Chapter 2—Analyzing Transactions: The Accounting Equation

TRUE/FALSE

1. A business entity is an individual, association, or organization with control over economic resources and which engages in economic activities.

   ANS: T PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-03-Business Forms KEY: Bloom's: Knowledge
   NOT: 1 min.

2. Liabilities represent an "inside" interest in a business.

   ANS: F PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-03-Business Forms KEY: Bloom's: Knowledge
   NOT: 1 min.

3. The accounting equation shows the relationship among the three basic accounting elements—assets, revenues, and owner's equity.

   ANS: F PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-2 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

4. If owner's equity and liabilities increased during the period, then assets must also have increased.

   ANS: T PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-2 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

5. An accounts payable is an unwritten promise to pay a supplier for assets purchased or services rendered.

   ANS: T PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

6. If the revenue of a period exceeds the expenses, the excess represents a net loss.

   ANS: F PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Evaluation
   NOT: 1 min.

7. Any accounting period of twelve months' duration is usually referred to as a calendar year.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

8. Revenues received during an accounting period increase owner's equity.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

9. Since supplies last for several months, they are recorded as assets.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

10. Since insurance lasts for several months, it is recorded as owner's equity.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

11. The income statement provides information about events over a period of a month, year, or other period of time.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

12. The terms "profit and loss statement" or "operating statement" are sometimes used as synonyms for the balance sheet.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

13. Other terms used for owner's equity include net worth and capital.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

14. Any item a business owns that will provide future benefits is called owner's equity.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

15. It is not necessary to measure a business transaction in dollars.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-3 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

16. The accounting equation may be expressed as assets − liabilities = owner's equity.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-2 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

17. According to the business entity concept, a proprietor may include nonbusiness assets and liabilities in the business entity's accounting records.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

18. Recognizing the effects of transactions on assets, liabilities, owner's equity, revenue, and expenses of a business is the processing function.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-6 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-06-Recording Transactions KEY: Bloom's: Comprehension
NOT: 1 min.

19. Expenses represent a decrease in liabilities.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

20. Expenses that are incurred in operating the enterprise increase owner's equity.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Comprehension
NOT: 1 min.

21. Withdrawing cash from a business entity will result in an increase in owner's equity.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Comprehension
NOT: 1 min.

22. An increase in a revenue account may also result in an increase in the accounts receivable account.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Comprehension
NOT: 1 min.

23. Financial statements commonly prepared by businesses include an income statement, a statement of owner's equity, and a balance sheet.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

24. The statement of owner's equity shows the state of the business on a specific date.

ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

25. The balance sheet reports assets, liabilities, and owner's equity on a specific date.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

26. The income statement and statement of owner's equity provide information covering a period of time.

ANS: T PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

MULTIPLE CHOICE

1. The accounting equation may be expressed as
   a. owner's equity = assets – liabilities.
   b. revenue – expenses = net income.
   c. revenue = net income – expenses.
   d. liabilities – owner's equity = assets.

ANS: A PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-2 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

2. Jason purchased office equipment for $4,800 on account. This transaction would
   a. increase assets and increase owner's equity.
   b. increase assets and increase liabilities.
   c. increase one asset and decrease another asset.
   d. decrease assets and decrease liabilities.

   ANS: B PTS: 1 DIF: Difficulty: Moderate
   OBJ: LO: 2-4 NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

3. Stephen purchased office supplies for $800 in cash. This transaction would
   a. increase assets and increase owner's equity.
   b. increase one asset and decrease another asset.
   c. increase assets and increase liabilities.
   d. decrease assets and decrease liabilities.

   ANS: B PTS: 1 DIF: Difficulty: Moderate
   OBJ: LO: 2-4 NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

4. Meghan started her business by investing $30,000 in cash. This transaction would
   a. increase assets and increase owner's equity.
   b. increase assets and increase liabilities.
   c. increase one asset and decrease another asset.
   d. decrease assets and decrease liabilities.

