CHAPTER 3
THE ACCOUNTING CYCLE:
CAPTURING ECONOMIC EVENTS

OVERVIEW OF BRIEF EXERCISES, EXERCISES, PROBLEMS, AND CRITICAL THINKING CASES

Brief Exercises	Topic	Learning Objectives	Skills
B. Ex. 3.1	The accounting cycle	1, 2, 5, 9, 10	Analysis
B. Ex. 3.2	Recording transactions	3–5	Analysis
B. Ex. 3.3	Recording transactions	7, 8	Analysis
B. Ex. 3.4	Debit and credit rules	3, 8	Analysis
B. Ex. 3.5	Changes in retained earnings	3, 6	Analysis
B. Ex. 3.6	Realization and matching principles	6, 7	Analysis
B. Ex. 3.7	Revenue realization	6, 7	Analysis, judgment
B. Ex. 3.8	Expense recognition	6, 7	Analysis, judgment
B. Ex. 3.9	Revenue realization	6, 7	Analysis
B. Ex. 3.10	Matching principle	6, 7	Analysis

Exercises	Topic	Learning Objectives	Skills
3.1	Accounting terminology	1–10	Analysis
3.2	The matching principle	6, 7	Communication, analysis
3.3	Journal and ledger relationships	2–5	Analysis
3.4	Preparing a trial balance	9	Analysis
3.5	**Real World: Apple Computer** Net income and owners' equity	6, 8	Analysis
3.6	Accounting equation relationships	2–6	Analysis
3.7	Accounting equation relationships	2–6	Analysis, communication
3.8	Revenue, expenses, and dividends	4, 6–8	Analysis
3.9	Financial statement effects	3, 6, 7	Analysis
3.10	Preparing a trial balance	3, 5, 8, 9	Analysis
3.11	Preparing a trial balance	3, 5, 8, 9	Analysis
3.12	Preparing a trial balance	3, 5, 8, 9	Analysis
3.13	Analyzing transactions	3, 6, 8	Analysis
3.14	Analyzing transactions	3, 6, 8	Analysis
3.15	**Real World: Home Depot, Inc.** Using an annual report	1–3, 7, 10	Communication, analysis

Problems Sets A, B	Topic	Learning Objectives	Skills
3.1 A,B	Recording journal entries and identifying their effects on the accounting equation	3–5	Communication, judgment
3.2 A,B	Recording journal entries and identifying their effects on the accounting equation	3–8	Analysis, judgment, communication
3.3 A,B	Recording journal entries and identifying their effects on the accounting equation	3–8	Communication, judgment, analysis
3.4 A,B	The accounting cycle	1–10	Analysis, communication
3.5 A,B	The accounting cycle	1–10	Analysis, communication
3.6 A,B	Short comprehensive problem	3–9	Analysis, communication
3.7 A,B	Short comprehensive problem	3–9	Analysis, communication
3.8 A,B	Analyzing the effects of errors	3, 8	Analysis

Critical Thinking Cases

3.1	Revenue recognition	7, 10	Analysis, communication, judgment
3.2	Income measurement	6, 7, 10	Communication, judgment, analysis
3.3	Whistle-Blowing (Ethics, fraud & corporate governance)	6, 7, 10	Analysis, judgment, communication
3.4	**Real World: PepsiCo., Inc.** *(Business Week)*	10	Analysis, technology, judgment, communication, research
3.5	**Real World: PC Connection -** Revenue from various sources (Internet)	6	Communication, technology, judgment,

DESCRIPTIONS OF PROBLEMS AND CRITICAL THINKING CASES

Below are brief descriptions of each problem and case. These descriptions are accompanied by the estimated time (in minutes) required for completion and by a difficulty rating. The time estimates assume use of the partially filled-in working papers.

Problems (Sets A and B)

3.1 A,B **Heartland Construction/North Enterprises** **30 Medium**
A company engages in numerous transactions during its first month of operations. Students are required to journalize each transaction and analyze the effect of each transaction on the accounting equation.

3.2 A,B **Environmental Services, Inc./Lyons, Inc.** **30 Medium**
Calls for a detailed analysis of numerous transactions, journalizing, and the application of the realization and matching principles.

3.3 A,B **Weida Surveying, Inc./Dana, Inc.** **35 Medium**
Requires students to journalize transactions and to understand the relationship between the income statement and the balance sheet.

3.4 A,B **Aerial Views/Tone Deliveries** **50 Strong**
Requires students to journalize and post transactions, prepare a trial balance, and understand the relationships between the income statement and balance sheet.

3.5 A,B **Dr. Schekter, DVM/Dr. Cravati, DMD** **60 Strong**
Requires students to journalize and post transactions, prepare a trial balance, and understand the relationships between the income statement and balance sheet.

3.6 A,B **Donegan's Lawn Care Service/Clown Around, Inc.** **50 Strong**
Requires students to journalize and post transactions, prepare a trial balance, and understand various relationships among financial statement elements.

3.7 A,B **Sanlucas, Inc./Ahuna, Inc.** **50 Strong**
Requires students to journalize and post transactions, prepare a trial balance, and understand various relationships among financial statement elements.

3.8 A,B **Home Team Corporation/Blind River, Inc.** **50 Strong**
Requires students to analyze the effects of errors on financial statement elements.

Critical Thinking Cases

3.1	**Revenue Recognition** Requires students to draw conclusions concerning the point at which various companies should recognize revenue.	**15 Medium**
3.2	**Measuring Income** Students are to determine whether a company's methods of measuring income are fair and reasonable. Also requires students to distinguish between net income and cash flow.	**30 Strong**
3.3	**Whistle-Blowing** **Ethics, Fraud & Corporate Governance** Students are asked to consider the legal and ethical implications of engaging in fraudulent reporting activities.	**5 Easy**
3.4	**PepsiCo, Inc.** ***Business Week*** Students are asked to consider types of information PepsiCo would track for its soft drink operations.	**15 Easy**
3.5	**PC Connection** **Revenue from Various Sources** **Internet** Using 10-K reports, students are asked to identify revenue from various sources.	**10 Easy**

SUGGESTED ANSWERS TO DISCUSSION QUESTIONS

1. Although it has no obligation to issue financial statements to creditors or investors, Baker Construction still should maintain an accounting system. For a start, the company probably has numerous reporting obligations *other than* financial statements. These include income tax returns, payroll tax returns, (including workers' compensation insurance) and payroll data, which must be reported to individual employees.

   Even though the company is not required by law to issue financial statements, Tom Baker should find such statements useful in managing the business and also in arranging financing should the business ever need additional capital.

   In addition, an accounting system provides managers and employees with a wealth of information vital to daily business operations. For example, the system keeps track of the amounts due from customers and amounts payable to employees, tax authorities, and suppliers. It also provides information about the company's cash position and the performance of different departments within the organization. Another important use of an accounting system is establishing the accountability of specific employees for the assets and operations under their direct control.

2. The three basic parts of an account are (1) its *title*, (2) a left side called the *debit* side, and (3) a right side called the *credit* side.

3. Assets are located on the *left* side of the balance sheet equation; an increase in an asset account is recorded by an entry on the *left* (or debit) side of the account. Liabilities and owners' equity are located on the *right* side of the balance sheet equation; an increase in a liability account or an owners' equity account is recorded by an entry on the *right* (or credit) side of the account.

4. Asset accounts:
   a. Increases are recorded by debits
   b. Decreases are recorded by credits

   Liability and owners' equity accounts:
   a. Increases are recorded by credits
   b. Decreases are recorded by debits

5. No, the term *debit* means an entry on the left-hand side of an account; the term *credit* simply means an entry on the right-hand side of an account. Consequently, the term *debit* means increase when applied to an asset account, but it signifies a decrease when applied to a liability or owners' equity account. The term *credit* means decrease when applied to an asset account, but it signifies an increase when applied to a liability or owners' equity account.

6. The double-entry system requires that equal dollar amounts of debit and credit entries be made for every business transaction recorded.

7. a. Credit Cash. Cash is an asset account and was decreased by this transaction. Decreases in assets are recorded by credits.

   b. Credit Office Equipment. Office Equipment is an asset account and was decreased by this transaction. Decreases in assets are recorded by credits.

   c. Debit Cash. Cash is an asset account and was increased by this transaction. Increases in assets are recorded by debits.

   d. Credit Accounts Payable. Accounts Payable is a liability account and was increased by this transaction. Increases in liabilities are recorded by credits.

   e. Credit Capital Stock. Capital Stock is an owners' equity account and was increased by this transaction. Increases in owners' equity are recorded by credits.

8. Operating profitably causes an increase in owners' equity. Usually, this increase in equity is accompanied by an increase in total assets. However, the increase in equity might be offset in part or in whole by a decrease in total liabilities.

9. No, net income does not represent an amount of cash. The entire amount of cash owned by a business appears on the asset side of the balance sheet and is entitled Cash. Net income is an increase in owners' equity and implies nothing about the *form* in which the company's assets are held.

10. *Revenue* represents the price of goods sold and of services rendered to customers during the period. It is an increase in owners' equity accompanied either by an increase in assets or a reduction in liabilities.

    Not every receipt of cash represents the earning of revenue. The borrowing of money from a bank causes cash to be received but does not increase the owners' equity and does not represent revenue. Collection of an account receivable is merely the exchange of one asset (the receivable) for another asset (cash) and does not constitute revenue.

11. The term *expenses* means the cost of the goods and services used up or consumed in the process of obtaining revenue. Expenses cause a decrease in owners' equity. To determine the net income for a given accounting period, it is necessary that all expenses of that period be deducted from the revenue earned in that period. In deciding whether a given transaction represents an expense of the current period, two questions are pertinent: (1) Was the alleged expense incurred primarily to generate revenue during the current period? (2) Does the item in question reduce the owners' equity?

    Not all cash payments represent expenses. Examples of cash payments that are not expenses include purchase of an asset such as a building or supplies, payment of an existing liability, and dividends.

12. The revenue is recognized in May. The journal entry in May consists of a $500 debit to Accounts Receivable and a $500 credit to a revenue account such as Commissions Earned or Fees Earned. The entry in June consists of a $500 debit to Cash and a $500 credit to Accounts Receivable.

13. Revenue is considered realized at the time that services are rendered to customers or goods sold are delivered to customers. The realization principle answers the question of *when* revenue should be recognized in accounting records.

14. Classic Auto Painters should recognize the paint as expense in the month of April—the month in which the paint was *used* in the effort to generate revenue. This answer demonstrates the *matching principle* —the idea that revenue should be offset by all the expenses incurred in the effort of producing that revenue.

15. The *matching principle* indicates that expenses should be recognized in the period (or periods) that the expenditure helps to produce revenue.

16. Revenue increases owners' equity; therefore revenue is recorded by a *credit.* Expenses decrease owners' equity; therefore expenses are recorded by *debits* .

