**CHAPTER 1**

**INTRODUCTION TO ACCOUNTING AND BUSINESS**

# DISCUSSION QUESTIONS

1. Some users of accounting information include managers, employees, investors, creditors, customers, and the government.
2. The role of accounting is to provide information for managers to use in operating the business. In addition, accounting provides information to others to use in assessing the economic performance and condition of the business.
3. The corporate form allows the company to obtain large amounts of resources by issuing stock. For this reason, most companies that require large investments in property, plant, and equipment are organized as corporations.
4. No. The business entity assumption limits the recording of economic data to transactions directly affecting the activities of the business. The payment of the interest of $4,500 is a personal transaction of Josh Reilly and should not be recorded by Dispatch Delivery Service.
5. The land should be recorded at its cost of $167,500 to Reliable Repair Service. This is consistent with the cost principle.
6. **A.** No. The offer of $2,000,000 and the increase in the assessed value should not be recognized in the accounting records.

**B.** Cash would increase by $2,125,000, land would decrease by $900,000, and stockholders’ equity would increase by $1,225,000.

1. An account receivable is a claim against a customer for goods or services sold. An account payable is an amount owed to a creditor for goods or services purchased. Therefore, an account receivable in the records of the seller is an account payable in the records of the purchaser.
2. **(B)** The business realized net income of $91,000 ($679,000 – $588,000).
3. **(A)** The business incurred a net loss of $75,000 ($640,000 – $715,000).
4. **(A)** Net income or net loss
   1. Retained earnings at the end of the period
   2. Cash at the end of the period

**1-1**

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# BASIC EXERCISES

BE 1–1

$275,000. Under the cost principle, the land should be recorded at the cost to Ritts Roofing.

BE 1–2

1. A = L + SE

$395,000 = $97,000 + SE SE = $298,000

1. A = L + SE

–$65,000 = +$36,000 + SE SE = –$101,000

SE on December 31, 2018 = $298,000 – SE on December 31, 2018 = $197,000

$101,000

BE 1–3

1. Expense (Advertising Expense) increases by $4,850; Asset (Cash) decreases by $4,850.
2. Asset (Supplies) increases by $2,100;

Liability (Accounts Payable) increases by $2,100.

1. Asset (Accounts Receivable) increases by $14,700; Revenue (Delivery Service Fees) increases by $14,700.
2. Asset (Cash) increases by $8,200;

Asset (Accounts Receivable) decreases by $8,200.

BE 1–4

|  |  |  |
| --- | --- | --- |
| **Paradise Travel Service Income Statement**  **For the Year Ended May 31, 2018** | | |
| **Fees earned** |  | **$900,000** |
| **Expenses:** |  |  |
| **Wages expense** | **$450,000** |  |
| **Office expense** | **300,000** |  |
| **Miscellaneous expense** | **15,000** |  |
| **Total expenses** |  | **765,000** |
| **Net income** |  | **$135,000** |
|  |  |  |

BE 1–5

|  |  |  |
| --- | --- | --- |
| **Paradise Travel Service**  **Retained Earnings Statement For the Year Ended May 31, 2018** | | |
| **Retained earnings, June 1, 2017** |  | **$300,000** |
| **Net income** | **$135,000** |  |
| **Dividends** | **(10,000)** |  |
| **Change in retained earnings** |  | **125,000** |
| **Retained earnings, May 31, 2018** |  | **$425,000** |
|  |  |  |

BE 1–6

|  |  |  |
| --- | --- | --- |
| **Paradise Travel Service Balance Sheet**  **May 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$ 52,000** |
| **Accounts receivable** |  | **38,000** |
| **Supplies** |  | **3,000** |
| **Land** |  | **450,000** |
| **Total assets** |  | **$543,000** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 18,000** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$100,000** |  |
| **Retained earnings** | **425,000** |  |
| **Total stockholders’ equity** |  | **525,000** |
| **Total liabilities and stockholders’ equity** |  | **$543,000** |
|  |  |  |

BE 1–7

|  |  |  |
| --- | --- | --- |
| **Paradise Travel Service Statement of Cash Flows**  **For the Year Ended May 31, 2018** | | |
| **Cash flows from operating activities:** |  |  |
| **Cash received from customers** | **$ 880,000** |  |
| **Cash payments for operating expenses** | **(758,000)** |  |
| **Net cash flows from operating activities** |  | **$ 122,000** |
| **Cash flows used for investing activities:** |  |  |
| **Cash payments for purchase of land** |  | **(150,000)** |
| **Cash flows from financing activities:** |  |  |
| **Cash received from issuing common stock** | **$ 40,000** |  |
| **Cash dividends** | **(10,000)** |  |
| **Net cash flows from financing activities** |  | **30,000** |
| **Net increase in cash** |  | **$ 2,000** |
| **Cash as of June 1, 2017** |  | **50,000** |
| **Cash as of May 31, 2018** |  | **$ 52,000** |
|  |  |  |

# EXERCISES

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Ex. 1–1**  **A. 1.** | **manufacturing** | **6.** | **manufacturing** | **11.** | **service** |
| **2.** | **manufacturing** | **7.** | **service** | **12.** | **service** |
| **3.** | **manufacturing** | **8.** | **service** | **13.** | **manufacturing** |
| **4.** | **service** | **9.** | **manufacturing** | **14.** | **service** |
| **5.** | **merchandise** | **10.** | **merchandise** | **15.** | **merchandise** |

B. The accounting equation is relevant to all companies. It serves as the basis of the accounting information system.

Ex. 1–2

As in many ethics issues, there is no one right answer. Oftentimes, disclosing only what is legally required may not be enough. In this case, it would be best for the company’s chief executive officer to disclose both reports to the county representatives. In doing so, the chief executive officer could point out any flaws or deficiencies in the fired researcher’s report.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Ex. 1–3** |  | | | |
| **A. 1.** | **M** | **5.** | **O** | **9. X** |
| **2.** | **L** | **6.** | **O** | **10. O** |
| **3.** | **O** | **7.** | **X** |  |
| **4.** | **M** | **8.** | **L** |  |

B. A business transaction is an economic event or condition that directly changes an entity’s financial condition or results of operations.

Ex. 1–4

Keurig’s stockholders’ equity: $4,797 – $1,338 = $3,459 Starbucks’ stockholders’ equity: $10,753 – $5,481 = $5,272

Ex. 1–5

Dollar Tree’s stockholders’ equity: $2,772 – $1,601 = $1,171 Target’s stockholders’ equity: $44,553 – $28,322 = $16,231

Ex. 1–6

A. $1,895,000 ($550,000 + $1,345,000) B. $187,700 ($776,500 – $588,800)

C. $10,295,000 ($14,750,000 – $4,455,000)

Ex. 1–7

|  |  |  |
| --- | --- | --- |
| **A.** | **$3,650,000** | **($5,250,000 – $1,600,000)** |
| **B.** | **$4,120,000** | **($3,650,000 + $800,000 – $330,000)** |
| **C.** | **$2,910,000** | **($3,650,000 – $600,000 – $140,000)** |
| **D.** | **$4,180,000** | **($3,650,000 + $440,000 + $90,000)** |

E. Net income: $540,000 ($6,140,000 – $1,950,000 – $3,650,000)

Ex. 1–8

1. (2) liability
2. (1) asset
3. (3) stockholders’ equity (revenue)
4. (1) asset
5. (1) asset
6. (3) stockholders’ equity (expense)

Ex. 1–9

1. Increases assets and increases stockholders’ equity.
2. Decreases assets and decreases stockholders’ equity.
3. Increases assets and decreases assets.
4. Increases assets and increases liabilities.
5. Increases assets and increases stockholders’ equity.

Ex. 1–10

A. (1) Total assets increased $183,000 ($298,000 – $115,000).

* 1. No change in liabilities.
  2. Stockholders’ equity increased $183,000.

1. (1) Total assets decreased $80,000.
2. Total liabilities decreased $80,000.
3. No change in stockholders’ equity.
4. No, it is false that a transaction always affects at least two elements (Assets, Liabilities, or Stockholders’ Equity) of the accounting equation. Some transactions affect only one element of the accounting equation. For example, purchasing supplies for cash only affects assets.