   ANS: A PTS: 1 DIF: Difficulty: Moderate
   OBJ: LO: 2-4 NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

5. Any accounting period of twelve months' duration is usually referred to as a(n)
   a. fiscal year.
   b. calendar year.
   c. physical year.
   d. operational year.

   ANS: A PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA BB-Industry
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

6. Increases to owner's equity may be from
   a. expenses that are incurred.
   b. expenses exceeding revenue for the period.
   c. withdrawals of cash from the business by the owner.
   d. revenue that is derived from sales of goods or services.

   ANS: D PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-4 NAT: BUSPROG: Communication
   STA: AICPA BB-Critical Thinking TOP: ACBSP: APC-09-Financial Statements
   KEY: Bloom's: Comprehension NOT: 1 min.

7. Tyler paid $3,700 on account to the company from which equipment was purchased on credit. This transaction would
   a. decrease assets and decrease liabilities.
   b. increase assets and increase owner's equity.
   c. increase assets and increase liabilities.
   d. increase one asset and decrease another asset.

   ANS: A PTS: 1 DIF: Difficulty: Moderate
   OBJ: LO: 2-4 NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

8. An example of an expense is
   a. investments.
   b. supplies consumed.
   c. prepaid insurance.
   d. withdrawals by the owner.

   ANS: B PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
   TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
   NOT: 1 min.

9. A decrease in owner's equity may result from a(n)
   a. purchase of office supplies for cash.
   b. withdrawal of cash from the business by the owner.
   c. revenue that is derived from sales of goods or services.
   d. investment of cash in the business by the owner.

   ANS: B PTS: 1 DIF: Difficulty: Easy
   OBJ: LO: 2-4 NAT: BUSPROG: Analytic
   STA: AICPA BB-Critical Thinking TOP: ACBSP: APC-09-Financial Statements
   KEY: Bloom's: Comprehension NOT: 1 min.

10. Which phase of the accounting process involves recognizing the effect of transactions on assets, liabilities, owner's equity, revenue, and expenses of a business?
    a. input
    b. processing
    c. output
    d. summarizing

    ANS: B PTS: 1 DIF: Difficulty: Easy
    OBJ: LO: 2-6 NAT: BUSPROG: Communication STA: AICPA BB-Industry
    TOP: ACBSP: APC-06-Recording Transactions KEY: Bloom's: Knowledge
    NOT: 1 min.

11. The financial statement that should be completed first is the
    a. balance sheet.
    b. statement of financial position.
    c. statement of financial condition.
    d. income statement.

    ANS: D PTS: 1 DIF: Difficulty: Easy
    OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
    TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Analysis
    NOT: 1 min.

12. Falana received $7,000 in cash from a client for professional services rendered. This transaction would
    a. increase assets and increase owner's equity.
    b. decrease assets and increase owner's equity.
    c. increase liabilities and decrease owner's equity.
    d. decrease assets and decrease owner's equity.

    ANS: A PTS: 1 DIF: Difficulty: Moderate
    OBJ: LO: 2-4 NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
    TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
    NOT: 1 min.

13. The financial statement that shows the state of the firm's assets, liabilities, and owner's equity on a specific date is called a(n)
    a. balance sheet.
    b. statement of operations.
    c. statement of owner's equity.
    d. income statement.

    ANS: A PTS: 1 DIF: Difficulty: Easy
    OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA FN-Measurement
    TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Analysis
    NOT: 1 min.

14. Sue Lee paid $1,200 for office rent. This transaction would
    a. increase assets and decrease owner's equity.
    b. increase assets and increase liabilities.
    c. decrease assets and decrease liabilities.
    d. decrease assets and decrease owner's equity.

    ANS: D PTS: 1 DIF: Difficulty: Moderate
    OBJ: LO: 2-4 NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
    TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
    NOT: 1 min.