17. The trial balance provides proof that the ledger is in balance. A trial balance does not, however, prove that transactions have been analyzed and recorded in the proper accounts and/or for the proper amounts. Furthermore, if a transaction were completely omitted from the ledger, the error would not be disclosed by the trial balance.

18. A dividend is a distribution of assets (usually cash) by a corporation to its stockholders. Dividends reduce both assets and owners' equity (specifically, the Retained Earnings account). Dividends are not an expense deducted from revenue in the computation of net income. Rather than being reported in the income statement as a component of net income, dividends are reported in the statement of retained earnings as a component of the Retained Earnings balance reported in the balance sheet.

19. The accrual basis of accounting calls for recording revenue in the period in which it is earned and recording expenses in the period in which they are incurred. The cash basis of accounting calls for recording revenue when it is received in cash and for recording expenses when they are paid. The accrual basis of accounting gives a more accurate picture of the profitability of a business because it matches revenue with the related expenses incurred in producing that revenue. Net income can be determined accurately only if we recognize all the revenue earned and all the related expenses incurred in a given time period.

20. Some of the more analytical functions performed by accountants include determining the information needs of decision makers, designing information systems, evaluating organizational efficiency, interpreting financial information, auditing financial records, forecasting future operations, and tax planning.

SOLUTIONS TO BRIEF EXERCISES

B. Ex. 3.1 **a.** 1. Journalize transactions.

2. Post transaction data to the ledger.
3. Prepare a trial balance.
4. Make end-of-period adjustments.
5. Prepare an adjusted trial balance.
6. Prepare financial statements.
7. Journalize and post closing entries.
8. Prepare an after-closing trial balance.

b. 1. Evaluate the efficiency of operations.

2. Establish accountability for assets and transactions.
3. Maintain a documentary record of business activities.
4. Help make business decisions.

B. Ex. 3.2

Oct.	**1**	Cash …………………………………………………	200,000	
		Capital Stock …………………………		200,000
		Issued capital stock at $50 per share.		
	4	Diagnostic Equipment ………………………………	75,000	
		Cash ……………………………………		25,000
		Notes Payable ………………………….		50,000
		Purchased equipment, paying part in cash and signing a note payable for the balance.		
	12	Accounts Payable …………………………………….	9,000	
		Cash …………………………………..		9,000
		Paid account payable to Zeller Laboratories.		
	19	Surgical Supplies …………………………………….	2,600	
		Accounts Payable ……………………..		2,600
		Purchased surgical supplies on account.		
	25	Cash …………………………………………………	24,000	
		Accounts Receivable …………………..		24,000
		Collected amount owed from Health One Insurance.		
	30	Dividends ……………………………………………	300,000	
		Cash …………………………………..		300,000
		Paid cash dividend.		

B. Ex. 3.3 **a.**

Jan. 18	Cash	30,000	
	Capital Stock		30,000
	Issued capital stock for $30,000.		
22	Cash	20,000	
	Notes Payable		20,000
	Borrowed $20,000 by issuing a note payable.		
23	Advertising Expense	100	
	Cash		100
	Paid for radio ad to be aired on January 24.		
25	Cash	1,000	
	Service Revenue		1,000
	Provided services to clients.		
26	Accounts Receivable	2,000	
	Service Revenue		2,000
	Provided services to clients on account.		
31	Cash	800	
	Accounts Receivable		800
	Collected $800 from clients for services performed on January 26.		

b. Jan. 31 Cash balance: $30,000 + $20,000 - $100 + $1,000 +$800 = $51,700 (debit)

B. Ex. 3.4

	Revenue	Expenses	Assets	Liabilities	Owners' Equity
Increases	**Credits**	**Debits**	**Debits**	**Credits**	**Credits**
Decreases	**Debits**	**Credits**	**Credits**	**Debits**	**Debits**

B. Ex. 3.5

Beginning Retained Earnings (1/1) ………	$ 75,000
Add: Income ($100,000 - $60,000) ……….	40,000
Less: Dividends…………………...……….	(5,000)
Ending Retained Earnings (1/31)………….	$110,000

The purchase of land for $20,000 does not affect the balance of Retained Earnings.

B. Ex. 3.6 **a.** Revenue is recognized when it is earned. Thus, KPRM Radio will recognize revenue from Breeze Camp Ground in the months that the ads are aired (at $50 per ad):

	May	June	July
Revenue	$ 100	$ 350	$ 50

b. Expenses are matched to the periods in which they contribute to generating revenue. Thus, Breeze Camp Ground will recognize advertising expense in the months that the ads are aired (at $50 per ad):

	May	June	July
Expense	$ 100	$ 350	$ 50

B. Ex. 3.7 **a.** An investment by stockholders does not constitute revenue. Although this investment causes an increase in owners' equity, this increase was not earned. It did not result from the rendering of services or sale of merchandise to outsiders.

b. The collection of an account receivable does not increase owners' equity and does not represent revenue.

c. The borrowing of money from a bank creates a liability; it does not increase the owners' equity and does not represent revenue.

d. The interest was earned in May and represents revenue of that month, despite the fact that no withdrawals were made from the bank.

e. This fee was earned in May and represents revenue of that month, despite the fact that collection will not be made until June.

B. Ex. 3.8 **a.** The purchase of a copying machine does not represent an expense. The asset Cash is exchanged for the asset Office Equipment, without any change in owners' equity. The purpose of the transaction was to obtain the use of the copier over a number of years, rather than to generate revenue only during the current period. (Evergreen will recognize depreciation expense on this asset throughout its useful life, but the *purchase* does not represent an expense in March. Depreciation issues are introduced in Chapter 4.)

b. Gasoline purchased is an expense because it is ordinarily used up in the current period. These purchases decrease the owners' equity and are for the purpose of generating revenue.

c. Payment to an employee for services rendered in March is a March expense. Such a payment is made to generate revenue and decreases owners' equity.

d. The payment to the attorney for services rendered in a prior period reduced an existing liability but did not affect the owners' equity. The payment was not an expense.

e. The dividend does not constitute an expense. Unlike payments for advertising, rent, and supplies, dividends do not generate revenue. Dividends constitute a return to stockholders of a portion of their equity in the business.

B. Ex. 3.9 Revenue is recognized when it is earned, not necessarily when cash is received. Thus, the airline will recognize revenue of $800,000 in its October income statement (of which $500,000 was collected in September and $300,000 was collected in October).

B. Ex. 3.10 Expenses are recognized when they are incurred, not necessarily when cash is paid. Thus, the company will report salary expense of $24,000 in its May income statement (of which $15,000 was paid in May and $9,000 was paid in June).

SOLUTIONS TO EXERCISES

Ex. 3.1 **a.** Accounting period

b. Accounting cycle

c. None (This statement describes the accounting convention of conservatism.)

d. Net income

e. Realization principle

f. Credit

g. Matching principle

h. Expenses

Ex. 3.2 **a.** Costs of owning and operating an automobile (estimates will vary; the following list is only an example):

Insurance	$	1,000
Gasoline (15,000 miles at 30 mpg. = $4.20/gal.)		2,100
Registration and license		100
Repairs and maintenance		200
Depreciation		1,200
Interest on car loan*		500
Annual total	$	5,100
Average cost per mile ($5,100 / 15,000 miles)		**$0.34**

**Note to instructor:* It is worth noting that including both depreciation and the "principal" portion of the car loan would be "double-counting" the purchase price of the car. Depreciation issues are introduced in Chapter 4.

b. Although you spent no money *during* this trip, you incurred significant costs. For example, you have used much of the gasoline in your tank. Also, the more miles you drive, the higher your repair and maintenance costs, depreciation, and insurance. Assuming that it cost you about 34 cents per mile to own and operate your vehicle, about $34 would be a reasonable estimate of your "driving expenses."

Note to instructor: Most employers do base their reimbursement of driving expenses on an average cost per mile. You may want to point out that the *incremental costs* of this trip are much less than the average cost. Thus, employees usually benefit somewhat in the short-term when they are reimbursed for using their own cars.

Ex. 3.3	**Nov.**	**1**	Cash	120,000	
			Capital Stock		120,000
			Issued stock in exchange for cash.		
		8	Land	70,000	
			Building	58,600	
			Cash		33,600
			Notes Payable		95,000
			Purchased land and building, by paying $33,600 cash and issuing a note payable for the remaining balance.		
		15	Office Equipment	3,200	
			Accounts Payable		3,200
			Purchased office equipment on account.		
		21	Accounts Payable	480	
			Office Equipment		480
			Returned some of the office equipment purchased on November 15.		
		25	Notes Payable	12,000	
			Cash		12,000
			Paid note payable.		
		30	Vehicles	9,400	
			Cash		1,400
			Notes Payable		8,000
			Purchased vehicles by paying $1,400 cash and issuing a note payable for the remaining balance.		

Ex. 3.4

AVENSON INSURANCE COMPANY
Trial Balance
November 30, 20__

Cash	$ 73,000	
Land	70,000	
Building	58,600	
Office equipment	2,720	
Vehicles	9,400	
Notes payable		$ 91,000
Accounts payable		2,720
Capital stock		120,000
	$ 213,720	$ 213,720

Ex. 3.5 **a.** Liabilities at the beginning of the year: \$17.2 billion – \$10.0 billion = \$7.2 billion

b. Owners' equity at the end of the year: \$25.3 billion – \$10.8 billion = \$14.5 billion

c.

Ending retained earnings ………...............	\$ 9,100,000,000
Less: Beginning retained earnings ….…..	(5,600,000,000)
Increase in retained earnings …..………..	\$ 3,500,000,000
Less: Dividends ……………..................…	-
Net income ……………………………….	\$ 3,500,000,000

Ex. 3.6

Trans-action	Income Statement: Revenue	– Expenses	= Net Income	Balance Sheet: Assets	– Liabilities	= Owners' Equity
1.	I	NE	I	I	NE	I
2.	NE	NE	NE	D	D	NE
3.	NE	NE	NE	NE	NE	NE
4.	NE	I	D	NE	I	D
5.	NE	NE	NE	I	I	NE
6.	NE	NE	NE	D	NE	D

Ex. 3.7

a.

Trans-action	Income Statement: Revenue	– Expenses	= Net Income	Balance Sheet: Assets	– Liabilities	= Owners' Equity
1.	NE	I	D	NE	I	D
2.	I	NE	I	I	NE	I
3.	NE	NE	NE	D	NE	D
4.	NE	NE	NE	I	I	NE
5.	NE	I	D	D	NE	D
6.	NE	NE	NE	NE	NE	NE
7.	NE	NE	NE	I	I	NE
8.	NE	NE	NE	D	D	NE

b.