Ex. 1–11

* 1. (B) decrease
  2. (A) increase
  3. (B) decrease
  4. (A) increase

Ex. 1–12

|  |  |  |  |
| --- | --- | --- | --- |
| **1.** | **C** | **6.** | **C** |
| **2.** | **A** | **7.** | **D** |
| **3.** | **E** | **8.** | **A** |
| **4.** | **E** | **9.** | **E** |
| **5.** | **C** | **10.** | **E** |

Ex. 1–13

* + 1. (1) Provided catering services for cash, $71,800.
  1. Purchase of land for cash, $15,000.
  2. Payment of cash for expenses, $47,500.
  3. Purchase of supplies on account, $1,100.
  4. Paid cash dividends, $5,000.
  5. Payment of cash to creditors, $4,000.
  6. Recognition of cost of supplies used, $1,500. B. $300 ($40,300 – $40,000)

|  |  |  |
| --- | --- | --- |
| **C.** | **$17,800** | **(–$5,000 + $71,800 – $49,000)** |
| **D.** | **$22,800** | **($71,800 – $49,000)** |
| **E.** | **$17,800** | **($22,800 – $5,000)** |

Ex. 1–14

No. It would be incorrect to say that the business had incurred a net loss of

$8,000. The excess of the dividends over the net income for the period is a decrease in the amount of stockholders’ equity (retained earnings) in the business.

Ex. 1–15

Amber

|  |  |
| --- | --- |
| **Stockholders’ equity at end of year ($1,730,000 – $1,150,000)…………………** | **$580,000** |
| **Deduct stockholders’ equity at beginning of year ($1,220,000 – $990,000)….** | **230,000** |
| **Net income (increase in stockholders’ equity)…………………………………** | **$350,000** |
| **Blue** |  |
| **Increase in stockholders’ equity (as determined for Amber)……………………** | **$350,000** |
| **Add dividends…………………………………………..……………………………………** | **60,000** |
| **Net income…………………………………………..……………………………………** | **$410,000** |
| **Coral** |  |
| **Increase in stockholders’ equity (as determined for Amber)……………………** | **$350,000** |
| **Deduct additional issuance of common stock……………..………………………** | **140,000** |
| **Net income……………...…………………………………………………………………** | **$210,000** |
| **Daffodil** |  |
| **Increase in stockholders’ equity (as determined for Amber)……………………** | **$350,000** |
| **Deduct additional issuance of common stock……….……………………………** | **140,000** |
|  | **$210,000** |
| **Add dividends…………...……………………………………………………………………** | **60,000** |
| **Net income…………………………………………………………………………………** | **$270,000** |

Ex. 1–16

Balance sheet items: 1, 2, 3, 5, 6, 10

Ex. 1–17

Income statement items: 4, 7, 8, 9

Ex. 1–18 A.

|  |  |  |
| --- | --- | --- |
| **Healthy Products Company Retained Earnings Statement**  **For the Month Ended November 30, 2018** | | |
| **Retained earnings, November 1, 2018** |  | **$2,940,000** |
| **Net income** | **$93,500** |  |
| **Dividends** | **(7,000)** |  |
| **Change in retained earnings** |  | **86,500** |
| **Retained earnings, November 30, 2018** |  | **$3,026,500** |
|  |  |  |

* + 1. The retained earnings statement is prepared before the November 30, 2018, balance sheet because retained earnings as of November 30, 2018, is needed for the balance sheet.

Ex. 1–19

|  |  |  |
| --- | --- | --- |
| **Imaging Services Income Statement**  **For the Month Ended March 31, 2018** | | |
| **Fees earned** |  | **$482,000** |
| **Expenses:** |  |  |
| **Wages expense** | **$300,000** |  |
| **Rent expense** | **41,500** |  |
| **Supplies expense** | **3,600** |  |
| **Miscellaneous expense** | **1,900** |  |
| **Total expenses** |  | **347,000** |
| **Net income** |  | **$135,000** |
|  |  |  |

Ex. 1–20

In each case, solve for a single unknown, using the following equation:

Stockholders’ Equity (beginning) + Additional Common Stock Issued – Dividends + Revenues – Expenses = Stockholders’ Equity (ending)

Freeman

|  |  |  |
| --- | --- | --- |
| **Stockholders’ equity at end of year ($1,260,000 – $330,000)………** |  | **$930,000** |
| **Stockholders’ equity at beginning of year ($900,000 – $360,000)…** |  | **540,000** |
| **Increase in stockholders’ equity…………………………………………** |  | **$390,000** |
| **Deduct increase due to net income ($570,000 – $240,000)…………** |  | **330,000** |
|  |  | **$ 60,000** |
| **Add dividends…………………………..………………………….……………** |  | **75,000** |
| **Additional common stock issued……………………………………** | **(A)** | **$135,000** |

Heyward

|  |  |  |
| --- | --- | --- |
| **Stockholders’ equity at end of year ($675,000 – $220,000)…………** |  | **$455,000** |
| **Stockholders’ equity at beginning of year ($490,000 – $260,000)…** |  | **230,000** |
| **Increase in stockholders’ equity…………………………………………** |  | **$225,000** |
| **Add dividends………………………………….………………….……………** |  | **32,000** |
|  |  | **$257,000** |
| **Deduct additional common stock issued………………………………** |  | **150,000** |
| **Increase due to net income………………………………………………** |  | **$107,000** |
| **Add expenses………….………………………………………….……………** |  | **128,000** |
| **Revenue………………………………………………….………………** | **(B)** | **$235,000** |

Jones

|  |  |  |
| --- | --- | --- |
| **Stockholders’ equity at end of year ($100,000 – $80,000)……………** |  | **$ 20,000** |
| **Stockholders’ equity at beginning of year ($115,000 – $81,000)……** |  | **34,000** |
| **Decrease in stockholders’ equity………………………………………** |  | **$(14,000)** |
| **Decrease in stockholders’ equity due to net loss**  **($115,000 – $122,500)……………………………………………………** |  | **7,500** |
|  |  | **$ (6,500)** |
| **Deduct common stock issued……………………………………………** |  | **(10,000)** |
| **Dividends…………………………………………………………………** | **(C)** | **$(16,500)** |

Ramirez

|  |  |
| --- | --- |
| **Stockholders’ equity at end of year ($270,000 – $136,000)…….……** | **$134,000** |
| **Add decrease due to net loss ($115,000 – $128,000)…………………** | **13,000** |
|  | **$147,000** |
| **Add dividends……………………………..……………………….……………** | **39,000** |
| **Stockholders’ equity at beginning of year………..……………………** | **$186,000** |
| **Deduct additional investment……………………………………….……** | **55,000** |
|  | **$131,000** |
| **Add liabilities at beginning of year………………………………………** | **120,000** |
| **Assets at beginning of year…………………………………………… (D)** | **$251,000** |

Ex. 1–21 A.

|  |  |  |
| --- | --- | --- |
| **Ebony Interiors**  **Balance Sheet February 28, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$ 320,000** |
| **Accounts receivable** |  | **800,000** |
| **Supplies** |  | **30,000** |
| **Total assets** |  | **$1,150,000** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 310,000** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$200,000** |  |
| **Retained earnings** | **640,000\*** |  |
| **Total stockholders’ equity** |  | **840,000** |
| **Total liabilities and stockholders’ equity** |  | **$1,150,000** |
|  |  |  |

**\*$640,000 = $320,000 + $800,000 + $30,000 – $310,000 – $200,000**

|  |  |  |
| --- | --- | --- |
| **Ebony Interiors Balance Sheet**  **March 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$ 380,000** |
| **Accounts receivable** |  | **960,000** |
| **Supplies** |  | **35,000** |
| **Total assets** |  | **$1,375,000** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 400,000** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$200,000** |  |
| **Retained earnings** | **775,000**\* |  |
| **Total stockholders’ equity** |  | **975,000** |
| **Total liabilities and stockholders’ equity** |  | **$1,375,000** |
|  |  |  |

|  |  |
| --- | --- |
| **\*$775,000 = $380,000 + $960,000 + $35,000 – $400,000 – $200,000** |  |
| **B. Stockholders’ equity, March 31………………………………………………** | **$975,000** |
| **Stockholders’ equity, February 28…………………….……………………** | **840,000** |
| **Net income……………………………………………………………………….** | **$135,000** |

|  |  |
| --- | --- |
| **Ex. 1–21 (Concluded)**  **C. Stockholders’ equity, March 31…………………………………………………** | **$975,000** |
| **Stockholders’ equity, February 28…………………….………………………** | **840,000** |
| **Increase in stockholders’ equity……………………………………………** | **$135,000** |
| **Add dividends………..…………………………………………………………………** | **50,000** |
| **Net income………………………………………….………………………………** | **$185,000** |

Ex. 1–22

A. Balance sheet: 1, 2, 3, 4, 6, 7, 8, 9, 10, 11, 13

Income statement: 5, 12, 14, 15

1. Yes, an item can appear on more than one financial statement. For example, cash appears on both the balance sheet and statement of cash flows. However, the same item cannot appear on both the income statement and balance sheet.
2. Yes, the accounting equation is relevant to all companies, including Exxon Mobil Corporation. The accounting equation is the basis for all accounting systems.