PROBLEM

1. Match the letter corresponding to one of the basic elements of accounting to each of the accounts below.

   A = Asset
   L = Liability
   OE = Owner's Equity
   R = Revenue
   E = Expense

   1. Utility Expense __________
   2. Accounts Payable __________
   3. Prepaid Rent __________
   4. Supplies __________
   5. P. Coyote, Drawing __________
   6. Wages Expense __________
   7. P. Coyote, Capital __________
   8. Cash __________
   9. Advertising Expense __________
   10. Fees Earned __________

ANS:
1. E
2. L
3. A
4. A
5. OE
6. E
7. OE
8. A
9. E
10. R

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-4
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 5 min.

2. Show the effect of each transaction on the three basic accounting elements by indicating the dollar amount of the increase or decrease under the proper element heading. Compute the resulting accounting equation.

a. Owner invested $16,500 cash in the business.
b. Paid premium for two-year insurance policy, $1,500.
c. Purchased a van valued at $35,000 with $5,000 down payment; the balance to be paid over three years.
d. Paid the rent for the month, $900.
e. Purchased $470 of supplies for cash.
f. Cash sales for the month, $8,750.
g. Billed credit customers $14,200 for monthly services.
h. Paid monthly utility bill, $210.
i. Owner withdrew $2,200 for personal use.
j. Received payments of $3,300 from credit customers.

					ASSETS					=	>
	Cash	+	**Accounts Rec.**	+	**Supplies**	+	**Prepaid Ins.**	+	**Van**	=	>
											>
a.	_____		_____		_____		_____		_____		>
b.	_____		_____		_____		_____		_____		>
c.	_____		_____		_____		_____		_____		>
d.	_____		_____		_____		_____		_____		>
e.	_____		_____		_____		_____		_____		>
f.	_____		_____		_____		_____		_____		>
g.	_____		_____		_____		_____		_____		>
h.	_____		_____		_____		_____		_____		>
i.	_____		_____		_____		_____		_____		>
j.	_____		_____		_____		_____		_____		>
	_____		_____		_____		_____		_____		>

		LIAB.	+			OWNER'S EQUITY				
<		Notes Payable	+	Capital	–	Drawing	+	Revenues	–	Expenses
<										
<	a.	_____		_____		_____		_____		_____
<	b.	_____		_____		_____		_____		_____
<	c.	_____		_____		_____		_____		_____
<	d.	_____		_____		_____		_____		_____
<	e.	_____		_____		_____		_____		_____
<	f.	_____		_____		_____		_____		_____
<	g.	_____		_____		_____		_____		_____
<	h.	_____		_____		_____		_____		_____
<	i.	_____		_____		_____		_____		_____
<	j.	_____		_____		_____		_____		_____
<		_____		_____		_____		_____		_____

PROOF

Cash	_____	Notes Payable	_____
Accounts Receivable	_____	Capital	_____
Supplies	_____	Drawing	_____
Prepaid Insurance	_____	Revenues	_____
Van	_____	Expenses	_____
	_____		_____

ANS:

					ASSETS					=	>
	Cash	+	Accounts Rec.	+	Supplies	+	Prepaid Ins.	+	Van	=	>
											>
a.	16,500										>
b.	(1,500)						1,500				>
c.	(5,000)								35,000		>
d.	(900)										>
e.	(470)				470						>
f.	8,750										>
g.			14,200								>
h.	(210)										>
i.	(2,200)										>
j.	3,300		(3,300)								>
	18,270		10,900		470		1,500		35,000		>

		LIAB.	+			OWNER'S EQUITY				
<		Note Payable	+	Capital	–	Drawing	+	Revenues	–	Expenses
<										
<	a.			16,500						
<	b.									
<	c.	30,000								
<	d.									900
<	e.									

<	f.				8,750	
<	g.				14,200	
<	h.					210
<	i.			2,200		
<	j.					
<		30,000	16,500	2,200	22,950	1,110

PROOF

Cash	18,270	Notes Payable	30,000
Accounts Receivable	10,900	Capital	16,500
Supplies	470	Drawing	(2,200)
Prepaid Insurance	1,500	Revenues	22,950
Van	35,000	Expenses	(1,110)
	66,140		66,140

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-2 | LO: 2-3 | LO: 2-4
NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
TOP: ACBSP: APC-06-Recording Transactions KEY: Bloom's: Application
NOT: 15 min.