1. Incurred wages expense to be paid at a later date.
2. Earned revenue to be collected at a later date.
3. Declared and paid a cash dividend.
4. Purchased office supplies on account.
5. Incurred and paid repairs expense.
6. Collected cash from a customer for revenue earned previously on account.
7. Purchased tools and equipment by paying part in cash and issuing a note payable for the remaining balance.
8. Paid an outstanding account payable.

Ex. 3.8

a.

Apr.	**5**	Accounts Receivable ………………………………	900	
		Drafting Fees Earned ……………………		900
		Prepared plans for Spangler Construction; payment due in 30 days.		
May	**17**	Dividends ……………………………………….	5,000	
		Dividends Payable ………………………		5,000
		Declared cash dividend; payment due June 25.		
May	**29**	Professional Expenses …………………………..	2,000	
		Accounts Payable ……………………….		2,000
		Received accounting bill from Bob Needham due on June 10.		
June	**4**	Cash …………………………………………….	900	
		Accounts Receivable …………………….		900
		Received full payment from Spangler Construction for bill sent April 5.		
June	**10**	Accounts Payable ………………………………	2,000	
		Cash …………………………………….		2,000
		Paid amount owed to Bob Needham, CPA.		
June	**25**	Dividends Payable ……………………………..	5,000	
		Cash …………………………………….		5,000
		Paid cash dividend declared May 17.		

b. The following transactions will not cause a change in net income.

May 17: Declaration of a cash dividend.
June 4: Collection of an account receivable.
June 10: Payment of an account payable.
June 25: Payment of a dividend payable.

Ex. 3.9

Transaction	Net Income	Assets	Liabilities	Equity
a.	NE	I	NE	I
b.	NE	I	I	NE
c.	D	NE	I	D
d.	NE	NE	NE	NE
e.	NE	D	D	NE
f.	NE	NE	I	D
g.	NE	NE	NE	NE
h.	NE	NE	NE	NE

Ex. 3.10	**a.**	**May**	**3**	Cash…………………………………………	800,000	
				Capital Stock…………………………….		800,000
				Issued capital stock for $800,000.		
			4	Office Rent Expense……………………………..	1,000	
				Cash……………………………………….		1,000
				Paid May office rent expense.		
			5	Office Supplies…………………………………	400	
				Cash………………………………….		400
				Purchased office supplies.		
			15	Office Equipment……………………………….	8,000	
				Accounts Payable………………………		8,000
				Purchased office equipment on account. Amount due June 15.		
			18	Vehicles………………………………………	27,000	
				Cash …………………………………….		7,000
				Notes Payable……………………………		20,000
				Purchased a company car. Paid $7,000 cash and issued a $20,000 note payable for the balance.		
			20	Accounts Receivable…………………………	32,000	
				Client Revenue………………………..		32,000
				Billed clients for services on account.		
			26	Dividends……………………………………….	5,000	
				Dividends Payable………………………		5,000
				Declared dividend to be distributed in June.		
			29	Utilities Expense………………………………..	200	
				Cash……………….……………………		200
				Paid May utilities.		
			30	Cash……………………………………………	30,000	
				Accounts Receivable……………………		30,000
				Collected cash on account from clients billed on May 20.		
			31	Salary Expense…………………………………	14,000	
				Cash……………………………………		14,000
				Paid salary expense incurred in May.		

b.

Cash

May 3	800,000	May 4	1,000
May 30	30,000	May 5	400
		May 18	7,000
		May 29	200
		May 31	14,000
May 31 bal.	807,400		

Accounts Receivable

May 20	32,000	May 30	30,000
May 31 bal.	2,000		

Office Supplies

May 5	400		
May 31 bal.	400		

Office Equipment

May 15	8,000		
May 31 bal.	8,000		

Vehicles

May 18	27,000		
May 31 bal.	27,000		

Notes Payable

		May 18	20,000
		May 31 bal.	20,000

Accounts Payable

		May 15	8,000
		May 31 bal.	8,000

Dividends Payable

		May 26	5,000
		May 31 bal.	5,000

Capital Stock

		May 3	800,000
		May 31 bal.	800,000

Client Revenue

		May 20	32,000
		May 31 bal.	32,000

Office Rent Expense

May 4	1,000		
May 31 bal.	1,000		

Salary Expense

May 31	14,000		
May 31 bal.	14,000		

Utilities Expense

May 29	200		
May 31 bal.	200		

Dividends

May 26	5,000		
May 31 bal.	5,000		

c.

Trafflet Enterprises
Trial Balance
May 31, 2009

	Debit	**Credit**
Cash…………………………………….	$807,400	
Accounts receivable……………………	2,000	
Office supplies…………………………	400	
Office equipment………………………	8,000	
Vehicles………………………………..	27,000	
Notes payable………………………….		$20,000
Accounts payable……………………….		8,000
Dividends payable……………………..		5,000
Dividends………………………………..	5,000	
Capital stock…………………………..		800,000
Client revenue………………………….		32,000
Office rent expense……………………	1,000	
Salary expense………………………..	14,000	
Utilities expense………………………..	200	
Total…………………………………….	$865,000	$865,000

					Debit	Credit
Ex. 3.11	**a.**	**Sep.**	**2**	Cash…………………………………………	900,000	
				Capital Stock…………………………….		900,000
				Issued capital stock for $900,000.		
			4	Land……………………………………………	50,000	
				Building………………………………………..	300,000	
				Cash …………………………………….		200,000
				Notes Payable……………………………		150,000
				Purchased land and building for $350,000. Paid $200,000 cash and issued a note payable for the balance.		
			12	Office Supplies…………………………………	600	
				Accounts Payable…………………………		600
				Purchased office supplies on account.		
			19	Accounts Receivable………………………….	75,000	
				Client Revenue………………………….		75,000
				Billed clients on account for services.		
			29	Salary Expense…………………………………	24,000	
				Cash………………………………………		24,000
				Recorded and paid salary expense.		
			30	Cash…………………………………………	30,000	
				Accounts Receivable……………………		30,000
				Collected cash on account from clients billed on September 19.		

b.

Cash

Sep. 2	900,000	Sep. 4	200,000
Sep. 30	30,000	Sep. 29	24,000
Sep. 30 bal.	706,000		

Accounts Receivable

Sep. 19	75,000	Sep. 30	30,000
Sep. 30 bal.	45,000		

Office Supplies

Sep. 12	600		
Sep. 30 bal.	600		

Land

Sep. 4	50,000		
Sep. 30 bal.	50,000		

Building

Sep. 4	300,000		
Sep. 30 bal.	300,000		

Notes Payable

		Sep. 4	150,000
		Sep. 30 bal.	150,000

Accounts Payable

		Sep. 12	600
		Sep. 30 bal.	600

Capital Stock

		Sep. 2	900,000
		Sep. 30 bal.	900,000

Client Revenue

		Sep. 19	75,000
		Sep. 30 bal.	75,000

Salary Expense

Sep. 29	24,000		
Sep. 30 bal.	24,000		

c.

McMillan Corporation
Trial Balance
September 30, 2009

	Debit	Credit
Cash…………………………………	$706,000	
Accounts receivable………………………	45,000	
Office supplies…………………………	600	
Land……………………………………	50,000	
Building…………………………………	300,000	
Notes payable………………………….		$150,000
Accounts payable……………………….		600
Capital stock…………………………..		900,000
Client revenue………………………….		75,000
Salary expense………………………….	24,000	
Total………………………………….	$1,125,600	$1,125,600

Ex. 3.12	**a. Feb.**	**1**	Cash…………………………………………….	750,000	
			Capital Stock…………………………….		750,000
			Issued capital stock for $750,000.		
		5	Cash…………………………………………….	50,000	
			Notes Payable……………………………		50,000
			Borrowed cash from bank by issuing a note payable.		
		8	Land…………………………………………..	100,000	
			Buildings…………………………………….	450,000	
			Office Equipment……………………………….	50,000	
			Cash…………………………………..		300,000
			Notes Payable……………………………		300,000
			Purchased land, building, and equipment building for $600,000. Paid $300,000 and issued a note payable for the balance.		
		11	Office Supplies………………………………….	600	
			Accounts Payable………………………..		600
			Purchased offices supplies on account.		
		14	Advertising Expense…………………………….	400	
			Cash …………………………………….		400
			Paid the newspaper $400 for an advertisement to be printed on February 18.		
		20	Accounts Payable………………………………	100	
			Office Supplies…………………………..		100
			Returned defective office supplies purchased on February 11. Received a $100 credit.		
		22	Cash……………………………………………..	6,000	
			Client Service Revenue…………………		6,000
			Collected cash from clients for services rendered.		
		24	Accounts Receivable…………………………	9,000	
			Client Service Revenue…………………		9,000
			Billed clients for services on account.		
		25	Salary Expense…………………………………	5,000	
			Cash……………………………………		5,000
			Paid salary expense incurred in February.		
		28	Accounts Payable………………………………	500	
			Cash……………………………………		500
			Paid for office supplies purchased February 11.		

b.

Cash

Feb. 1	750,000	Feb. 8	300,000
Feb. 5	50,000	Feb. 14	400
Feb. 22	6,000	Feb. 25	5,000
		Feb. 28	500
Feb. 28 bal.	500,100		

Accounts Receivable

Feb. 24	9,000		
Feb. 28 bal.	9,000		

Office Supplies

Feb. 11	600	Feb. 20	100
Feb. 28 bal.	500		

Land

Feb. 8	100,000		
Feb. 28 bal.	100,000		

Buildings

Feb. 8	450,000		
Feb. 28 bal.	450,000		

Office Equipment

Feb. 8	50,000		
Feb. 28 bal.	50,000		

Notes Payable

		Feb. 5	50,000
		Feb. 8	300,000
		Feb. 28 bal.	350,000

Accounts Payable

Feb. 20	100	Feb. 11	600
Feb. 28	500		
		Feb. 28 bal.	0

Capital Stock

		Feb. 1	750,000
		Feb. 28 bal.	750,000

Client Service Revenue

		Feb. 22	6,000
		Feb. 24	9,000
		Feb. 28 bal.	15,000

Advertising Expense

Feb. 14	400		
Feb. 28 bal.	400		

Salary Expense

Feb. 25	5,000		
Feb. 28 bal.	5,000		

c.

Herrold Consulting Incorporated
Trial Balance
February 28, 2009

	Debit	Credit
Cash……………………………………	$500,100	
Accounts receivable……………………	9,000	
Office supplies………………………	500	
Land……………………………………	100,000	
Building…………………………………	450,000	
Office equipment………………………	50,000	
Notes payable…………………………		$350,000
Capital stock…………………………..		750,000
Client service revenue…………………		15,000
Advertising expense……………………	400	
Salary expense…………………………	5,000	
Total……………………………………	$1,115,000	$1,115,000

Ex. 3.13

	Transaction
1.	e.
2.	f.
3.	b.
4.	a.
5.	d.
6.	c.