Ex. 1–23

* 1. (A) operating activity
  2. (A) operating activity
  3. (B) investing activity
  4. (C) financing activity

Ex. 1–24

|  |  |  |
| --- | --- | --- |
| **Ethos Consulting Group Statement of Cash Flows**  **For the Year Ended May 31, 2018** | | |
| **Cash flows from operating activities:** |  |  |
| **Cash received from customers** | **$ 637,500** |  |
| **Cash payments for operating expenses** | **(475,000)** |  |
| **Net cash flows from operating activities** |  | **$162,500** |
| **Cash flows used for investing activities:** |  |  |
| **Cash payments for purchase of land** |  | **(90,000)** |
| **Cash flows from financing activities:** |  |  |
| **Cash received from issuing common stock** | **$ 62,500** |  |
| **Cash dividends** | **(17,500)** |  |
| **Net cash flows from financing activities** |  | **45,000** |
| **Net decrease in cash** |  | **$117,500** |
| **Cash as of June 1, 2017** |  | **58,000** |
| **Cash as of May 31, 2018** |  | **$175,500** |
|  |  |  |

Ex. 1–25

* + 1. All financial statements should contain the name of the business in their heading. The retained earnings statement is incorrectly headed as “Omar Farah” rather than We-Sell Realty. The heading of the balance sheet needs the name of the business.
    2. The income statement and retained earnings statement cover a period of time and should be labeled “For the Month Ended August 31, 2018.”
    3. The year in the heading for the retained earnings statement should be 2018 rather than 2017.
    4. The balance sheet should be labeled “August 31, 2018,” rather than “For the Month Ended August 31, 2018.”
    5. In the income statement, the miscellaneous expense amount should be listed as the last expense.
    6. In the income statement, the total expenses are incorrectly subtracted from the sales commissions, resulting in an incorrect net income amount. The correct net income should be $24,150. This also affects the retained earnings statement and the amount of retained earnings that appears on the balance sheet.
    7. The additional issuance of common stock of $15,000 should not be included in the retained earnings statement.
    8. In the retained earnings statement, the net income should be presented first. Dividends should then be subtracted from net income to yield a net increase in retained earnings.
    9. Accounts payable should be listed as a liability on the balance sheet.
    10. Accounts receivable and supplies should be listed as assets on the balance sheet.
    11. The balance sheet assets should equal the sum of the liabilities and stockholders’ equity.

Ex. 1–25 (Concluded)

Corrected financial statements appear as follows:

|  |  |  |
| --- | --- | --- |
| **We-Sell Realty Income Statement**  **For the Month Ended August 31, 2018** | | |
| **Sales commissions** |  | **$140,000** |
| **Expenses:** |  |  |
| **Office salaries expense** | **$87,000** |  |
| **Rent expense** | **18,000** |  |
| **Automobile expense** | **7,500** |  |
| **Supplies expense** | **1,150** |  |
| **Miscellaneous expense** | **2,200** |  |
| **Total expenses** |  | **115,850** |
| **Net income** |  | **$ 24,150** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **We-Sell Realty Retained Earnings Statement**  **For the Month Ended August 31, 2018** | | |
| **Retained earnings, August 1, 2018** |  | **$ 0** |
| **Net income** | **$ 24,150** |  |
| **Dividends** | **(10,000)** |  |
| **Change in retained earnings** |  | **14,150** |
| **Retained earnings, August 31, 2018** |  | **$14,150** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **We-Sell Realty**  **Balance Sheet August 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$ 8,900** |
| **Accounts receivable** |  | **38,600** |
| **Supplies** |  | **4,000** |
| **Total assets** |  | **$51,500** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$22,350** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$15,000** |  |
| **Retained earnings** | **14,150** |  |
| **Total stockholders’ equity** |  | **29,150** |
| **Total liabilities and stockholders’ equity** |  | **$51,500** |
|  |  |  |

CHAPTER 1 Introduction to Accounting and Business

**Prob. 1–1A**

**1. Assets = Liabilities +**

PROBLEMS

**Stockholders’ Equity**

**Cash**

**Accts.**

**+ Rec.**

**+ Supplies =**

**Accts. Payable +**

**Common Stock**

**– Dividends +**

**Fees Earned**

**Rent**

**– Expense –**

**Salaries Expense –**

**Supplies Expense –**

**Auto Exp.**

**Misc.**

**– Exp.**

**(A) + 36,000 + 36,000**

**(B) + 1,800 + 1,800**

**Bal. 36,000 1,800 1,800 36,000**

**(C) + 6,750 + 6,750**

**Bal. 42,750 1,800 1,800 36,000 6,750**

**(D) – 5,000 – 5,000**

**Bal. 37,750 1,800 1,800 36,000 6,750 – 5,000**

**(E) – 1,375 – 1,375**

**Bal. 36,375 1,800 425 36,000 6,750 – 5,000**

**(F) + 9,500 + 9,500**

**Bal. 36,375 9,500 1,800 425 36,000 16,250 – 5,000**

**(G) – 1,800 – 840 – 960**

**Bal. 34,575 9,500 1,800 425 36,000 16,250 – 5,000 – 840 – 960**

**(H) – 3,600 – 3,600**

**Bal. 30,975 9,500 1,800 425 36,000 16,250 – 5,000 – 3,600 – 840 – 960**

1. **– 1,450 – 1,450**

**Bal. 30,975 9,500 350 425 36,000 16,250 – 5,000 – 3,600 – 1,450 – 840 – 960**

**(J) – 3,000 – 3,000**

**Bal. 27,975 9,500 350 425 36,000 – 3,000 16,250 – 5,000 – 3,600 – 1,450 – 840 – 960**

**2. Stockholders’ equity is the right of stockholders (owners) to the assets of the business. These rights are increased by issuing common stock and revenues and decreased by dividends and expenses.**

**3. $4,400 ($16,250 – $5,000 – $3,600 – $1,450 – $840 – $960)**

**4. September’s transactions increased retained earnings by $1,400 ($4,400 – $3,000), which is September's net income of $4,400 less dividends of $3,000.**

**1-15**

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Prob. 1–2A 1.

|  |  |  |
| --- | --- | --- |
| **Journey Travel Agency Income Statement**  **For the Year Ended December 31, 2018** | | |
| **Fees earned** |  | **$383,500** |
| **Expenses:** |  |  |
| **Wages expense** | **$170,000** |  |
| **Rent expense** | **22,500** |  |
| **Utilities expense** | **16,700** |  |
| **Supplies expense** | **11,300** |  |
| **Miscellaneous expense** | **14,500** |  |
| **Total expenses** |  | **235,000** |
| **Net income** |  | **$148,500** |
|  |  |  |

2.

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| --- | --- | --- |
| **Journey Travel Agency Retained Earnings Statement**  **For the Year Ended December 31, 2018** | | |
| **Retained earnings, January 1, 2018** |  | **$1,341,000** |
| **Net income** | **$148,500** |  |
| **Dividends** | **(75,000)** |  |
| **Change in retained earnings** |  | **73,500** |
| **Retained earnings, December 31, 2018** |  | **$1,414,500** |
|  |  |  |

3.

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| --- | --- | --- |
| **Journey Travel Agency Balance Sheet**  **December 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$ 190,500** |
| **Accounts receivable** |  | **236,500** |
| **Supplies** |  | **7,000** |
| **Land** |  | **1,500,000** |
| **Total assets** |  | **$1,934,000** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 69,500** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$ 450,000** |  |
| **Retained earnings** | **1,414,500** |  |
| **Total stockholders’ equity** |  | **1,864,500** |
| **Total liabilities and stockholders’ equity** |  | **$1,934,000** |
|  |  |  |

4. Ending retained earnings appears on both the retained earnings statement and the balance sheet. For Journey Travel Agency, the December 31, 2018, retained earnings of $1,414,500 appears on the retained earnings statement and balance sheet.

Prob. 1–3A 1.

|  |  |  |
| --- | --- | --- |
| **Reliance Financial Services Income Statement**  **For the Month Ended July 31, 2018** | | |
| **Fees earned** |  | **$144,500** |
| **Expenses:** |  |  |
| **Salaries expense** | **$55,000** |  |
| **Rent expense** | **33,000** |  |
| **Auto expense** | **16,000** |  |
| **Supplies expense** | **4,500** |  |
| **Miscellaneous expense** | **4,800** |  |
| **Total expenses** |  | **113,300** |
| **Net income** |  | **$ 31,200** |
|  |  |  |

2.