3. Show the effects of each transaction on the accounting equation by indicating under the proper heading the dollar amount of increase or decrease for each transaction listed below. Compute the resulting accounting equation.

a. Owner deposited $20,000 in his new business checking account.
b. Supplies were purchased for $300 on account.
c. Paid a $1,200 premium for six months of liability insurance.
d. Purchased supplies for $200 cash.
e. Purchased equipment for $4,000 by paying $1,000; the rest to be paid in six months.
f. Paid the $300 bill outstanding (from transaction b).
g. Owner withdrew $700 from the business for personal use.

				ASSETS				=	**LIAB.**	+		**OWNER'S EQUITY**		
	Cash	+	**Supp.**	+	**Prep. Insur.**	+	**Equip**	=	**Accts. Pay.**	+	**Capital**	–	**Drawing**	
a.	_____		_____		_____		_____		_____		_____		_____	
b.	_____		_____		_____		_____		_____		_____		_____	
c.	_____		_____		_____		_____		_____		_____		_____	
d.	_____		_____		_____		_____		_____		_____		_____	
e.	_____		_____		_____		_____		_____		_____		_____	
f.	_____		_____		_____		_____		_____		_____		_____	
g.	_____		_____		_____		_____		_____		_____		_____	
	_____		_____		_____		_____		_____		_____		_____	

ANS:

	ASSETS							=	LIAB.	+	OWNER'S EQUITY		
	Cash	+	Supp.	+	Prep. Insur.	+	Equip	=	Accts. Pay.	+	Capital	–	Drawing
a.	20,000										20,000		
b.			300						300				
c.	(1,200)				1,200								
d.	(200)		200										
e.	(1,000)						4,000		3,000				
f.	(300)								(300)				
g.	(700)												700
	16,600		500		1,200		4,000		3,000		20,000		700

PROOF

Cash	16,600	Accounts Payable	3,000
Supplies	500	Capital	20,000
Prepaid Insurance	1,200	Drawing	(700)
Equipment	4,000		
	22,300		22,300

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-2 | LO: 2-3 | LO: 2-4
NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
TOP: ACBSP: APC-06-Recording Transactions KEY: Bloom's: Application
NOT: 15 min.

4. Madame Shira began a fortune telling business on May 1. The following transactions occurred:

1. Owner Madame Shira invested $5,000 cash in the business.
2. Purchased $2,000 of furniture with a down payment of $500; the rest by issuing an account payable to be paid in three monthly installments.
3. Paid $700 rent.
4. Purchased a crystal ball for $300.
5. Paid $1,700 for a 12-month insurance policy.
6. During the first month received $2,500 from cash customers.
7. Sent billings of $2,000 for services rendered to credit customers.
8. Paid assistant $1,500 wages for the month.
9. Received $600 in payments from credit customers.
10. Borrowed $3,200 by signing a note.
11. Made a $500 payment on the furniture bill (from transaction 2).
12. Owner withdrew $300 cash for personal use.
13. Paid bills for advertising $60, utilities $39, and repairs $52.

Required:
1. Enter the above transactions in an accounting equation work sheet.
2. Prepare an income statement for Madame Shira for the month of May.
3. Prepare a statement of owner's equity for the month of May.

ANS:

1.