Ex. 3.14

	Transaction
1.	d.
2.	e.
3.	a.
4.	f.
5.	c.
6.	b.

Ex. 3.15

a. The company's balance sheet is dated February 3, 2008. Thus, it is apparent that its financial year does not coincide with the calendar year.

b. $44,324 = $26,610 + $17,714

c. Cash (and equivalents) decreased from $600 million to $445 million during the year. Thus, credits to Cash exceeded debits by $155 million.

SOLUTIONS TO PROBLEMS SET A

30 Minutes, Medium

PROBLEM 3.1A
HEARTLAND CONSTRUCTION

a.				
		General Journal		
20__				
Feb.	1	Cash	500,000	
		Capital Stock		500,000
		Issued 25,000 shares of Capital Stock.		
	10	Land	100,000	
		Office Building	200,000	
		Cash		60,000
		Notes Payable		240,000
		Purchased land and office building.		
	16	Computer Systems	12,000	
		Cash		12,000
		Purchased computer system.		
	18	Office Furnishings	9,000	
		Cash		1,000
		Accounts Payable		8,000
		Purchased office furnishings.		
	22	Office Supplies	300	
		Cash		300
		Purchased office supplies.		
	23	Accounts Receivable	36	
		Computer Systems		36
		Refund due from PC World.		
	27	Accounts Payable	4,000	
		Cash		4,000
		Made payment on an account payable.		
	28	Cash	36	
		Accounts Receivable		36
		Collected cash refunded by PC World.		

PROBLEM 3.1A
HEARTLAND CONSTRUCTION (concluded)

b.

Transaction	**Assets**	**=**	**Liabilities**	**+**	**Owners' Equity**
Feb. 1	+ $500,000 (Cash)		$0		+ $500,000 (Capital
Feb. 10	+ $100,000 (Land) + $200,000 (Office Building) – $60,000 (Cash)		+ $240,000 (Notes Payable)		$0
Feb. 16	+ $12,000 (Computer Systems) – $12,000 (Cash)		$0		$0
Feb. 18	+ $9,000 (Office Furnishings) – $1,000 (Cash)		+ $8,000 (Accounts Payable)		$0
Feb. 22	+ $300 (Office Supplies) – $300 (Cash)		$0		$0
Feb. 23	+ $36 (Accounts Receivable) – $36 (Computer Systems)		$0		$0
Feb. 27	– $4,000 (Cash)		- $4,000 (Accounts Payable)		$0
Feb. 28	+ $36 (Cash) – $36 (Accounts Receivable)		$0		$0

30 Minutes, Medium

PROBLEM 3.2A
ENVIRONMENTAL SERVICES, INC.

a. **(1)** **(a)** The asset Accounts Receivable was increased. Increases in assets are recorded by debits. Debit Accounts Receivable, $2,500.

(b) Revenue has been earned. Revenue increases owners' equity. Increases in owners' equity are recorded by credits. Credit Testing Service Revenue, $2,500.

(2) **(a)** The asset Testing Supplies was increased. Increases in assets are recorded by debits. Debit Testing Supplies, $3,800.

(b) The asset Cash was decreased. Decreases in assets are recorded by credits. Credit Cash, $800.

(c) The liability Accounts Payable was increased. Increases in liabilities are recorded by credits. Credit Accounts Payable, $3,000.

(3) **(a)** The liability Accounts Payable was decreased. Decreases in liabilities are recorded by debits. Debit Accounts Payable, $100.

(b) The asset Testing Supplies was decreased. Decreases in assets are recorded by credits. Credit Testing Supplies, $100.

(4) **(a)** The asset Cash was increased. Increases in assets are recorded by debits. Debit Cash, $20,000.

(b) The owners' equity account Capital Stock was increased. Increases in owners' equity are recorded by credits. Credit Capital Stock, $20,000.

(5) **(a)** The asset Cash was increased. Increases in assets are recorded by debits. Debit Cash, $600.

(b) The asset Accounts Receivable was decreased. Decreases in assets are recorded by credits. Credit Accounts Receivable, $600.

(6) **(a)** The liability Accounts Payable was decreased. Decreases in liabilities are recorded by debits. Debit Accounts Payable, $2,900 ($3,800 - $800 - $100).

(b) The asset Cash was decreased. Decreases in assets are recorded by credits. Credit Cash, $2,900.

(7) **(a)** The Dividends account was increased. Dividends decrease the owners' equity account Retained Earnings. Decreases in owners' equity are recorded by debits. Debit Dividends, $6,800.

(b) The asset Cash was decreased. Decreases in assets are recorded by credits. Credit Cash, $6,800.

PROBLEM 3.2A
ENVIRONMENTAL SERVICES, INC. (continued)

b.

General Journal

20__		(1)		
Aug.	1	Accounts Receivable	2,500	
		Testing Service Revenue		2,500
		Billed customers for services rendered.		
		(2)		
	3	Testing Supplies	3,800	
		Cash		800
		Accounts Payable		3,000
		Purchased testing supplies.		
		(3)		
	5	Accounts Payable	100	
		Testing Supplies		100
		Returned portion of testing supplies purchased on		
		Aug. 3.		
		(4)		
	17	Cash	20,000	
		Capital Stock		20,000
		Issued 2,500 shares of capital stock at $8 per share.		
		(5)		
	22	Cash	600	
		Accounts Receivable		600
		Received partial payment for services billed on		
		Aug. 1.		
		(6)		
	29	Accounts Payable	2,900	
		Cash		2,900
		Paid outstanding balance owed for testing supplies		
		purchased on Aug. 3.		
		(7)		
	30	Dividends	6,800	
		Cash		6,800
		Declared and paid a cash dividend.		

PROBLEM 3.2A
ENVIRONMENTAL SERVICES, INC. (concluded)

c. The realization principle requires that revenue be recorded when it is *earned*, even if cash for the goods or services provided has not been received.

d. The matching principle requires that expenses incurred in an accounting period be matched with revenue earned in the same period. Testing supplies are recorded as an asset when they are first purchased. As these supplies are used in a particular accounting period, their cost will be matched against the revenue earned in that period.

35 Minutes, Medium

PROBLEM 3.3A
WEIDA SURVEYING, INC.

a.

	Income Statement			Balance Sheet		
Transaction	Revenue –	Expenses =	Net Income	Assets –	Liabilities =	Owners' Equity
Sept. 1	NE	I	D	D	NE	D
Sept. 3	I	NE	I	I	NE	I
Sept. 9	I	NE	I	I	NE	I
Sept. 14	NE	I	D	NE	I	D
Sept. 25	NE	NE	NE	NE	NE	NE
Sept. 26	I	NE	I	I	NE	I
Sept. 29	NE	NE	NE	D	D	NE
Sept. 30	NE	NE	NE	D	NE	D

PROBLEM 3.3A
WEIDA SURVEYING, INC. (concluded)

b.

General Journal

Sept.	1	Rent Expense	4,400	
		Cash		4,400
		Paid September rent.		
	3	Accounts Receivable	5,620	
		Surveying Revenue		5,620
		Billed Fine Line Homes for surveying services.		
	9	Cash	2,830	
		Surveying Revenue		2,830
		Collected cash from Sunset Ridge Development for		
		services provided.		
	14	Advertising Expense	165	
		Accounts Payable		165
		Placed ad in the newspaper to be published on		
		Sept. 20. Total amount due in 30 days.		
	25	Cash	5,620	
		Accounts Receivable		5,620
		Received payment from Fine Line Homes for		
		service billed on Sept. 3.		
	26	Cash	400	
		Accounts Receivable	1,490	
		Surveying Revenue		1,890
		Collected partial payment from Thompson Co. and		
		billed remainder.		
	29	Accounts Payable	165	
		Cash		165
		Paid newspaper for advertisement published on		
		Sept. 20.		
	30	Dividends	7,600	
		Cash		7,600
		Declared and paid a cash dividend.		

c. Three situations in which a cash payment does not involve an expense include: (1) the payment of a cash dividend, (2) the payment of a liability for a previously recorded expense, and (3) the purchase of an asset, including expenses paid in advance such as insurance, rent, and advertising.

50 Minutes,Strong

PROBLEM 3.4A
AERIAL VIEWS

a.

	Income Statement			Balance Sheet		
Transaction	Revenue –	Expenses =	Net Income	Assets –	Liabilities =	Owners' Equity
June 1	NE	NE	NE	I	NE	I
June 2	NE	NE	NE	I	I	NE
June 4	NE	I	D	D	NE	D
June 15	I	NE	I	I	NE	I
June 15	NE	I	D	D	NE	D
June 18	NE	I	D	D	NE	D
June 25	NE	NE	NE	NE	NE	NE
June 30	I	NE	I	I	NE	I
June 30	NE	I	D	D	NE	D
June 30	NE	I	D	NE	I	D
June 30	NE	NE	NE	NE	I	D

PROBLEM 3.4A
AERIAL VIEWS (continued)

b.

General Journal

2009				
June	1	Cash	60,000	
		Capital Stock		60,000
		Issued stock to Wendy Winger.		
	2	Aircraft	220,000	
		Cash		40,000
		Notes Payable		180,000
		Purchased plane from Utility Aircraft.		
	4	Rent Expense	2,500	
		Cash		2,500
		Paid office rent for June.		
	15	Accounts Receivable	8,320	
		Aerial Photography Revenue		8,320
		Billed customers for first half of June.		
	15	Salaries Expense	5,880	
		Cash		5,880
		Paid salaries for first half of June.		
	18	Maintenance Expense	1,890	
		Cash		1,890
		Paid Hannigan's Hangar for repair services.		
	25	Cash	4,910	
		Accounts Receivable		4,910
		Collected portion of amount billed to customers.		
	30	Accounts Receivable	16,450	
		Aerial Photography Revenue		16,450
		Billed customers for services rendered through		
		month-end.		
	30	Salaries Expense	6,000	
		Cash		6,000
		Paid salaries through month-end.		
	30	Fuel Expense	2,510	
		Accounts Payable		2,510
		Received bill for fuel used during June.		
	30	Dividends	2,000	
		Dividends Payable		2,000
		Declared dividend payable June 15.		

PROBLEM 3.4A
AERIAL VIEWS (continued)

c.