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| --- | --- | --- |
| **Reliance Financial Services Retained Earnings Statement**  **For the Month Ended July 31, 2018** | | |
| **Retained earnings, July 1, 2018** |  | **$ 0** |
| **Net income** | **$ 31,200** |  |
| **Dividends** | **(15,000)** |  |
| **Change in retained earnings** |  | **16,200** |
| **Retained earnings, July 31, 2018** |  | **$16,200** |
|  |  |  |

3.

|  |  |  |
| --- | --- | --- |
| **Reliance Financial Services Balance Sheet**  **July 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$32,600** |
| **Accounts receivable** |  | **34,500** |
| **Supplies** |  | **2,500** |
| **Total assets** |  | **$69,600** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 3,400** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$50,000** |  |
| **Retained earnings** | **16,200** |  |
| **Total stockholders’ equity** |  | **66,200** |
| **Total liabilities and stockholders’ equity** |  | **$69,600** |
|  |  |  |

**1-17**

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Prob. 1–3A (Concluded)

4. (Optional)

|  |  |  |
| --- | --- | --- |
| **Reliance Financial Services Statement of Cash Flows**  **For the Month Ended July 31, 2018** | | |
| **Cash flows from operating activities:** |  |  |
| **Cash received from customers** | **$ 110,000** |  |
| **Cash payments for expenses** |  |  |
| **and payments to creditors\*** | **(112,400)** |  |
| **Net cash flows used for operating activities** |  | **$ (2,400)** |
| **Cash flows from investing activities** |  | **0** |
| **Cash flows from financing activities:** |  |  |
| **Cash received from issuing common stock** | **$ 50,000** |  |
| **Cash dividends** | **(15,000)** |  |
| **Net cash flows from financing activities** |  | **35,000** |
| **Net increase in cash and July 31, 2018, cash balance** |  | **$32,600** |
|  |  |  |

**\* $3,600 + $33,000 + $20,800 + $55,000; these amounts are taken from the cash column shown in the problem.**

CHAPTER 1 Introduction to Accounting and Business

**Prob. 1–4A 1.**

**Assets**

**= Liabilities +**

**Stockholders’ Equity**

**Cash**

**+ Supplies =**

**Accts. Payable +**

**Common Stock**

* **Dividends +**

**Sales Comm.**

**Salaries**

* + **Exp. –**

**Rent Exp.**

**Auto**

* + **Exp.**

**Supplies**

* + **Exp. –**

**Misc. Exp.**

**(A) + 35,000 + 35,000**

**(B) + 2,750 + 2,750**

**Bal. 35,000 2,750 2,750 35,000**

**(C) – 1,800 – 1,800**

**Bal. 33,200 2,750 950 35,000**

**(D) + 52,800 + 52,800**

**Bal. 86,000 2,750 950 35,000 52,800**

**(E) – 4,500 – 4,500**

**Bal. 81,500 2,750 950 35,000 52,800 – 4,500**

**(F) – 3,000 – 3,000**

**Bal. 78,500 2,750 950 35,000 – 3,000 52,800 – 4,500**

**(G) – 2,300 – 1,100 – 1,200**

**Bal. 76,200 2,750 950 35,000 – 3,000 52,800 – 4,500 – 1,100 – 1,200**

**(H) – 5,250 – 5,250**

**Bal. 70,950 2,750 950 35,000 – 3,000 52,800 – 5,250 – 4,500 – 1,100 – 1,200**

1. **– 1,000 – 1,000**

**Bal. 70,950 1,750 950 35,000 – 3,000 52,800 – 5,250 – 4,500 – 1,100 – 1,000 – 1,200**

**1-19**

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Prob. 1–4A (Concluded) 2.

|  |  |  |
| --- | --- | --- |
| **Western Realty Income Statement**  **For the Month Ended August 31, 2018** | | |
| **Sales commissions** |  | **$52,800** |
| **Expenses:** |  |  |
| **Salaries expense** | **$5,250** |  |
| **Rent expense** | **4,500** |  |
| **Automobile expense** | **1,100** |  |
| **Supplies expense** | **1,000** |  |
| **Miscellaneous expense** | **1,200** |  |
| **Total expenses** |  | **13,050** |
| **Net income** |  | **$39,750** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **Western Realty Retained Earnings Statement**  **For the Month Ended August 31, 2018** | | |
| **Retained earnings, August 1, 2018** |  | **$ 0** |
| **Net income** | **$39,750** |  |
| **Dividends** | **(3,000)** |  |
| **Change in retained earnings** |  | **36,750** |
| **Retained earnings, August 31, 2018** |  | **$36,750** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **Western Realty**  **Balance Sheet August 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$70,950** |
| **Supplies** |  | **1,750** |
| **Total assets** |  | **$72,700** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 950** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$35,000** |  |
| **Retained earnings** | **36,750** |  |
| **Total stockholders’ equity** |  | **71,750** |
| **Total liabilities and stockholders’ equity** |  | **$72,700** |
|  |  |  |

Prob. 1–5A 1.

**Assets**

**= Liabilities**

**+ Stockholders’ Equity**

**Cash +**

**Accounts Receivable**

**+ Supplies +**

**Land**

**Accounts**

**= Payable**

**Common**

**+ Stock +**

**Retained Earnings**

**$45,000 +**

**$93,000**

**+ $7,000**

**+ $75,000**

**= $40,000**

**+ 60,000 +**

**Retained Earnings**

**$220,000**

**= $100,000**

**+ Retained Earnings**

**$120,000**

**= Retained Earnings**

**Prob. 1–5A (Continued)**

**2. Assets = Liabilities + Stockholders’ Equity**

**Cash**

**Accts.**

**+ Rec.**

**+ Supplies +**

**Land**

**Accts.**

**= Payable**

**Common**

**+ Stock**

**Retained**

**+ Earnings –**

**Dividends**

**Bal. 45,000 93,000 7,000 75,000 40,000 60,000 120,000**

**(A) + 35,000 + 35,000**

**Bal. 80,000 93,000 7,000 75,000 40,000 95,000 120,000**

**(B) – 50,000 + 50,000**

**Bal. 30,000 93,000 7,000 125,000 40,000 95,000 120,000**

**(C) + 32,125**

**Bal. 62,125 93,000 7,000 125,000 40,000 95,000 120,000**

**(D) – 6,000**

**Bal. 56,125 93,000 7,000 125,000 40,000 95,000 120,000**

**(E) + 2,500 + 2,500**

**Bal. 56,125 93,000 9,500 125,000 42,500 95,000 120,000**

**(F) – 22,800 – 22,800**

**Bal. 33,325 93,000 9,500 125,000 19,700 95,000 120,000**

**(G) + 84,750**

**Bal. 33,325 177,750 9,500 125,000 19,700 95,000 120,000**

**(H) + 29,500**

**Bal. 33,325 177,750 9,500 125,000 49,200 95,000 120,000**

**(I) – 14,000**

**Bal. 19,325 177,750 9,500 125,000 49,200 95,000 120,000**

**(J) + 88,000 – 88,000**

**Bal. 107,325 89,750 9,500 125,000 49,200 95,000 120,000**

**(K) – 3,600**

**Bal. 107,325 89,750 5,900 125,000 49,200 95,000 120,000**

**(L) – 12,000 – 12,000**

**Bal. 95,325 89,750 5,900 125,000 49,200 95,000 120,000 – 12,000**

Prob. 1–5A (Continued)

**Stockholders’ Equity (Continued)**

**Dry Cleaning**

**+ Revenue**

**Dry Cleaning**

**– Exp. –**

**Wages Exp. –**

**Rent Exp.**

**Supplies**

* **Exp. –**

**Truck Exp.**

**Utilities**

* **Exp. –**

**Misc. Exp.**

**Bal.**

**(A)**

**Bal.**

**(B)**

**Bal.**

**(C) + 32,125**

**Bal. 32,125**

**(D) – 6,000**

**Bal. 32,125 – 6,000**

**(E)**

**Bal. 32,125 – 6,000**

**(F)**

**Bal. 32,125 – 6,000**

**(G) + 84,750**

**Bal. 116,875 – 6,000**

**(H) – 29,500**

**Bal. 116,875 – 29,500 – 6,000**

**(I) – 7,500 – 2,500 – 1,300 – 2,700**

**Bal. 116,875 – 29,500 – 7,500 – 6,000 – 2,500 – 1,300 – 2,700**

**(J)**

**Bal. 116,875 – 29,500 – 7,500 – 6,000 – 2,500 – 1,300 – 2,700**

**(K) – 3,600**

**Bal. 116,875 – 29,500 – 7,500 – 6,000 – 3,600 – 2,500 – 1,300 – 2,700**

**(L)**

**Bal. 116,875 – 29,500 – 7,500 – 6,000 – 3,600 – 2,500 – 1,300 – 2,700**

Prob. 1–5A (Continued) 3.