	ASSETS					= LIABILITIES		+ OWNER'S EQUITY				
	Cash	+ Furniture	+ Crystal Ball	+ Accounts Rec.	+ Prepaid Ins.	= Accounts Payable	+ Notes Payable	+ Shira, Capital	– Shira, Drawing	+ Revenues	– Expenses	Desc.
1.	5,000							5,000				
2.	(500)	2,000				1,500						
3.	(700)										700	Rent
4.	(300)		300									
5.	(1,700)				1,700							
6.	2,500									2,500		
7.				2,000						2,000		
8.	(1,500)										1,500	Wages
9.	600			(600)								
10.	3,200						3,200					
11.	(500)					(500)						
12.	(300)								300			
13.	(60)										60	Advertising
	(39)										39	Utilities
	(52)										52	Repairs
	5,649	2,000	300	1,400	1,700	1,000	3,200	5,000	300	4,500	2,351	

2.

Madame Shira Fortune Telling
Income Statement
For Month Ended May 31, 20--

Revenues:		
Fortune telling fees		$4,500
Expenses:		
Rent expense	$ 700	
Wages expense	1,500	
Advertising expense	60	
Utilities expense	39	
Repairs expense	52	
Total expenses		2,351
Net income		$2,149

3.

Madame Shira Fortune Telling
Statement of Owner's Equity
For Month Ended May 31, 20--

Madame Shira, capital May 1, 20--		$ 0
Investment by owner		5,000
Net income for May	$2,149	
Less withdrawals for May	300	
Increase in capital		1,849
Madame Shira, capital May 31, 20--		$6,849

PTS: 1 DIF: Difficulty: Moderate OBJ: LO: 2-3 | LO: 2-4 | LO: 2-5
NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
TOP: ACBSP: APC-06-Recording Transactions KEY: Bloom's: Application
NOT: 15 min.

5. From the following list of accounts, prepare an income statement, statement of owner's equity, and balance sheet for the year ended or at December 31, 20--, for Milner's Star Express Cleaning Service.

Cash	$ 2,026
Fees Earned	13,835
Accounts Payable	7,530
D. Milner, Capital January 1, 20--	6,000
D. Milner, Drawing	1,750
Utilities Expense	153
Prepaid Insurance	1,216
Rent Expense	1,200
Accounts Receivable	4,080
Equipment	15,290
Wages Expense	1,650

ANS:

Milner's Star Express Cleaning Service
Income Statement
For the Year Ended December 31, 20--

Revenues:		
Fees earned		$13,835
Expenses:		
Utilities expense	$ 153	
Rent expense	1,200	
Wages expense	1,650	
Total expenses		3,003
Net income		$10,832

Milner's Star Express Cleaning Service
Statement of Owner's Equity
For the Year Ended December 31, 20--

D. Milner, capital January 1, 20--		$ 6,000
Net income for the year	$10,832	
Less withdrawals for the year	1,750	
Increase in capital		9,082
D. Milner, capital December 31, 20--		$15,082

Milner's Star Express Cleaning Service
Balance Sheet
December 31, 20--

Assets		**Liabilities**	
Cash	$ 2,026	Accounts payable	$ 7,530
Prepaid insurance	1,216		
Accounts receivable	4,080	**Owner's Equity**	
Equipment	15,290	D. Milner, capital	15,082
Total assets	$22,612	Total liab. & owner's equity	$22,612

PTS: 1 DIF: Difficulty: Moderate OBJ: LO: 2-5
NAT: BUSPROG: Analytic STA: AICPA FN-Reporting
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Application
NOT: 15 min.

6. From the following list of accounts, prepare an income statement, statement of owner's equity, and balance sheet for the year ended or at December 31, 20--, for J. Carr's Delivery Service.

Cash	$11,450
Accounts Payable	4,450
Fees Earned	41,500
J. Carr, Capital January 1, 20--	14,500
J. Carr, Drawing	7,000
Office Supplies	250
Rent Expense	10,000
Accounts Receivable	7,000
Equipment	6,000
Wages Expense	14,000
Repairs Expense	250
Furniture	4,500

ANS:

J. Carr's Delivery Service
Income Statement
For the Year Ended December 31, 20--

Revenues:		
Fees earned		$41,500
Expenses:		
Rent expense	$10,000	
Wages expense	14,000	
Repairs expense	250	
Total expenses		24,250
Net income		$17,250