Cash					
Date		Explanation	Debit	Credit	Balance
2009					
June	1		60,000		60,000
	2			40,000	20,000
	4			2,500	17,500
	15			5,880	11,620
	18			1,890	9,730
	25		4,910		14,640
	30			6,000	8,640

Accounts Receivable					
Date		Explanation	Debit	Credit	Balance
2009					
June	15		8,320		8,320
	25			4,910	3,410
	30		16,450		19,860

Aircraft					
Date		Explanation	Debit	Credit	Balance
2009					
June	2		220,000		220,000

Notes Payable					
Date		Explanation	Debit	Credit	Balance
2009					
June	2			180,000	180,000

Accounts Payable					
Date		Explanation	Debit	Credit	Balance
2009					
June	30			2,510	2,510

PROBLEM 3.4A
AERIAL VIEWS (continued)

Dividends Payable					
Date		Explanation	Debit	Credit	Balance
2009					
June	30			2,000	2,000

Capital Stock					
Date		Explanation	Debit	Credit	Balance
2009					
June	1			60,000	60,000

Dividends					
Date		Explanation	Debit	Credit	Balance
2009					
June	30		2,000		2,000

Aerial Photography Revenue					
Date		Explanation	Debit	Credit	Balance
2009					
June	15			8,320	8,320
	30			16,450	24,770

Maintenance Expense					
Date		Explanation	Debit	Credit	Balance
2009					
June	18		1,890		1,890

PROBLEM 3.4A
AERIAL VIEWS (continued)

Fuel Expense

Date		Explanation	Debit	Credit	Balance
2009					
June	30		2,510		2,510

Salaries Expense

Date		Explanation	Debit	Credit	Balance
2009					
June	15		5,880		5,880
	30		6,000		11,880

Rent Expense

Date		Explanation	Debit	Credit	Balance
2009					
June	4		2,500		2,500

PROBLEM 3.4A
AERIAL VIEWS (continued)

d.

AERIAL VIEWS Trial Balance June 30, 2009		
Cash	$ 8,640	
Accounts Receivable	19,860	
Aircraft	220,000	
Notes payable		$ 180,000
Accounts payable		2,510
Dividends payable		2,000
Capital stock		60,000
Retained earnings		0
Dividends	2,000	
Aerial photography revenue		24,770
Maintenance expense	1,890	
Fuel expense	2,510	
Salaries expense	11,880	
Rent expense	2,500	
	$ 269,280	$ 269,280

PROBLEM 3.4A
AERIAL VIEWS (concluded)

e.

Total Assets:		
Cash	$ 8,640	
Accounts Receivable	19,860	
Aircraft	220,000	
Total assets		$ 248,500
Total liabilities:		
Notes payable	$ 180,000	
Accounts payable	2,510	
Dividends payable	2,000	
Total liabilities		$ 184,510
Total stockholders' equity:		
Total assets - total liabilities ($248,500 - $184,510)		$ 63,990

The above figures are most likely not the amounts to be reported in the balance sheet dated June 30. The accounting cycle includes adjustments that must be made to the trial balance figures before financial statements are prepared. The adjusting process is covered in Chapter 4.

60 Minutes, Strong

PROBLEM 3.5A
DR. SCHEKTER, DVM

a.

	Income Statement			Balance Sheet		
Transaction	Revenue –	Expenses =	Net Income	Assets –	Liabilities =	Owners' Equity
May 1	NE	NE	NE	I	NE	I
May 4	NE	NE	NE	I	I	NE
May 9	NE	NE	NE	NE	NE	NE
May 16	NE	NE	NE	I	I	NE
May 21	NE	NE	NE	NE	NE	NE
May 24	I	NE	I	I	NE	I
May 27	NE	I	D	NE	I	D
May 28	NE	NE	NE	NE	NE	NE
May 31	NE	I	D	D	NE	D

PROBLEM 3.5A
DR. SCHEKTER, DVM (continued)

b.

General Journal

2009				
May	1	Cash	400,000	
		Capital Stock		400,000
		Issued 5,000 shares of capital stock.		
	4	Land	70,000	
		Building	180,000	
		Cash		100,000
		Notes Payable		150,000
		Purchased land and building.		
	9	Medical Instruments	130,000	
		Cash		130,000
		Purchased medical instruments.		
	16	Office Fixtures & Equipment	50,000	
		Cash		20,000
		Accounts Payable		30,000
		Purchased fixtures and equipment.		
	21	Office Supplies	5,000	
		Cash		5,000
		Purchased office supplies.		
	24	Cash	1,900	
		Accounts Receivable	300	
		Veterinary Service Revenue		2,200
		Recorded veterinary service revenue earned.		
	27	Advertising Expense	400	
		Accounts Payable		400
		Recorded advertising expense incurred in May.		
	28	Cash	100	
		Accounts Receivable		100
		Collected cash for May 24 services.		
	31	Salary Expense	2,800	
		Cash		2,800
		Paid May salary expense.		

PROBLEM 3.5A
DR. SCHEKTER, DVM (continued)

c.

Cash

Debit		Credit	
May 1	400,000	May 4	100,000
May 24	1,900	May 9	130,000
May 28	100	May16	20,000
		May 21	5,000
		May 31	2,800
May 31 Bal.	144,200		

Notes Payable

Debit		Credit	
		May 4	150,000
		May 31 Bal.	150,000

Accounts Receivable

Debit		Credit	
May 24	300	May 28	100
May 31 Bal.	200		

Accounts Payable

Debit		Credit	
		May 16	30,000
		May 27	400
		May 31 Bal.	30,400

Office Supplies

Debit		Credit	
May 21	5,000		
May 31 Bal.	5,000		

Capital Stock

Debit		Credit	
		May 1	400,000
		May 31 Bal.	400,000

Medical Instruments

Debit		Credit	
May 9	130,000		
May 31 Bal.	130,000		

Veterinary Service Revenue

Debit		Credit	
		May 24	2,200
		May 31 Bal.	2,200

Office, Fixtures & Equipment

Debit		Credit	
May 16	50,000		
May 31 Bal.	50,000		

Advertising Expense

Debit		Credit	
May 27	400		
May 31 Bal.	400		

Land

Debit		Credit	
May 4	70,000		
May 31 Bal.	70,000		

Salary Expense

Debit		Credit	
May 31	2,800		
May 31 Bal.	2,800		

Building

Debit		Credit	
May 4	180,000		
May 31 Bal.	180,000		

PROBLEM 3.5A

d.

DR. SCHEKTER, DVM (continued)

DR. SCHEKTER, DVM		
Trial Balance		
May 31, 2009		
Cash	$ 144,200	
Accounts receivable	200	
Office supplies	5,000	
Medical instruments	130,000	
Office fixtures & equipment	50,000	
Land	70,000	
Building	180,000	
Notes payable		$ 150,000
Accounts payable		30,400
Capital stock		400,000
Retained earnings		0
Veterinary service revenue		2,200
Advertising expense	400	
Salary expense	2,800	
	$ 582,600	$ 582,600

PROBLEM 3.5A
DR. SCHEKTER, DVM (concluded)

e.

Total Assets:		
Cash	$ 144,200	
Accounts receivable	200	
Office supplies	5,000	
Medical instruments	130,000	
Office fixtures & equipment	50,000	
Land	70,000	
Building	180,000	
Total assets		$ 579,400
Total liabilities:		
Notes payable	$ 150,000	
Accounts payable	30,400	
Total liabilities		$ 180,400
Total owners' (stockholders') equity:		
Total assets - total liabilities ($579,400 -$180,400)		$ 399,000
As shown below, the business was not profitable in its first month of operations:		
Veterinary service revenue		$ 2,200
Less: Advertising expense	$ 400	
Salary expense	2,800	$ 3,200
Net loss		$ (1,000)
Note to instructor: It is not uncommon for new small businesses to initially report a net loss from operations. In this particular situation, there were so few revenue and expense transactions in May that it is difficult, if not impossible, to draw any conclusions about the expected performance of the veterinary clinic in the future.		

50 Minutes, Strong

PROBLEM 3.6A
DONEGAN'S LAWN CARE SERVICE

a.

General Journal

2009				
July	18	Cash	1,500	
		Capital Stock		1,500
		Issued 500 shares of capital stock.		
	22	Office Supplies	100	
		Accounts Payable		100
		Purchased office supplies on account.		
	23	Mowing Equipment	2,000	
		Cash		400
		Notes payable		1,600
		Purchased mowing equipment paying $400 cash		
		and issuing a $1,600 note payable for the balance.		
	24	Fuel Expense	25	
		Cash		25
		Paid for gasoline to be used in July.		
	25	Accounts Receivable	150	
		Mowing Revenue		150
		Billed Lost Creek Cemetery for mowing services.		
		Payment is due July 30.		
	26	Accounts Receivable	200	
		Mowing Revenue		200
		Billed Golf View Condominium for mowing		
		services. Payment is due August 1.		
	30	Cash	150	
		Accounts Receivable		150
		Collected amount due from Lost Creek Cemetery		
		for mowing services provided July 25.		
	31	Salaries Expense	80	
		Cash		80
		Paid salary to Teddy Grimm for work performed		
		in July.		

PROBLEM 3.6A
DONEGAN'S LAWN CARE SERVICE (continued)

b.

Cash

Debit		Credit	
Jul 18	1,500	July 23	400
Jul 30	150	July 24	25
		July 31	80
July 31 Bal.	1,145		

Accounts Receivable

Debit		Credit	
July 25	150	July 30	150
July 26	200		
July 31 Bal.	200		

Office Supplies

Debit		Credit	
July 22	100		
July 31 Bal.	100		

Mowing Equipment

Debit		Credit	
July 23	2,000		
July 31 Bal.	2,000		

Accounts Payable

Debit		Credit	
		July 22	100
		July 31 Bal.	100

Notes Payable

Debit		Credit	
		July 23	1,600
		July 31 Bal.	1,600

Capital Stock

Debit		Credit	
		July 18	1,500
		July 31 Bal.	1,500

Retained Earnings

Debit		Credit	
		July 31 Bal.	0

Mowing Revenue

Debit		Credit	
		July 25	150
		July 26	200
		July 31 Bal.	350

Salaries Expense

Debit		Credit	
July 31	80		
July 31 Bal.	80		

Fuel Expense

Debit		Credit	
July 24	25		
July 31 Bal.	25		

PROBLEM 3.6A
DONEGAN'S LAWN CARE SERVICE
(concluded)

c.

DONEGAN'S LAWN CARE SERVICE		
Trial Balance		
July 31, 2009		
Cash	$ 1,145	
Accounts receivable	200	
Office supplies	100	
Mowing Equipment	2,000	
Accounts payable		$ 100
Notes payable		1,600
Capital stock		1,500
Retained earnings		0
Mowing revenue		350
Salaries expense	80	
Fuel expense	25	
	$ 3,550	$ 3,550

d.

Donegan's Retained Earnings balance is zero because the company has been in business for only two weeks and has not yet updated the Retained Earnings account for any revenue or expense activities. The procedure to update the Retained Earnings account is discussed in Chapter 5.

50 Minutes, Strong

PROBLEM 3.7A
SANLUCAS, INC.

a.