|  |  |  |
| --- | --- | --- |
| **D’Lite Dry Cleaners Income Statement**  **For the Month Ended July 31, 2018** | | |
| **Dry cleaning revenue** |  | **$116,875** |
| **Expenses:** |  |  |
| **Dry cleaning expense** | **$29,500** |  |
| **Wages expense** | **7,500** |  |
| **Rent expense** | **6,000** |  |
| **Supplies expense** | **3,600** |  |
| **Truck expense** | **2,500** |  |
| **Utilities expense** | **1,300** |  |
| **Miscellaneous expense** | **2,700** |  |
| **Total expenses** |  | **53,100** |
| **Net income** |  | **$ 63,775** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **D’Lite Dry Cleaners Retained Earnings Statement**  **For the Month Ended July 31, 2018** | | |
| **Retained earnings, July 1, 2018** |  | **$120,000** |
| **Net income** | **$ 63,775** |  |
| **Dividends** | **(12,000)** |  |
| **Change in retained earnings** |  | **51,775** |
| **Retained earnings, July 31, 2018** |  | **$171,775** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **D’Lite Dry Cleaners Balance Sheet**  **July 31, 2018** | | |
| **Assets** | | |
| **Cash** |  | **$ 95,325** |
| **Accounts receivable** |  | **89,750** |
| **Supplies** |  | **5,900** |
| **Land** |  | **125,000** |
| **Total assets** |  | **$315,975** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 49,200** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$ 95,000** |  |
| **Retained earnings** | **171,775** |  |
| **Total stockholders’ equity** |  | **266,775** |
| **Total liabilities and stockholders’ equity** |  | **$315,975** |
|  |  |  |

Prob. 1–5A (Concluded)

4. (Optional)

|  |  |  |
| --- | --- | --- |
| **D’Lite Dry Cleaners Statement of Cash Flows**  **For the Month Ended July 31, 2018** | | |
| **Cash flows from operating activities:** |  |  |
| **Cash received from customers\*** | **$120,125** |  |
| **Cash payments for expenses** |  |  |
| **and payments to creditors\*\*** | **(42,800)** |  |
| **Net cash flows from operating activities** |  | **$ 77,325** |
| **Cash flows used for investing activities:** |  |  |
| **Purchase of land** |  | **(50,000)** |
| **Cash flows from financing activities:** |  |  |
| **Cash received from issuing common stock** | **$ 35,000** |  |
| **Cash dividends** | **(12,000)** |  |
| **Net cash flows from financing activities** |  | **23,000** |
| **Net Increase in cash** |  | **$ 50,325** |
| **Cash balance, July 1, 2018** |  | **45,000** |
| **Cash balance, July 31, 2018** |  | **$ 95,325** |
|  |  |  |

**\* $32,125 + $88,000; these amounts are taken from the cash column of the spreadsheet in Part 2.**

**\*\* $6,000 + $22,800 + $14,000; these amounts are taken from the cash column of the spreadsheet in Part 2.**

Prob. 1–6A

A. Fees earned, $750,000 ($275,000 + $475,000)

B. Supplies expense, $30,000 ($475,000 – $300,000 – $100,000 – $20,000 – $25,000)

1. Retained earnings, April 1, 2018, $0; Wolverine Realty was organized on April 1, 2018.
2. Net income for April, $275,000 from income statement E. $150,000 ($275,000 – $125,000)

F. Retained earnings, April 30, 2018, $150,000

G. Total assets, $625,000 ($462,500 + $12,500 + $150,000)

H. Retained earnings, $150,000; same as (F)

I. Total stockholders’ equity, $525,000 ($375,000 + $150,000)

1. Total liabilities and stockholders’ equity, $625,000 ($100,000 + $525,000)
2. Cash received from customers, $750,000 ($387,500 + $362,500); this is the same as fees earned (A) since there are no accounts receivable.
3. Net cash flows from operating activities, $362,500 ($750,000 – $387,500)
4. Cash payments for acquisition of land, ($150,000)
5. Cash received from issuing common stock, $375,000
6. Cash dividends, ($125,000)
7. Net cash flows from financing activities, $250,000 ($375,000 – $125,000)

Q. Net cash flow and April 30, 2018, cash balance, $462,500 ($362,500 – $150,000

+ $250,000); also the cash balance on the balance sheet.

CHAPTER 1 Introduction to Accounting and Business

**Prob. 1–1B**

* 1. **Assets = Liabilities +**

**Stockholders’ Equity**

**Cash**

**Accts.**

**+ Rec.**

**+ Supplies =**

**Accts. Payable +**

**Common Stock**

* **Dividends +**

**Fees Earned**

**Rent**

* + **Expense –**

**Salaries Expense**

**Supplies**

* **Expense –**

**Auto Exp.**

**Misc.**

* + **Exp.**

**(A) + 50,000 + 50,000**

**(B) + 4,000 + 4,000**

**Bal. 50,000 4,000 4,000 50,000**

**(C) – 2,300 – 2,300**

**Bal. 47,700 4,000 1,700 50,000**

**(D) + 13,800 + 13,800**

**Bal. 61,500 4,000 1,700 50,000 13,800**

**(E) – 5,000 – 5,000**

**Bal. 56,500 4,000 1,700 50,000 13,800 – 5,000**

**(F) – 1,450 – 1,150 – 300**

**Bal. 55,050 4,000 1,700 50,000 13,800 – 5,000 – 1,150 – 300**

**(G) – 2,500 – 2,500**

**Bal. 52,550 4,000 1,700 50,000 13,800 – 5,000 – 2,500 – 1,150 – 300**

**(H) – 1,300 – 1,300**

**Bal. 52,550 2,700 1,700 50,000 13,800 – 5,000 – 2,500 – 1,300 – 1,150 – 300**

1. **+ 12,500 + 12,500**

**Bal. 52,550 12,500 2,700 1,700 50,000 26,300 – 5,000 – 2,500 – 1,300 – 1,150 – 300**

**(J) – 3,900 – 3,900**

**Bal. 48,650 12,500 2,700 1,700 50,000 – 3,900 26,300 – 5,000 – 2,500 – 1,300 – 1,150 – 300**

**2. Stockholders’ equity is the right of stockholders (owners) to the assets of the business. These rights are increased by issuing common stock and revenues and decreased by dividends and expenses.**

**3. $16,050 ($26,300 – $5,000 – $2,500 – $1,300 – $1,150 – $300)**

**4. March’s transactions increased retained earnings by $12,150 ($16,050 – $3,900), which is the excess of March’s net income of $16,050 over dividends of $3,900.**

**1-27**

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Prob. 1–2B 1.

|  |  |  |
| --- | --- | --- |
| **Wilderness Travel Service Income Statement**  **For the Year Ended April 30, 2018** | | |
| **Fees earned** |  | **$875,000** |
| **Expenses:** |  |  |
| **Wages expense** | **$525,000** |  |
| **Rent expense** | **75,000** |  |
| **Utilities expense** | **38,000** |  |
| **Supplies expense** | **12,000** |  |
| **Taxes expense** | **10,000** |  |
| **Miscellaneous expense** | **15,000** |  |
| **Total expenses** |  | **675,000** |
| **Net income** |  | **$200,000** |
|  |  |  |

2.

|  |  |  |
| --- | --- | --- |
| **Wilderness Travel Service Retained Earnings Statement**  **For the Year Ended April 30, 2018** | | |
| **Retained earnings, May 1, 2017** |  | **$145,000** |
| **Net income** | **$200,000** |  |
| **Dividends** | **(40,000)** |  |
| **Change in retained earnings** |  | **160,000** |
| **Retained earnings, April 30, 2018** |  | **$305,000** |
|  |  |  |

3.

|  |  |  |
| --- | --- | --- |
| **Wilderness Travel Service Balance Sheet**  **April 30, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$146,000** |
| **Accounts receivable** |  | **210,000** |
| **Supplies** |  | **9,000** |
| **Total assets** |  | **$365,000** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 25,000** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$ 35,000** |  |
| **Retained earnings** | **305,000** |  |
| **Total stockholders’ equity** |  | **340,000** |
| **Total liabilities and stockholders’ equity** |  | **$365,000** |
|  |  |  |

4. Net income (or net loss) appears on both the income statement and the retained earnings statement. For Wilderness Travel Service, net income for the year of

$200,000 appears on the income statement and retained earnings statement.