J. Carr's Delivery Service
Statement of Owner's Equity
For the Year Ended December 31, 20--

J. Carr, capital January 1, 20--		$14,500
Net income for the year	$17,250	
Less withdrawals for the year	7,000	
Increase in capital		10,250
J. Carr, capital December 31, 20--		$24,750

J. Carr's Delivery Service
Balance Sheet
December 31, 20--

Assets		**Liabilities**	
Cash	$11,450	Accounts Payable	$ 4,450
Accounts receivable	7,000		
Office supplies	250		
Equipment	6,000	**Owner's Equity**	
Furniture	4,500	J. Carr, capital	24,750
Total assets	$29,200	Total liab. & owner's equity	$29,200

PTS: 1 DIF: Difficulty: Moderate OBJ: LO: 2-5
NAT: BUSPROG: Analytic STA: AICPA FN-Reporting
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Application
NOT: 15 min.

7. Dr. Etana Jenson is a podiatrist. As of December 31, Jenson owned the following assets related to the professional practice:

Cash	$6,600	X-ray Equipment	$9,000
Office Equipment	3,500	Laboratory Equipment	3,000

As of that date, Jenson owed business suppliers as follows:

Top Flight Office Equipment Co.	$3,000
Dunhill Medical Supplies Company	1,000
Island Gas Company	2,200

Required:

a. Compute the amount of assets, liabilities, and owners' equity as of December 31.

Assets	=	Liabilities	+	Owner's Equity
________________		________________		________________

b. Assuming that during January there is an increase of $4,600 in Dr. Jenson's business assets and an increase of $2,500 in the business liabilities, compute the resulting equation as of January 31.

________________ ________________ ________________

c. Assuming that during February there is a decrease of $1,500 in assets and a decrease of $1,200 in liabilities, compute the resulting accounting equation as of February 28.

________________ ________________ ________________

ANS:

	Assets	**=**	**Liabilities**	**+**	**Owner's Equity**
a.	$22,100	=	$6,200	+	$15,900
b.	26,700	=	8,700	+	18,000
c.	25,200	=	7,500	+	17,700

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-3 | LO: 2-4
NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Comprehension
NOT: 3 min.

8. Kristin Holden started her own consulting business in July, 20--. During the first month, the following transactions occurred:

a. Owner invested $12,000 cash in the business.
b. Purchased office equipment for $7,500 cash.
c. Purchased computer equipment costing $11,500 on account.
d. Paid $1,100 office rent for the month.
e. Received $1,700 cash from a client for services rendered.
f. Paid water bill for the month, $170.
g. Paid $2,400 on account for computer equipment purchased in transaction (c).
h. Paid the electric bill for the month, $200.

Required:
Record the effects of these transactions in an accounting equation worksheet.

			ASSETS			**=**	**LIABILITIES**			>
			Office		**Computer**		**Accounts**		**K. Holden,**	>
	Cash	**+**	**Equip.**	**+**	**Equip.**	**=**	**Payable**	**+**	**Capital**	
a.	_____		_____		_____		_____		_____	>
Bal.	_____		_____		_____		_____		_____	>
b.	_____		_____		_____		_____		_____	>
Bal.	_____		_____		_____		_____		_____	>
c.	_____		_____		_____		_____		_____	>
Bal.	_____		_____		_____		_____		_____	>
d.	_____		_____		_____		_____		_____	>
Bal.	_____		_____		_____		_____		_____	>
e.	_____		_____		_____		_____		_____	>

Bal.	_____	_____	_____	_____	_____	>
f.	_____	_____	_____	_____	_____	>
Bal.	_____	_____	_____	_____	_____	>
g.	_____	_____	_____	_____	_____	>
Bal.	_____	_____	_____	_____	_____	>
h.	_____	_____	_____	_____	_____	>
Bal.	_____	_____	_____	_____	_____	>