General Journal

2009				
June	4	Cash	1,500	
		Notes Payable		1,500
		Borrowed cash from bank by issuing a note payable.		
	9	Cash	1,600	
		Accounts Receivable		1,600
		Collected $1,600 from Nina Lesher on account.		
	10	Inspection Supplies	150	
		Accounts Payable		150
		Purchased inspection supplies on account.		
	17	Accounts Receivable	1,650	
		Inspection Revenue		1,650
		Billed homeowners $1,650 on account.		
	25	Advertising Expense	200	
		Cash		200
		Paid WLIR Radio for ads to be aired June 27.		
	28	Testing Expense	1,300	
		Cash		1,300
		Paid for June testing expenses.		
	30	Salaries Expense	1,100	
		Cash		1,100
		Paid June salaries.		

PROBLEM 3.7A
SANLUCAS, INC. (continued)

b.

Cash

June 1 bal.	5,100	June 25	200
June 4	1,500	June 28	1,300
June 9	1,600	June 30	1,100
June 30 bal.	5,600		

Accounts Receivable

June 1 bal.	2,600	June 9	1,600
June 17	1,650		
June 30 bal.	2,650		

Inspection Supplies

June 1 bal.	800		
June 10	150		
June 30 bal.	950		

Accounts Payable

		June 1 bal.	850
		June 10	150
		June 30 bal.	1,000

Notes Payable

		June 1 bal.	2,000
		June 4	1,500
		June 30 bal.	3,500

Dividends

June 1 bal.	600		
June 30 bal.	600		

Capital Stock

		June 1 bal.	3,000
		June 30 bal.	3,000

Retained Earnings

		June 1 bal.	1,800
		June 30 bal.	1,800

Inspection Revenue

		June 1 bal.	8,350
		June 17	1,650
		June 30 bal.	10,000

Salaries Expense

June 1 bal.	4,900		
June 30	1,100		
June 30 bal.	6,000		

Advertising Expense

June 1 bal.	300		
June 25	200		
June 30 bal.	500		

Testing Expense

June 1 bal.	1,700		
June 28	1,300		
June 30 bal.	3,000		

PROBLEM 3.7A
SANLUCAS, INC. (concluded)

c.

SANLUCAS, INC.		
Trial Balance		
June 30, 2009		
Cash	$ 5,600	
Accounts receivable	2,650	
Inspection supplies	950	
Accounts payable		$ 1,000
Notes payable		3,500
Dividends	600	
Capital stock		3,000
Retained earnings		1,800
Inspection revenue		10,000
Salaries expense	6,000	
Advertising expense	500	
Testing expense	3,000	
	$ 19,300	$ 19,300

d.

The company must have paid all of the dividends it has declared. Otherwise, its trial balance would have reported dividends payable.

10 Minutes, Difficult

PROBLEM 3.8A
HOME TEAM CORPORATION

Error	Net Income	Total Assets	Total Liabilities	Owners' Equity
Recorded the issuance of capital stock by debiting Capital Stock and crediting Service Revenue.	O	U	NE	U
Recorded the declaration and payment of a dividend by debiting Capital Stock and crediting Cash.	NE	NE	NE	NE
Recorded the payment of an account payable by debiting Cash and crediting Rent Expense.	O	O	O	O
Recorded the collection of an outstanding account receivable by debiting Cash and crediting Service Revenue.	O	O	NE	O
Recorded client billings on account by debiting Accounts Receivable and crediting Advertising Expense.	NE	NE	NE	NE
Recorded the cash purchase of land by debiting Supplies Expense and crediting Notes Payable.	U	NE	O	U
Recorded the purchase of a building on account by debiting Cash and crediting Dividends Payable.	NE	NE	NE	NE

SOLUTIONS TO PROBLEMS SET B

30 Minutes, Medium

PROBLEM 3.1B
NORTH ENTERPRISES

a.

General Journal

20__				
Apr.	1	Cash	650,000	
		Capital Stock		650,000
		Issued 10,000 shares of capital stock.		
	6	Land	60,000	
		Office Building	240,000	
		Cash		100,000
		Notes Payable		200,000
		Purchased land and office building.		
	10	Computer Systems	6,000	
		Cash		6,000
		Purchased computer system.		
	12	Office Furnishings	12,000	
		Cash		1,000
		Accounts Payable		11,000
		Purchased office furnishings.		
	20	Office Supplies	750	
		Cash		750
		Purchased office supplies.		
	25	Accounts Receivable	200	
		Computer Systems		200
		Refund due from Comp Central.		
	28	Accounts Payable	5,500	
		Cash		5,500
		Made payment on account payable.		
	29	Cash	200	
		Accounts Receivable		200
		Collected refund from Comp Central.		

PROBLEM 3.1B
NORTH ENTERPRISES (concluded)

b.

Transaction	**Assets**	**=**	**Liabilities**	**+**	**Owners' Equity**
Apr. 1	+ $650,000 (Cash)		$0		+ $650,000 (Capital
Apr. 6	+ $60,000 (Land) + $240,000 (Office Building) – $100,000 (Cash)		+ $200,000 (Notes Payable)		$0
Apr. 10	+ $6,000 (Computer Systems) – $6,000 (Cash)		$0		$0
Apr. 12	+ $12,000 (Office Furnishings) – $1,000 (Cash)		+ $11,000 (Accounts Payable)		$0
Apr. 20	+ $750 (Office Supplies) – $750 (Cash)		$0		$0
Apr. 25	+ $200 (Accounts Receivable) – $200 (Computer Systems)		$0		$0
Apr. 28	– $5,500 (Cash)		- $5,500 (Accounts Payable)		$0
Apr. 29	+ $200 (Cash) – $200 (Accounts Receivable)		$0		$0

30 Minutes, Medium

PROBLEM 3.2B
LYONS, INC.

a. **(1)** **(a)** The asset Accounts Receivable was increased. Increases in assets are recorded by debits. Debit Accounts Receivable, $5,000.

(b) Revenue has been earned. Revenue increases owners' equity. Increases in owners' equity are recorded by credits. Credit Consulting Revenue, $5,000.

(2) **(a)** The asset Office Supplies was increased. Increases in assets are recorded by debits. Debit Office Supplies, $3,200.

(b) The asset Cash was decreased. Decreases in assets are recorded by credits. Credit Cash, $800.

(c) The liability Accounts Payable was increased. Increases in liabilities are recorded by credits. Credit Accounts Payable, $2,400.

(3) **(a)** The liability Accounts Payable was decreased. Decreases in liabilities are recorded by debits. Debit Accounts Payable, $100.

(b) The asset Office Supplies was decreased. Decreases in assets are recorded by credits. Credit Office Supplies, $100.

(4) **(a)** The asset Cash was increased. Increases in assets are recorded by debits. Debit Cash, $5,000.

(b) The owners' equity account Capital Stock was increased. Increases in owners' equity are recorded by credits. Credit Capital Stock, $5,000.

(5) **(a)** The asset Cash was increased. Increases in assets are recorded by debits. Debit Cash, $1,200.

(b) The asset Accounts Receivable was decreased. Decreases in assets are recorded by credits. Credit Accounts Receivable, $1,200.

(6) **(a)** The liability Accounts Payable was decreased. Decreases in liabilities are recorded by debits. Debit Accounts Payable, $2,300 ($2,400 - $100).

(b) The asset Cash was decreased. Decreases in assets are recorded by credits. Credit Cash, $2,300.

(7) **(a)** The Dividends account was increased. Dividends decrease the owners' equity account Retained Earnings. Decreases in owners' equity are recorded by debits. Debit Dividends, $1,800.

(b) The asset Cash was decreased. Decreases in assets are recorded by credits. Credit Cash, $1,800.

PROBLEM 3.2B
LYONS, INC. (continued)

a.

General Journal

20__		(1)		
June	1	Accounts Receivable	5,000	
		Consulting Revenue		5,000
		Billed customers for services rendered.		
		(2)		
	3	Office Supplies	3,200	
		Cash		800
		Accounts Payable		2,400
		Purchased Offfice Supplies.		
		(3)		
	5	Accounts Payable	100	
		Office Supplies		100
		Returned portion of supplies purchased June 3.		
		(4)		
	17	Cash	5,000	
		Capital Stock		5,000
		Issued 1,000 shares of capital stock at $5/share.		
		(5)		
	22	Cash	1,200	
		Accounts Receivable		1,200
		Received partial payment for services billed on		
		June 1.		
		(6)		
	29	Accounts Payable	2,300	
		Cash		2,300
		Paid outstanding balance owed for office supplies		
		purchased on June 3.		
		(7)		
	30	Dividends	1,800	
		Cash		1,800
		Declared and paid a cash dividend.		

PROBLEM 3.2B
LYONS, INC. (concluded)

c. The realization principle requires that revenue be recorded when it is *earned* , even if cash for the goods or services provided has not been received.

d. The matching principle requires that expenses incurred in an accounting period be matched with revenue earned in the same period. Office supplies are recorded as an asset when they are first purchased. As these supplies are used in a particular accounting period, their cost will be matched against the revenue earned in that period.

35 Minutes, Medium

PROBLEM 3.3B
DANA, INC.

a.

	Income Statement			Balance Sheet		
Transaction	Revenue –	Expenses =	Net Income	Assets –	Liabilities =	Owners' Equity
Oct. 1	NE	I	D	D	NE	D
Oct. 4	I	NE	I	I	NE	I
Oct. 8	I	NE	I	I	NE	I
Oct. 12	NE	I	D	NE	I	D
Oct. 20	NE	NE	NE	NE	NE	NE
Oct. 24	I	NE	I	I	NE	I
Oct. 25	NE	NE	NE	D	D	NE
Oct. 29	NE	NE	NE	D	NE	D

PROBLEM 3.3B
DANA, INC. (concluded)

b.

General Journal

Oct.	1	Rent Expense	4,000	
		Cash		4,000
		Paid October rent.		
	4	Accounts Receivable	8,500	
		Service Revenue		8,500
		Billed Milton Hotels for services.		
	8	Cash	4,700	
		Service Revenue		4,700
		Collected cash from Dirt Valley Development for		
		services provided.		
	12	Advertising Expense	320	
		Accounts Payable		320
		Placed ad in the newspaper to be published on		
		October 25. Total amount due in 30 days.		
	20	Cash	8,500	
		Accounts Receivable		8,500
		Received payment from Milton Hotels for services		
		billed on Oct. 4.		
	24	Cash	300	
		Accounts Receivable	3,300	
		Service Revenue		3,600
		Collected partial payment from Dudley Co. and		
		billed remainder.		
	25	Accounts Payable	320	
		Cash		320
		Paid newspaper for advertisement.		
	29	Dividends	2,600	
		Cash		2,600
		Declared and paid a cash dividend.		

c. Three situations in which a cash payment does not involve an expense include: (1) the payment of a cash dividend, (2) the payment of a liability for a previously recorded expense, and (3) the purchase of an asset, including expenses paid in advance such as insurance, rent, and advertising.