Prob. 1–3B 1.

|  |  |  |
| --- | --- | --- |
| **Bronco Consulting Income Statement**  **For the Month Ended August 31, 2018** | | |
| **Fees earned** |  | **$125,000** |
| **Expenses:** |  |  |
| **Salaries expense** | **$58,000** |  |
| **Rent expense** | **27,000** |  |
| **Auto expense** | **15,500** |  |
| **Supplies expense** | **6,100** |  |
| **Miscellaneous expense** | **7,500** |  |
| **Total expenses** |  | **114,100** |
| **Net income** |  | **$ 10,900** |
|  |  |  |

2.

|  |  |  |
| --- | --- | --- |
| **Bronco Consulting Retained Earnings Statement**  **For the Month Ended August 31, 2018** | | |
| **Retained earnings, August 1, 2018** |  | **$ 0** |
| **Net income** | **$10,900** |  |
| **Dividends** | **(5,000)** |  |
| **Change in retained earnings** |  | **5,900** |
| **Retained earnings, August 31, 2018** |  | **$5,900** |
|  |  |  |

3.

|  |  |  |
| --- | --- | --- |
| **Bronco Consulting Balance Sheet**  **August 31, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$48,000** |
| **Accounts receivable** |  | **33,000** |
| **Supplies** |  | **2,900** |
| **Total assets** |  | **$83,900** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 3,000** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$75,000** |  |
| **Retained earnings** | **5,900** |  |
| **Total stockholders’ equity** |  | **80,900** |
| **Total liabilities and stockholders’ equity** |  | **$83,900** |
|  |  |  |

**1-29**

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Prob. 1–3B (Concluded)

4. (Optional)

|  |  |  |
| --- | --- | --- |
| **Bronco Consulting Statement of Cash Flows**  **For the Month Ended August 31, 2018** | | |
| **Cash flows from operating activities:** |  |  |
| **Cash received from customers** | **$ 92,000** |  |
| **Cash payments for expenses** |  |  |
| **and payments to creditors\*** | **(114,000)** |  |
| **Net cash flows used for operating activities** |  | **$(22,000)** |
| **Cash flows from investing activities** |  | **0** |
| **Cash flows from financing activities:** |  |  |
| **Cash received from issuing common stock** | **$ 75,000** |  |
| **Cash dividends** | **(5,000)** |  |
| **Net cash flows from financing activities** |  | **70,000** |
| **Net increase in cash and August 31, 2018, cash balance** |  | **$ 48,000** |
|  |  |  |

**\* $27,000 + $6,000 + $23,000 + $58,000; these amounts are taken from the cash column shown in the problem.**

CHAPTER 1 Introduction to Accounting and Business

**Prob. 1–4B 1.**

**Assets**

**= Liabilities +**

**Stockholders’ Equity**

**Cash**

**+ Supplies =**

**Accts. Payable +**

**Common Stock**

**– Dividends +**

**Sales Comm. –**

**Rent Exp.**

**Salaries**

* **Exp. –**

**Auto Exp.**

**Supplies**

* **Exp. –**

**Misc. Exp.**

**(A) + 24,000 + 24,000**

**(B) – 3,600 – 3,600**

**Bal. 20,400 24,000 – 3,600**

**(C) – 1,950 – 1,350 – 600**

**Bal. 18,450 24,000 – 3,600 – 1,350 – 600**

**(D) + 1,200 + 1,200**

**Bal. 18,450 1,200 1,200 24,000 – 3,600 – 1,350 – 600**

**(E) + 19,800 + 19,800**

**Bal. 38,250 1,200 1,200 24,000 19,800 – 3,600 – 1,350 – 600**

**(F) – 750 – 750**

**Bal. 37,500 1,200 450 24,000 19,800 – 3,600 – 1,350 – 600**

**(G) – 2,500 – 2,500**

**Bal. 35,000 1,200 450 24,000 19,800 – 3,600 – 2,500 – 1,350 – 600**

**(H) – 3,500 – 3,500**

**Bal. 31,500 1,200 450 24,000 – 3,500 19,800 – 3,600 – 2,500 – 1,350 – 600**

**(I) – 900 – 900**

**Bal. 31,500 300 450 24,000 – 3,500 19,800 – 3,600 – 2,500 – 1,350 – 900 – 600**

**1-31**

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Prob. 1–4B (Concluded) 2.

|  |  |  |
| --- | --- | --- |
| **Custom Realty Income Statement**  **For the Month Ended April 30, 2018** | | |
| **Sales commissions** |  | **$19,800** |
| **Expenses:** |  |  |
| **Rent expense** | **$3,600** |  |
| **Salaries expense** | **2,500** |  |
| **Automobile expense** | **1,350** |  |
| **Supplies expense** | **900** |  |
| **Miscellaneous expense** | **600** |  |
| **Total expenses** |  | **8,950** |
| **Net income** |  | **$10,850** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **Custom Realty Retained Earnings Statement**  **For the Month Ended April 30, 2018** | | |
| **Retained earnings, April 1, 2018** |  | **$ 0** |
| **Net income** | **$10,850** |  |
| **Dividends** | **(3,500)** |  |
| **Change in retained earnings** |  | **7,350** |
| **Retained earnings, April 30, 2018** |  | **$7,350** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **Custom Realty Balance Sheet**  **April 30, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$31,500** |
| **Supplies** |  | **300** |
| **Total assets** |  | **$31,800** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 450** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$24,000** |  |
| **Retained earnings** | **7,350** |  |
| **Total stockholders’ equity** |  | **31,350** |
| **Total liabilities and stockholders’ equity** |  | **$31,800** |
|  |  |  |

Prob. 1–5B 1.

**Assets**

**= Liabilities +**

**Stockholders’ Equity**

**Cash**

**Accounts**

**+ Receivable**

**+ Supplies +**

**Land**

**Accounts**

**= Payable +**

**Common Stock +**

**Retained Earnings**

**50,000 +**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **$39,000 +** | **$80,000** | **+ $11,000** | **+ $50,000** | **=** | **$31,500** | **+** |
|  |  |  | **$180,000** | **=** | **$81,500** | **+** |

**Retained Earnings**

**$98,500**

**Retained Earnings**

**= Retained Earnings**

**Prob. 1–5B (Continued)**

**2. Assets**

**= Liabilities +**

**Stockholders’ Equity**

**Cash**

**Accts.**

**+ Rec.**

**+ Supplies +**

**Land**

**Accts.**

**= Payable**

**Common**

**+ Stock**

**Retained**

**+ Earnings –**

**Dividends**

**Bal. 39,000 80,000 11,000 50,000 31,500 50,000 98,500**

**(A) + 21,000 + 21,000**

**Bal. 60,000 80,000 11,000 50,000 31,500 71,000 98,500**

**(B) – 35,000 + 35,000**

**Bal. 25,000 80,000 11,000 85,000 31,500 71,000 98,500**

**(C) – 4,000**

**Bal. 21,000 80,000 11,000 85,000 31,500 71,000 98,500**

**(D) + 72,000**

**Bal. 21,000 152,000 11,000 85,000 31,500 71,000 98,500**

**(E) – 20,000 – 20,000**

**Bal. 1,000 152,000 11,000 85,000 11,500 71,000 98,500**

**(F) + 8,000 + 8,000**

**Bal. 1,000 152,000 19,000 85,000 19,500 71,000 98,500**

**(G) + 38,000**

**Bal. 39,000 152,000 19,000 85,000 19,500 71,000 98,500**

**(H) + 77,000 – 77,000**

**Bal. 116,000 75,000 19,000 85,000 19,500 71,000 98,500**

**(I) + 29,450**

**Bal. 116,000 75,000 19,000 85,000 48,950 71,000 98,500**

**(J) – 29,200**

**Bal. 86,800 75,000 19,000 85,000 48,950 71,000 98,500**

**(K) – 7,200**

**Bal. 86,800 75,000 11,800 85,000 48,950 71,000 98,500**

**(L) – 5,000 – 5,000**

**Bal. 81,800 75,000 11,800 85,000 48,950 71,000 98,500 – 5,000**

Prob. 1–5B (Continued)