<	+			**OWNER'S EQUITY**			
<			**Client**				**Utilities**
		+	**Fees**	–	**Rent Expense**	–	**Expense**
<	a.		_____		_____		_____
<	Bal.		_____		_____		_____
<	b.		_____		_____		_____
<	Bal.		_____		_____		_____
<	c.		_____		_____		_____
<	Bal.		_____		_____		_____
<	d.		_____		_____		_____
<	Bal.		_____		_____		_____
<	e.		_____		_____		_____
<	Bal.		_____		_____		_____
<	f.		_____		_____		_____
<	Bal.		_____		_____		_____
<	g.		_____		_____		_____
<	Bal.		_____		_____		_____
<	h.		_____		_____		_____
<	Bal.		_____		_____		_____

ANS:

			ASSETS			=	**LIABILITIES**			>
			Office		**Computer**		**Accounts**		**K. Holden,**	>
	Cash	+	**Equip.**	+	**Equip.**	=	**Payable**	+	**Capital**	>
a.	12,000								12,000	>
Bal.	12,000								12,000	>
b.	(7,500)		7,500						______	>
Bal.	4,500		7,500						12,000	>
c.	______		______		11,500		11,500		______	>
Bal.	4,500		7,500		11,500		11,500		12,000	>
d.	(1,100)		______		______		______		______	>
Bal.	3,400		7,500		11,500		11,500		12,000	>
e.	1,700		______		______		______		______	>
Bal.	5,100		7,500		11,500		11,500		12,000	>
f.	(170)		______		______		______		______	>
Bal.	4,930		7,500		11,500		11,500		12,000	>
g.	(2,400)		______		______		(2,400)		______	>
Bal.	2,530		7,500		11,500		9,100		12,000	>
h.	(200)		______		______		______		______	>
Bal.	2,330		7,500		11,500		9,100		12,000	>

<		+	OWNER'S EQUITY				
			Client				**Utilities**
<		+	**Fees**	–	**Rent Expense**	–	**Expense**
<	a.						
<	Bal.						
<	b.						
<	Bal.						
<	c.						
<	Bal.						
<	d.				1,100		
<	Bal.						
<	e.		1,700		1,100		
<	Bal.		1,700		1,100		
<	f.						170
<	Bal.		1,700		1,100		170
<	g.						
<	Bal.		1,700		1,100		170
<	h.						200
<	Bal.		1,700		1,100		370

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-4
NAT: BUSPROG: Analytic STA: AICPA FN-Measurement
TOP: ACBSP: APC-06-Recording Transactions KEY: Bloom's: Knowledge
NOT: 10 min.

COMPLETION

1. Most businesses recognize ____________________ when earned, even if cash has not yet been received.

ANS: revenue

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-4
NAT: BUSPROG: Communication STA: AICPA FN-Measurement
TOP: ACBSP: APC-04-Cash vs. Accrual KEY: Bloom's: Knowledge
NOT: 1 min.

2. ____________________ represent the decrease in assets (or increase in liabilities) as a result of efforts made to produce revenues.

ANS: Expenses

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-4
NAT: BUSPROG: Communication STA: AICPA FN-Reporting
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

3. The ____________________, sometimes called the profit and loss statement, reports the profitability of business operations for a specific period of time.

ANS: income statement

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-5
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

4. ____________________ represent the amount a business charges customers for products sold or services performed.

ANS: Revenues

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-4
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

5. The relationship between the three basic accounting elements: ____________________, ____________________, and ____________________, can be expressed in the form of a simple equation known as the accounting equation.

ANS:
assets, liabilities, owner's equity
assets, owner's equity, liabilities
liabilities, assets, owner's equity
liabilities, owner's equity, assets
owner's equity, assets, liabilities
owner's equity, liabilities, assets

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-2
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

6. ____________________ represent something owed to another business entity.

ANS: Liabilities

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-1
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

7. A(n) ____________________ is a written promise to pay a supplier for assets purchased or services received.

ANS: notes payable

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-1
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

8. The report which shows a firm's assets, liabilities, and owner's equity as of a specific date is called the ____________________.

