08\%$

Requirement 7

Starbucks Corporation's return on assets (0.08%)
was significantly lower than Green Mountain Coffee Roasters, Inc. (13.1%).