50 Minutes, Strong

PROBLEM 3.4B
TONE DELIVERIES

a.

	Income Statement				Balance Sheet				
Transaction	Revenue	–	Expenses	= Net Income	Assets	–	Liabilities	=	Owners' Equity
Mar. 2	NE		NE	NE	I		NE		I
Mar. 4	NE		NE	NE	I		I		NE
Mar. 5	NE		I	D	D		NE		D
Mar. 9	I		NE	I	I		NE		I
Mar. 15	NE		I	D	D		NE		D
Mar. 19	NE		I	D	D		NE		D
Mar. 20	NE		NE	NE	NE		NE		NE
Mar. 28	I		NE	I	I		NE		I
Mar. 30	NE		I	D	D		NE		D
Mar. 30	NE		I	D	NE		I		D
Mar. 30	NE		NE	NE	NE		I		D

PROBLEM 3.4B
TONE DELIVERIES (continued)

b.

General Journal

2009				
Mar.	2	Cash	80,000	
		Capital Stock		80,000
		Issued stock to Mary Tone.		
	4	Truck	45,000	
		Cash		15,000
		Notes Payable		30,000
		Purchased truck.		
	5	Rent Expense	2,500	
		Cash		2,500
		Paid office rent for March.		
	9	Accounts Receivable	11,300	
		Service Revenue		11,300
		Billed customers.		
	15	Salaries Expense	7,100	
		Cash		7,100
		Paid salaries for first half of March.		
	19	Maintenance Expense	900	
		Cash		900
		Paid Bill's Auto for repair services.		
	20	Cash	3,800	
		Accounts Receivable		3,800
		Collected portion of amount billed to customers.		
	28	Accounts Receivable	14,400	
		Service Revenue		14,400
		Billed customers for services rendered through		
		month-end.		
	30	Salaries Expense	7,500	
		Cash		7,500
		Paid salaries through month-end.		
	30	Fuel Expense	830	
		Accounts Payable		830
		Received bill for fuel used during March.		
	30	Dividends	1,200	
		Dividends Payable		1,200
		Declared dividend payable April 30.		

PROBLEM 3.4B
TONE DELIVERIES (continued)

c.

Cash					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	2		80,000		80,000
	4			15,000	65,000
	5			2,500	62,500
	15			7,100	55,400
	19			900	54,500
	20		3,800		58,300
	30			7,500	50,800

Accounts Receivable					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	9		11,300		11,300
	20			3,800	7,500
	28		14,400		21,900

Truck					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	4		45,000		45,000

Notes Payable					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	4			30,000	30,000

Accounts Payable					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	30			830	830

PROBLEM 3.4B
TONE DELIVERIES (continued)

Dividend Payable

Date		Explanation	Debit	Credit	Balance
2009					
Mar.	30			1,200	1,200

Capital Stock

Date		Explanation	Debit	Credit	Balance
2009					
Mar.	2			80,000	80,000

Dividends

Date		Explanation	Debit	Credit	Balance
2009					
Mar.	30		1,200		1,200

Service Revenue

Date		Explanation	Debit	Credit	Balance
2009					
Mar.	9			11,300	11,300
	28			14,400	25,700

Maintenance Expense

Date		Explanation	Debit	Credit	Balance
2009					
Mar.	19		900		900

PROBLEM 3.4B
TONE DELIVERIES (continued)

Fuel Expense					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	30		830		830

Salaries Expense					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	15		7,100		7,100
	30		7,500		14,600

Rent Expense					
Date		Explanation	Debit	Credit	Balance
2009					
Mar.	5		2,500		2,500

PROBLEM 3.4B

d.

TONE DELIVERIES (continued)

TONE DELIVERIES		
Trial Balance		
March 31, 2009		
Cash	$ 50,800	
Accounts receivable	21,900	
Truck	45,000	
Notes payable		$ 30,000
Accounts payable		830
Dividends payable		1,200
Capital stock		80,000
Retained earnings		0
Dividends	1,200	
Service revenue		25,700
Maintenance expense	900	
Fuel expense	830	
Salaries expense	14,600	
Rent expense	2,500	
	$ 137,730	$ 137,730

PROBLEM 3.4B
TONE DELIVERIES (concluded)

e.

Total Assets:		
Cash	$ 50,800	
Accounts Receivable	21,900	
Trucks	45,000	
Total assets		$ 117,700
Total liabilities:		
Notes payable	$ 30,000	
Accounts payable	830	
Dividends payable	1,200	
Total liabilities		$ 32,030
Total stockholders' equity:		
Total assets - total liabilities ($117,700 - $32,030)		$ 85,670

The above figures are most likely not the amounts to be reported in the balance sheet dated March 31. The accounting cycle includes adjustments that must be made to the trial balance prior preparing the financial statements. The adjusting process is covered in Chapter 4.

60 Minutes, Strong

PROBLEM 3.5B
DR. CRAVATI, DMD

a.

	Income Statement					Balance Sheet				
Transaction	Revenue	–	Expenses	=	Net Income	Assets	–	Liabilities	=	Owners' Equity
Aug. 1	NE		NE		NE	I		NE		I
Aug. 4	NE		NE		NE	I		I		NE
Aug. 9	NE		NE		NE	NE		NE		NE
Aug. 16	NE		NE		NE	I		I		NE
Aug. 21	NE		NE		NE	NE		NE		NE
Aug. 24	I		NE		I	I		NE		I
Aug. 27	NE		I		D	NE		I		D
Aug. 28	NE		NE		NE	NE		NE		NE
Aug. 31	NE		I		D	D		NE		D

PROBLEM 3.5B
DR. CRAVATI, DMD (continued)

b.

General Journal

2009				
Aug.	1	Cash	280,000	
		Capital Stock		280,000
		Issued 1,000 shares of capital stock.		
	4	Land	60,000	
		Building	340,000	
		Cash		80,000
		Notes Payable		320,000
		Purchased land and building.		
	9	Medical Instruments	75,000	
		Cash		75,000
		Purchased medical instruments.		
	16	Office Fixtures & Equipment	25,000	
		Cash		10,000
		Accounts Payable		15,000
		Purchased fixtures and equipment.		
	21	Office Supplies	4,200	
		Cash		4,200
		Purchased office supplies.		
	24	Cash	1,000	
		Accounts Receivable	12,000	
		Service Revenue		13,000
		Recorded dental service revenue earned.		
	27	Advertising Expense	450	
		Accounts Payable		450
		Recorded advertising expense incurred in Aug.		
	28	Cash	500	
		Accounts Receivable		500
		Collected cash for Aug. 24 services.		
	31	Salary Expense	2,200	
		Cash		2,200
		Paid Aug. salary expense.		

PROBLEM 3.5B
DR. CRAVATI, DMD (continued)

c.

Cash

Debit		Credit	
Aug. 1	280,000	Aug. 4	80,000
Aug. 24	1,000	Aug. 9	75,000
Aug. 28	500	Aug. 16	10,000
		Aug. 21	4,200
		Aug. 31	2,200
Aug.31 Bal.	110,100		

Notes Payable

Debit		Credit	
		Aug. 4	320,000
		Aug. 31 Bal.	320,000

Accounts Receivable

Debit		Credit	
Aug. 24	12,000	Aug. 28	500
Aug. 31 Bal.	11,500		

Accounts Payable

Debit		Credit	
		Aug. 16	15,000
		Aug. 27	450
		Aug. 31 Bal.	15,450

Office Supplies

Debit		Credit	
Aug. 21	4,200		
Aug. 31 Bal.	4,200		

Capital Stock

Debit		Credit	
		Aug. 1	280,000
		Aug. 31 Bal.	280,000

Medical Instruments

Debit		Credit	
Aug. 9	75,000		
Aug. 31 Bal.	75,000		

Service Revenue

Debit		Credit	
		Aug. 24	13,000
		Aug. 31 Bal.	13,000

Office, Fixtures & Equipment

Debit		Credit	
Aug. 16	25,000		
Aug. 31 Bal.	25,000		

Advertising Expense

Debit		Credit	
Aug. 27	450		
Aug. 31 Bal.	450		

Land

Debit		Credit	
Aug. 4	60,000		
Aug. 31 Bal.	60,000		

Salary Expense

Debit		Credit	
Aug. 31	2,200		
Aug. 31 Bal.	2,200		

Building

Debit		Credit	
Aug. 4	340,000		
Aug. 31 Bal.	340,000		

PROBLEM 3.5B
DR. CRAVATI, DMD (continued)

d.

DR. CRAVATI, DMD		
Trial Balance		
August 31, 2009		
Cash	$ 110,100	
Accounts Receivable	11,500	
Office Supplies	4,200	
Medical instruments	75,000	
Office fixtures & equipment	25,000	
Land	60,000	
Building	340,000	
Notes payable		$ 320,000
Accounts Payable		15,450
Capital stock		280,000
Retained earnings		0
Service revenue		13,000
Advertising expense	450	
Salary expense	2,200	
	$ 628,450	$ 628,450

PROBLEM 3.5B
DR. CRAVATI, DMD (concluded)

e.

Total Assets:		
Cash	$ 110,100	
Accounts receivable	11,500	
Office supplies	4,200	
Medical instruments	75,000	
Office fixtures & equipment	25,000	
Land	60,000	
Building	340,000	
Total assets		$ 625,800
Total liabilities:		
Notes payable	$ 320,000	
Accounts payable	15,450	
Total liabilities		$ 335,450
Total owners (stockholders') equity:		
Total assets - total liabilities ($625,800 - $335,450)		$ 290,350
As shown below, the business was profitable in its first		
month of operations:		
Service revenue		$ 13,000
Less: Advertising expense	$ 450	
Salary expense	2,200	2,650
Net income (profit)		$ 10,350

50 Minutes, Strong

PROBLEM 3.6B
CLOWN AROUND, INC.

a.

General Journal

2009				
Feb.	2	Accounts Payable	750	
		Cash		750
		Paid $750 in partial settlement of outstanding		
		accounts payable.		
	6	Cash	900	
		Accounts Receivable		900
		Collected $900 in full settlement of outstanding		
		accounts receivable.		
	18	Accounts Receivable	175	
		Party Revenue		175
		Billed Sunflower Child Care for clown services.		
		The entire amount is due March 15.		
	26	Cash	480	
		Party Revenue		480
		Billed and collected cash for performing at		
		several birthday parties.		
	28	Salaries Expense	260	
		Cash		260
		Paid clown salaries for work performed in		
		February.		
	28	Travel Expense	40	
		Cash		40
		Paid travel expenses incurred in February.		
	28	Dividends	100	
		Cash		100
		Declared and distributed dividend to Ralph		
		Jaschob.		