ANS: balance sheet

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-5
NAT: BUSPROG: Communication STA: AICPA FN-Reporting
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Comprehension
NOT: 1 min.

9. The ____________________ reports the investments and withdrawals by the owner, the profits and losses generated through operations, and how they have affected the capital account.

ANS: statement of owner's equity

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-5
NAT: BUSPROG: Communication STA: AICPA FN-Reporting
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Comprehension
NOT: 1 min.

10. A(n) ____________________ is a reduction in owner's equity as a result of the owner taking cash or other assets out of the business for personal use.

ANS: withdrawal

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-4
NAT: BUSPROG: Communication STA: AICPA FN-Reporting
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

11. ____________________ is the amount by which business assets exceed the business liabilities.

ANS: Owner's equity

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-1
NAT: BUSPROG: Communication STA: AICPA FN-Reporting
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

12. Amounts owed to the business by its customers are called ____________________.

ANS: accounts receivable

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-1
NAT: BUSPROG: Communication STA: AICPA FN-Reporting
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

13. A(n) ____________________ is an economic event that has a direct impact on the business.

ANS: business transaction

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-3
NAT: BUSPROG: Communication STA: AICPA BB-Industry

TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

14. A(n) ____________________ is a separate record used to summarize changes in assets, liabilities, and owner's equity of a business.

ANS: account

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-3
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

15. According to the ____________________, nonbusiness assets and liabilities are not included in the business entity's accounting records.

ANS: business entity concept

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-1
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

16. Items that are owned by a business and will provide future benefits are called ____________________.

ANS: assets

PTS: 1 DIF: Difficulty: Easy OBJ: LO: 2-1
NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.

MATCHING

Match the terms with the definitions.

a. account
b. accounts payable
c. accounts receivable
d. accounting equation
e. assets
f. balance sheet
g. business entity
h. business entity concept
i. business transaction
j. drawing
k. expenses
l. income statement
m. liability
n. net income
o. net loss
p. notes payable
q. owner's equity
r. revenues
s. statement of owner's equity

1. The amount by which the business assets exceed the business liabilities.
2. Reports assets, liabilities, and owner's equity on a specific date.
3. Withdrawals that reduce owner's equity as a result of the owner taking cash or other assets out of the business for personal use.
4. The decrease in assets (or increase in liabilities) as a result of efforts to produce revenues.
5. A formal written promise to pay a supplier or lender a specified sum of money at a definite future time.
6. The excess of total revenues over total expenses for the period.
7. Reports the profitability of business operations for a specific period of time.
8. Reports beginning capital, plus net income, less withdrawals to compute ending capital.
9. An economic event that has a direct impact on the business.
10. The concept that nonbusiness assets and liabilities are not included in the business' accounting records.
11. Consists of the three basic accounting elements: assets = liabilities + owner's equity.
12. Items a business owns that will provide future benefits.
13. An unwritten promise to pay a supplier for assets purchased or services rendered.
14. A separate record used to summarize changes in each asset, liability, and owner's equity of a business.
15. An amount owed to a business by its customers as a result of the sale of goods or services.
16. An individual, association, or organization that engages in economic activities and controls specific economic resources.

1. ANS: Q PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
2. ANS: F PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.
3. ANS: J PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
4. ANS: K PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
5. ANS: P PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
6. ANS: N PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-4 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.
7. ANS: L PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.

8. ANS: S PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-5 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-09-Financial Statements KEY: Bloom's: Knowledge
NOT: 1 min.
9. ANS: I PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-3 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
10. ANS: H PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
11. ANS: D PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-2 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
12. ANS: E PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
13. ANS: B PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
14. ANS: A PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-3 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
15. ANS: C PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.
16. ANS: G PTS: 1 DIF: Difficulty: Easy
OBJ: LO: 2-1 NAT: BUSPROG: Communication STA: AICPA BB-Industry
TOP: ACBSP: APC-02-GAAP KEY: Bloom's: Knowledge
NOT: 1 min.