**Stockholders’ Equity (Continued)**

**Dry Cleaning**

**+ Revenue**

**Dry Cleaning**

**– Exp. –**

**Wages Exp. –**

**Supplies Exp. –**

**Rent Exp.**

**Truck**

* **Exp.**

**Utilities**

* **Exp. –**

**Misc. Exp.**

**Bal.**

**(A)**

**Bal.**

**(B)**

**Bal.**

**(C) – 4,000**

**Bal. – 4,000**

**(D) + 72,000**

**Bal. 72,000 – 4,000**

**(E)**

**Bal. 72,000 – 4,000**

**(F)**

**Bal. 72,000 – 4,000**

**(G) + 38,000**

**Bal. 110,000 – 4,000**

**(H)**

**Bal. 110,000 – 4,000**

**(I) – 29,450**

**Bal. 110,000 – 29,450 – 4,000**

**(J) – 24,000 – 2,100 – 1,800 – 1,300**

**Bal. 110,000 – 29,450 – 24,000 – 4,000 – 2,100 – 1,800 – 1,300**

**(K) – 7,200**

**Bal. 110,000 – 29,450 – 24,000 – 7,200 – 4,000 – 2,100 – 1,800 – 1,300**

**(L)**

**Bal. 110,000 – 29,450 – 24,000 – 7,200 – 4,000 – 2,100 – 1,800 – 1,300**

Prob. 1–5B (Continued) 3.

|  |  |  |
| --- | --- | --- |
| **Bev’s Dry Cleaners Income Statement**  **For the Month Ended November 30, 2018** | | |
| **Dry cleaning revenue** |  | **$110,000** |
| **Expenses:** |  |  |
| **Dry cleaning expense** | **$29,450** |  |
| **Wages expense** | **24,000** |  |
| **Supplies expense** | **7,200** |  |
| **Rent expense** | **4,000** |  |
| **Truck expense** | **2,100** |  |
| **Utilities expense** | **1,800** |  |
| **Miscellaneous expense** | **1,300** |  |
| **Total expenses** |  | **69,850** |
| **Net income** |  | **$ 40,150** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **Bev’s Dry Cleaners Retained Earnings Statement**  **For the Month Ended November 30, 2018** | | |
| **Retained earnings, November 1, 2018** |  | **$ 98,500** |
| **Net income** | **$40,150** |  |
| **Dividends** | **(5,000)** |  |
| **Change in retained earnings** |  | **35,150** |
| **Retained earnings, November 30, 2018** |  | **$133,650** |
|  |  |  |

|  |  |  |
| --- | --- | --- |
| **Bev’s Dry Cleaners Balance Sheet**  **November 30, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$ 81,800** |
| **Accounts receivable** |  | **75,000** |
| **Supplies** |  | **11,800** |
| **Land** |  | **85,000** |
| **Total assets** |  | **$253,600** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 48,950** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$ 71,000** |  |
| **Retained earnings** | **133,650** |  |
| **Total stockholders’ equity** |  | **204,650** |
| **Total liabilities and stockholders’ equity** |  | **$253,600** |
|  |  |  |

Prob. 1–5B (Concluded)

4. (Optional)

|  |  |  |
| --- | --- | --- |
| **Bev’s Dry Cleaners Statement of Cash Flows**  **For the Month Ended November 30, 2018** | | |
| **Cash flows from operating activities:** |  |  |
| **Cash received from customers\*** | **$115,000** |  |
| **Cash payments for expenses** |  |  |
| **and payments to creditors\*\*** | **(53,200)** |  |
| **Net cash flows from operating activities** |  | **$ 61,800** |
| **Cash flows used for investing activities:** |  |  |
| **Purchase of land** |  | **(35,000)** |
| **Cash flows from financing activities:** |  |  |
| **Cash received from issuing common stock** | **$ 21,000** |  |
| **Cash dividends** | **(5,000)** |  |
| **Net cash flows from financing activities** |  | **16,000** |
| **Net increase in cash** |  | **$ 42,800** |
| **Cash balance, November 1, 2018** |  | **39,000** |
| **Cash balance, November 30, 2018** |  | **$ 81,800** |
|  |  |  |

**\* $38,000 + $77,000; these amounts are taken from the cash column of the spreadsheet in Part 2.**

**\*\* $4,000 + $20,000 + $29,200; these amounts are taken from the cash column of the**

**spreadsheet in Part 2.**

Prob. 1–6B

A. Wages expense, $203,200 ($288,000 – $48,000 – $17,600 – $14,400 – $4,800) B. Net income, $112,000 ($400,000 – $288,000)

1. Retained Earnings, May 1, 2018, $0; Atlas Realty was organized on May 1, 2018.
2. Net income for May, $112,000; from (B)
3. Dividends, $64,000; from statement of cash flows.
4. Increase in retained earnings, $48,000 ($112,000 – $64,000)
5. Retained earnings, May 31, 2018, $48,000 (same as F)
6. Land, $120,000; from statement of cash flows.

I. Total assets, $256,000 ($123,200 + $12,800 + $120,000)

1. Common stock, $160,000; from statement of cash flows.
2. Retained earnings, $48,000; from retained earnings statement. L. Total stockholders' equity, $208,000 ($160,000 + $48,000)
3. Total liabilities and stockholders’ equity, $256,000 ($48,000 + $208,000)
4. Cash received from customers, $400,000; this is the same as fees earned since there are no accounts receivable.
5. Net cash flows from operating activities, $147,200 ($400,000 – $252,800)
6. Net cash flows from financing activities, $96,000 ($160,000 – $64,000)

Q. Net cash flows and May 31, 2018, cash balance, $123,200 ($147,200 – $120,000

+ $96,000); also, the cash balance on the balance sheet.

This Page Not Used.

# CONTINUING PROBLEM

* 1. **Assets**

**= Liabilities +**

**Stockholders' Equity**

**Cash**

**Accts.**

**+ Rec.**

**+ Supplies =**

**Accts. Payable**

**Common**

**+ Stock**

* **Dividends +**

**Fees Earned**

**June 1 + 4,000 + 4,000**

**June 2 + 3,500 + 3,500**

**Bal. 7,500 4,000 3,500**

**June 2 – 800**

**Bal. 6,700 4,000 3,500**

**June 4 + 350 + 350**

**Bal. 6,700 350 350 4,000 3,500**

**June 6 – 500**

**Bal. 6,200 350 350 4,000 3,500**

**June 8 – 675**

**Bal. 5,525 350 350 4,000 3,500**

**June 12 – 350**

**Bal. 5,175 350 350 4,000 3,500**

**June 13 – 100 – 100**

**Bal. 5,075 350 250 4,000 3,500**

**June 16 + 300 + 300**

**Bal. 5,375 350 250 4,000 3,800**

**June 22 + 1,000 + 1,000**

**Bal. 5,375 1,000 350 250 4,000 4,800**

**June 25 + 500 + 500**

**Bal. 5,875 1,000 350 250 4,000 5,300**

**June 29 – 240**

**Bal. 5,635 1,000 350 250 4,000 5,300**

**June 30 + 900 + 900**

**Bal. 6,535 1,000 350 250 4,000 6,200**

**June 30 – 400**

**Bal. 6,135 1,000 350 250 4,000 6,200**

**June 30 – 300**

**Bal. 5,835 1,000 350 250 4,000 6,200**

**June 30 – 180**

**Bal. 5,835 1,000 170 250 4,000 6,200**

**June 30 – 415**

**Bal. 5,420 1,000 170 250 4,000 6,200**

**June 30 – 1,000**

**Bal. 4,420 1,000 170 250 4,000 6,200**

**June** **30** **– 500**  **– 500**

**Bal.** **3,920**  **1,000**  **170**  **250**  **4,000 – 500 6,200**

Continuing Problem (Continued)

**Stockholders’ Equity (Continued)**

**Music**

**– Exp.**

**Office Rent**

* + **Exp.**

**Equip. Rent**

* + **Exp.**

**Adver- tising**

* + **Exp.**

**Wages**

* + **Exp.**

**Utilities**

* **Exp.**

**Supplies**

* **Exp. –**

**Misc. Exp.**

**June 1**

**June 2 Bal.**

**June 2 – 800**

**Bal. – 800**

**June 4**

**Bal. – 800**

**June 6 – 500**

**Bal. – 800 – 500**

**June 8 – 675**

**Bal. – 800 – 675 – 500**

**June 12 – 350**

**Bal. – 350 – 800 – 675 – 500**

**June 13**

**Bal. – 350 – 800 – 675 – 500**

**June 16**

**Bal. – 350 – 800 – 675 – 500**

**June 22**

**Bal. – 350 – 800 – 675 – 500**

**June 25**

**Bal. – 350 – 800 – 675 – 500**

**June 29 – 240**

**Bal. – 590 – 800 – 675 – 500**

**June 30**

**Bal. – 590 – 800 – 675 – 500**

**June 30 – 400**

**Bal. – 590 – 800 – 675 – 500 – 400**

**June 30 – 300**

**Bal. – 590 – 800 – 675 – 500 – 400 – 300**

**June 30 – 180**

**Bal. – 590 – 800 – 675 – 500 – 400 – 300 – 180**

**June 30 – 415**

**Bal. – 590 – 800 – 675 – 500 – 400 – 300 – 180 – 415**

**June 30 – 1,000**

**Bal. – 1,590 – 800 – 675 – 500 – 400 – 300 – 180 – 415**

**June 30**

**Bal. – 1,590 – 800 – 675 – 500 – 400 – 300 – 180 – 415**

Continuing Problem (Concluded) 2.