PROBLEM 3.6B
CLOWN AROUND, INC. (continued)

b.

Cash

Debit		Credit	
Feb. 1 Bal.	2,850	Feb. 2	750
Feb. 6	900	Feb. 28	260
Feb. 26	480	Feb. 28	40
		Feb. 28	100
Feb. 28 Bal.	3,080		

Accounts Receivable

Debit		Credit	
Feb. 1 Bal.	900	Feb. 6	900
Feb. 18	175		
Feb. 28 Bal.	175		

Accounts Payable

Debit		Credit	
Feb. 2	750	Feb. 1 Bal.	800
		Feb. 28 Bal.	50

Capital Stock

Debit		Credit	
		Feb. 1 Bal.	2,000
		Feb. 28 Bal.	2,000

Retained Earnings

Debit		Credit	
		Feb. 1 Bal.	750
		Feb. 28 Bal.	750

Dividends

Debit		Credit	
Feb. 1 Bal.	0		
Feb. 28	100		
Feb. 28 Bal.	100		

Party Revenue

Debit		Credit	
		Feb. 1 Bal.	1,350
		Feb. 18	175
		Feb. 26	480
		Feb. 28 Bal.	2,005

Salaries Expense

Debit		Credit	
Feb. 1 Bal.	830		
Feb. 28	260		
Feb. 28 Bal.	1,090		

Party Food Expense

Debit		Credit	
Feb. 1 Bal.	240		
Feb. 28 Bal.	240		

Travel Expense

Debit		Credit	
Feb. 1 Bal.	80		
Feb. 28	40		
Feb. 28 Bal.	120		

PROBLEM 3.6B
CLOWN AROUND, INC.
(concluded)

c.

CLOWN AROUND, INC.		
Trial Balance		
February 28, 2009		
Cash	$ 3,080	
Accounts receivable	175	
Accounts payable		$ 50
Capital stock		2,000
Retained earnings		750
Dividends	100	
Party revenue		2,005
Salaries expense	1,090	
Party food expense	240	
Travel expense	120	
	$ 4,805	$ 4,805

d. Dividends are not an expense. Thus, they are not deducted from revenue in the determination of net income reported in the income statement. The reason dividends are not viewed as expenses is that these payments do not serve to generate revenue. Rather, they are a distribution of profits to the owners of the business.

50 Minutes, Strong

PROBLEM 3.7B
AHUNA, INC.

a.

General Journal

2009				
Mar.	3	Cash	1,200	
		Accounts Receivable		1,200
		Collected $1,200 from Kim Mitchell on account.		
	11	Cooking Supplies	700	
		Cash		700
		Purchased cooking supplies with cash.		
	15	Accounts Payable	200	
		Cash		200
		Paid $200 of outstanding account payable.		
	20	Cash	4,000	
		Capital Stock		4,000
		Issued additional shares of capital stock.		
	24	Accounts Receivable	6,200	
		Client Revenue		6,200
		Recorded revenue on account.		
	27	Salaries Expense	900	
		Cash		900
		Recorded March salaries expense.		
	30	Travel Expense	400	
		Cash		400
		Recorded March travel expense.		
	31	Printing Expense	300	
		Accounts Payable		300
		Recorded printing expense on account.		

PROBLEM 3.7B
AHUNA, INC. (continued)

b.

Cash

Mar. 1 bal.	5,700	Mar. 11	700
Mar. 3	1,200	Mar. 15	200
Mar. 20	4,000	Mar. 27	900
		Mar. 30	400
Mar. 31 bal.	8,700		

Accounts Receivable

Mar. 1 bal.	1,800	Mar. 3	1,200
Mar. 24	6,200		
Mar. 31 bal.	6,800		

Cooking Supplies

Mar. 1 bal.	800		
Mar. 11	700		
Mar. 31 bal.	1,500		

Accounts Payable

Mar. 15	200	Mar. 1 bal.	300
		Mar. 31	300
		Mar. 31 bal.	400

Dividends Payable

		Mar. 1 bal.	500
		Mar. 31 bal.	500

Dividends

Mar. 1 bal.	500		
Mar. 31 bal.	500		

Capital Stock

		Mar. 1 bal.	6,000
		Mar. 20	4,000
		Mar. 31 bal.	10,000

Retained Earnings

		Mar. 1 bal.	1,400
		Mar. 31 bal.	1,400

Client Revenue

		Mar. 1 bal.	5,800
		Mar. 24	6,200
		Mar. 31 bal.	12,000

Salaries Expense

Mar. 1 bal.	3,100		
Mar. 27	900		
Mar. 31 bal.	4,000		

Travel Expense

Mar. 1. bal.	1,500		
Mar. 30	400		
Mar. 31 bal.	1,900		

Printing Expense

Mar. 1 bal.	600		
Mar. 31	300		
Mar. 31 bal.	900		

PROBLEM 3.7B
AHUNA, INC. (concluded)

c.

AHUNA, INC.		
Trial Balance		
March 31, 2009		
Cash	$ 8,700	
Accounts receivable	6,800	
Cooking supplies	1,500	
Accounts payable		$ 400
Dividends payable		500
Dividends	500	
Capital stock		10,000
Retained earnings		1,400
Client revenue		12,000
Salaries expense	4,000	
Travel expense	1,900	
Printing expense	900	
	$ 24,300	$ 24,300

d.

The company has not paid the dividends it previously declared as evidenced by the $500 dividends payable liability in the trial balance.

10 Minutes, Difficult

PROBLEM 3.8B
BLIND RIVER, INC.

Error	Net Income	Total Assets	Total Liabilities	Owners' Equity
Recorded the issuance of capital stock by debiting Dividends and crediting Cash.	NE	U	NE	U
Recorded the payment of an account payable by debiting Cash and crediting Accounts Receivable.	NE	O	O	NE
Recorded the collection of an outstanding account receivable by debiting Service Revenue and crediting Cash.	U	U	NE	U
Recorded client billings on account by debiting Accounts Payable and crediting Cash.	U	U	U	U
Recorded the payment of an outstanding dividend payable by debiting Dividends and crediting Cash.	NE	NE	O	U
Recorded the payment of salaries payable by debiting Salaries Expense and crediting Salaries Payable.	U	O	O	U
Recorded the purchase of office supplies on account by debiting Rent Expense and crediting Office Supplies.	U	U	U	U

SOLUTIONS TO CRITICAL THINKING CASES

15 Minutes, Medium

CASE 3.1
REVENUE RECOGNITION

Revenue is realized in the period that services are rendered to customers or goods are delivered to customers. Using this principle as a guide, the three independent situations are analyzed below:

a. *Period of flight.* Airlines earn revenue by rendering a service—transportation—to their customers. Therefore, revenue should be recognized in the accounting period in which this service is rendered. (Selling a ticket does not qualify as "delivering goods" to the customer. The ticket is not a "product"-it is merely a receipt showing that the customer has already made payment for services to be rendered in the future.)

b. *Period furniture sold.* In this case the furniture store delivers goods to its customers and acquires an account receivable at the date of sale. This is the period in which revenue should be recognized, even though the account receivable may not be collected for many months. Collection of an account receivable does not produce revenue; this action merely converts one asset (receivable) into another (cash).

c. *Periods that magazines are mailed to customers.* The "goods" that a magazine publisher delivers to its customers are magazines. Thus, the publisher does not earn its revenue until the magazines are delivered to the customers. (For practical purposes, the act of mailing the magazine may be viewed as "delivery.")

30 Minutes, Strong

CASE 3.2
MEASURING INCOME

a. Discussion of “fairness and reasonableness” of income measurement policies:

(1) Given that most revenue is received in cash and that credit terms are constant, recognizing revenue on a cash basis will cause little distortion in annual results. Thus, it appears “fair and reasonable”—at least for the first two years. But we should consider that in the last (third) year of the agreement, this policy will exclude from net income credit sales in December. Stanley may expect some adjustment for this.

(2) Charging weekly expenditures for business supplies directly to expense is reasonable, but considering the Morris family’s grocery and dry cleaning bills as expenses of the business is neither fair nor reasonable (nor legal).

(3) Morris’s salary of $60,000 is “fair and reasonable” because it has been agreed upon by both parties. But to make additional salary payments of $90,000 per year to Morris family members who worked only on a part-time basis does *not* seem to meet the “fair and reasonable” criteria.

(4) Income taxes on the Morris family’s salaries are *personal* expenses, not expenses of the business. It is neither fair nor reasonable to deduct these taxes in computing the income of the corporation.

(5) It is not reasonable to report the entire $150,000 value of the equipment as an expense in the first-year income statement. This equipment will be used by the company for many years to generate revenue. By assigning the entire cost of the equipment to the first year of operations, Morris has violated the matching principle. In Chapter 4, we will see how the process of depreciation should be used to spread the cost of the printing equipment over its estimated useful life.

b. The state-of-the-art printing equipment valued at $150,000 is an *asset*, not an expense. By reporting the equipment’s entire $150,000 value as an expense in the company’s first-year income statement, the net income computed by Morris was probably significantly lower than the net cash flow generated by the business.

5 Minutes, Easy

CASE 3.3
WHISTLE-BLOWING
ETHICS, FRAUD & CORPORATE GOVERNANCE

It is certainly unethical, and probably illegal, for Ed Grimm's boss to demand that Ed knowingly engage in fraudulent reporting activities in order to retain his job. Ed may have been told that he would be insulated from any responsibility or legal liability, but in reality, this may not be an acceptable defense. In fact, Ed's involvement could result in serious consequences, including criminal prosecution and incarceration. Ed should "blow the whistle" on his boss, even if doing so puts his job in jeopardy. Should the resort's executive management be uncooperative, Ed would be wise to seek legal advice immediately.

15 Minutes, Easy

CASE 3.4
PEPSICO., INC.
BUSINESS WEEK

Financial information of interest would have included, but not have been limited to:

- The value of Groupe Danone's assets.
- Groupe Danone's current amount of outstanding debt that PepsiCo would acquire.
- Groupe Danone's current and expected profitability.
- Groupe Danone's current and expected cash flow.
- The means by which PepsiCo would finance the acquisition (debt versus equity).
- The acquisition's impact on stock price.

Non financial information of interest would have included, but would not have been limited to:

- Groupe Danone's current channels of distribution in domestic and international markets.
- The viability of combining a "junk food" company with a "health food" company.
- The inherent risks associated with PepsiCo becoming overly diversified.
- Consumer trends and the future outlook for yogurt and bottled water products.
- Potential layoffs (especially of Groupe Danone's current management) that result from the acquisition.

10 Minutes, Easy

CASE 3.5
PC CONNECTION
INTERNET

A recent annual report in the Investor and Media section of the company's homepage shows that sales of products to public sector clients has averaged approximately 17% of total sales. Small to medium businesses (SMB) and large businesses are the company's other business segments.