|  |  |  |
| --- | --- | --- |
| **PS Music Income Statement**  **For the Month Ended June 30, 2018** | | |
| **Fees earned:** |  | **$6,200** |
| **Expenses:** |  |  |
| **Music expense** | **$1,590** |  |
| **Office rent expense** | **800** |  |
| **Equipment rent expense** | **675** |  |
| **Advertising expense** | **500** |  |
| **Wages expense** | **400** |  |
| **Utilities expense** | **300** |  |
| **Supplies expense** | **180** |  |
| **Miscellaneous expense** | **415** |  |
| **Total expenses** |  | **4,860** |
| **Net income** |  | **$1,340** |
|  |  |  |

3.

|  |  |  |
| --- | --- | --- |
| **PS Music**  **Retained Earnings Statement For the Month Ended June 30, 2018** | | |
| **Retained earnings, June 1, 2018** |  | **$ 0** |
| **Net income** | **$1,340** |  |
| **Dividends** | **(500)** |  |
| **Change in retained earnings** |  | **840** |
| **Retained earnings, June 30, 2018** |  | **$840** |
|  |  |  |

4.

|  |  |  |
| --- | --- | --- |
| **PS Music Balance Sheet**  **June 30, 2018** | | |
| **Assets** |  |  |
| **Cash** |  | **$3,920** |
| **Accounts receivable** |  | **1,000** |
| **Supplies** |  | **170** |
| **Total assets** |  | **$5,090** |
| **Liabilities** |  |  |
| **Accounts payable** |  | **$ 250** |
| **Stockholders’ Equity** |  |  |
| **Common stock** | **$4,000** |  |
| **Retained earnings** | **840** |  |
| **Total stockholders’ equity** |  | **4,840** |
| **Total liabilities and stockholders’ equity** |  | **$5,090** |
|  |  |  |

ADM–1

# ANALYSIS FOR DECISION MAKING

* + 1. Ratio of Liabilities to Stockholders’ Equity =

$43,764

Total Liabilities

Total Stockholders’ Equity

Amazon:

$10,741

= 4.07

Best Buy:

$10,024

$3,989

= 2.51

* + 1. Amazon’s ratio exceeds 4.0, which means the total liabilities are four times as great as the stockholders’ equity. For Best Buy, the ratio is only 2.51, which means total liabilities are 2.5 times as great as the stockholders’ equity. Thus, the margin of protection is less for Amazon’s creditors than it is for Best Buy’s creditors.

ADM–2

1. Assets = Liabilities + Stockholders’ Equity Liabilities = Assets – Stockholders’ Equity

Liabilities, Year 1: $40,518 – $17,898 = $22,620 Liabilities, Year 2: $41,804 – $17,777 = $24,027 Liabilities, Year 3: $40,518 – $12,522 = $27,996

*Note:* The equality of total assets in Year 1 and Year 3 is an unusual coincidence.

1. Ratio of Liabilities to Stockholders’ Equity = Total Liabilities

Total Stockholders’ Equity

Ratio of Liabilities to Stockholders’ Equity, Year 1:

Ratio of Liabilities to Stockholders’ Equity, Year 2:

Ratio of Liabilities to Stockholders’ Equity, Year 3:

$22,620

$17,898

$24,027

$17,777

$27,996

$12,522

= 1.26

= 1.35

= 2.24

1. The ratio of liabilities to stockholders’ equity for Home Depot increased from

1.26 in Year 1 to 2.24 in Year 3, causing the margin of protection to creditors to decrease. This is a significant increase in this ratio for a three-year time period. The majority of the increase occurred between Year 2 and Year 3.

*Note to Instructor:* This increase is due to the company using debt to finance the repurchase of its common stock. This intentional transaction caused liabilities to increase and stockholders’ equity to decrease in Year 3.

ADM–3

1. Assets = Liabilities + Stockholders’ Equity Stockholders’ Equity = Assets – Liabilities

Stockholders’ Equity, Year 1: $33,559 – $17,026 = $16,533 Stockholders’ Equity, Year 2: $32,666 – $18,809 = $13,857 Stockholders’ Equity, Year 3: $32,732 – $20,879 = $11,853

1. Ratio of Liabilities to Stockholders’ Equity = Total Liabilities

Total Stockholders’ Equity

Ratio of Liabilities to Stockholders’ Equity, Year 1:

Ratio of Liabilities to Stockholders’ Equity, Year 2:

Ratio of Liabilities to Stockholders’ Equity, Year 3:

$17,026

$16,533

$18,809

$13,857

$20,879

$11,853

= 1.03

= 1.36

= 1.76

1. The ratio of liabilities to stockholders’ equity for Lowe’s increased from 1.03 in Year 1 to 1.76 in Year 3, causing the margin of protection to creditors to

decrease. This is a noticeable increase in this ratio for a three-year time period.

*Note to Instructor:* This increase occurred because the company used debt to finance the repurchase of its common stock. This intentional transaction caused liabilities to increase and stockholders’ equity to decrease over the three-year period.

1. Lowe’s ratio of liabilities to stockholders’ equity is less than that of Home Depot for two out of the three years, including the most recent year. Thus, the risk to Lowe’s creditors is slightly less than the risk to Home Depot’s creditors. The trend for both companies shows that the size of this ratio is increasing over time.

ADM–4

1. Ratio of Liabilities to Stockholders’ Equity = Total Liabilities

Total Stockholders’ Equity

Ratio of Liabilities to Stockholders’ Equity, Papa John’s:

Ratio of Liabilities to Stockholders’ Equity, Yum! Brands:

$405

$99

$6,732

$1,604

= 4.1

= 4.2

1. The ratio of liabilities to stockholders’ equity is greater than 4.0 for both companies. This means the total liabilities are more than four times as great as the stockholders’ equity. These are both very high ratios and suggest that creditors have risk with their investments in these two companies. The small level of stockholders’ equity provides only a narrow margin of protection to creditors.
2. The ratio of liabilities to stockholders’ equity is slightly higher for Yum! Brands at 4.2, compared to a 4.1 ratio for Papa John’s. Both are risky, but this 0.1 difference does not represent a material difference in risk.

TIF 1–1

# TAKE IT FURTHER

1. The car repair is a personal expense and is Marco’s personal responsibility. By using partnership funds to pay for the repair, Marco is behaving unethically because he is violating the business entity assumption. The business entity assumption treats the business as a separate entity from its owners. By taking money from the partnership for a personal expense, Marco is effectively stealing from his partners.
2. The partnership’s net income will be reduced by the $2,000 Marco has taken. This will reduce the amount of net income available to Marco’s partners.
3. Marco could ask his partners for a loan from the partnership. The loan could be repaid out of his salary or from his share of the partnership income.

TIF 1–2

A sample solution based on Nike Inc.’s Form 10-K for the fiscal year ended May 31, 2015, follows:

1. Nike, Inc.
2. Beaverton, Oregon
3. Mark G. Parker
4. Manufacturing
5. Our principal business activity is the design, development, and worldwide marketing and selling of athletic footwear, apparel, equipment, accessories, and services.
6. Income statement, statement of comprehensive income, balance sheet, statement of stockholders’ equity, statement of cash flows

TIF 1–3

Example Memo

To: My Teacher From: Ima Student Date: January 1, 20XX

Re: Causes of Accounting Fraud

Business and accounting fraud typically result from either a failure of individual character or a culture of greed within an organization. Managers and accountants often face pressure to meet or exceed a company’s financial goals. At times, supervisors can place pressure on individuals to violate accounting standards to improve a company’s reported financial results. Individuals who give in to these pressures exhibit a failure of individual character. In other situations, the organization may expect employees to violate accounting rules as part of their job. This occurs in organizations that do not value ethical decision making or fair financial reporting and exhibit a culture of ethical indifference.