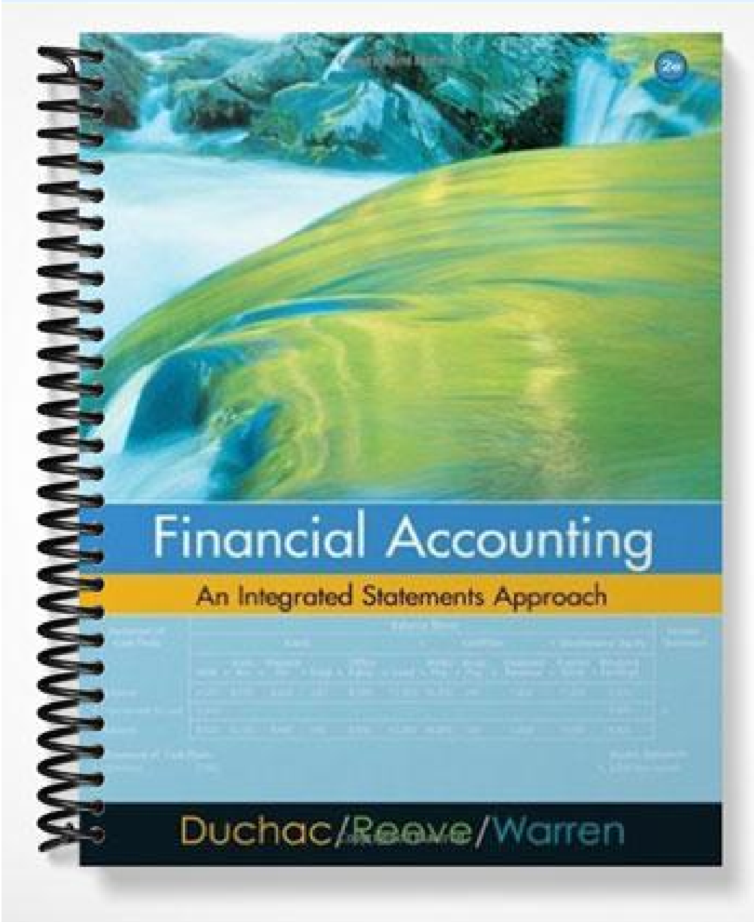
TEST BANK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Financial Accounting
An Integrated Statements Approach
Duchac/Reeve/Warren

Chapter 2— Basic Accounting Concepts

Multiple Choice	Learning Goal(s)	Level of Difficulty	AACSB Tag	AICPA Tag	Multiple Choice	Learning Goal(s)	Level of Difficulty	AACSB Tag	AICPA Tag
1	1	Easy	Communication	Reporting	**37**	2	Moderate	Analytic	Reporting
2	1	Easy	Communication	Reporting	**38**	2	Moderate	Reflective	Reporting
3	1	Moderate	Communication	Reporting	**39**	2	Moderate	Analytic	Reporting
4	1	Easy	Communication	Reporting	**40**	2	Moderate	Reflective	Reporting
5	1	Easy	Reflective	Reporting	**41**	2	Moderate	Reflective	Reporting
6	1	Moderate	Reflective	Reporting	**42**	2	Difficult	Reflective	Reporting
7	1	Moderate	Analytic	Reporting	**43**	2	Difficult	Reflective	Reporting
8	1	Moderate	Analytic	Reporting	**44**	2	Difficult	Reflective	Reporting
9	1	Moderate	Analytic	Reporting	**45**	2	Moderate	Reflective	Reporting
10	1	Moderate	Analytic	Reporting	**46**	3	Easy	Reflective	Reporting
11	2	Moderate	Reflective	Reporting	**47**	2	Easy	Reflective	Reporting
12	2	Moderate	Analytic	Reporting	**48**	3	Moderate	Reflective	Reporting
13	2	Moderate	Reflective	Reporting	**49**	3	Moderate	Reflective	Reporting
14	2	Moderate	Analytic	Reporting	**50**	3	Moderate	Reflective	Reporting
15	2	Moderate	Analytic	Reporting	**51**	3	Moderate	Reflective	Reporting
16	2	Moderate	Reflective	Reporting	**52**	3	Moderate	Reflective	Reporting
17	2	Moderate	Analytic	Reporting	**53**	3	Moderate	Reflective	Reporting
18	2	Moderate	Reflective	Reporting	**54**	3	Moderate	Reflective	Reporting
19	2	Moderate	Reflective	Reporting	**55**	3	Moderate	Analytic	Reporting
20	2	Moderate	Reflective	Reporting	**56**	4	Moderate	Reflective	Reporting
21	2	Moderate	Reflective	Reporting	**57**	5	Difficult	Analytic	Reporting
22	2	Moderate	Reflective	Reporting	**58**	5	Difficult	Analytic	Reporting
23	2	Moderate	Reflective	Reporting	**59**	5	Difficult	Analytic	Reporting
24	2,4	Moderate	Reflective	Reporting	**60**	5	Difficult	Analytic	Reporting
25	2,4	Moderate	Reflective	Reporting	**61**	2	Easy	Reflective	Reporting
26	2,4	Moderate	Reflective	Reporting	**62**	2	Moderate	Reflective	Reporting
27	2,4	Moderate	Reflective	Reporting	**63**	2	Moderate	Reflective	Reporting
28	2	Moderate	Reflective	Reporting	**64**	2	Moderate	Reflective	Reporting
29	2	Moderate	Analytic	Reporting	**65**	2	Moderate	Reflective	Reporting
30	2	Moderate	Analytic	Reporting	**66**	5	Easy	Reflective	Reporting
31	2	Moderate	Analytic	Reporting	**67**	5	Moderate	Analytic	Reporting
32	2	Moderate	Analytic	Reporting	**68**	5	Moderate	Reflective	Reporting
33	2	Moderate	Analytic	Reporting	**69**	5	Moderate	Reflective	Reporting
34	2	Moderate	Analytic	Reporting	**70**	6	Easy	Analytic	Risk
35	2	Moderate	Analytic	Reporting	**71**	6	Easy	Analytic	Reporting
36	2	Moderate	Reflective	Reporting	**72**	6	Moderate	Analytic	Risk

True/ False	Learning Goal(s)	Level of Difficulty	AACSB Tag	AICPA Tag
1	1	Moderate	Reflective	Reporting
2	1	Moderate	Analytic	Reporting
3	1	Moderate	Analytic	Reporting
4	1	Moderate	Analytic	Reporting
5	1	Moderate	Reflective	Reporting
6	1	Moderate	Analytic	Reporting
7	1	Moderate	Analytic	Reporting
8	1	Moderate	Reflective	Reporting
9	1	Moderate	Analytic	Reporting
10	1	Moderate	Analytic	Reporting
11	2	Moderate	Analytic	Reporting
12	2	Moderate	Reflective	Reporting
13	2	Moderate	Reflective	Reporting
14	2	Moderate	Reflective	Reporting
15	2	Moderate	Reflective	Reporting
16	2	Moderate	Reflective	Reporting
17	2	Moderate	Reflective	Reporting
18	2	Moderate	Reflective	Reporting
19	2	Moderate	Reflective	Reporting
20	2	Moderate	Reflective	Reporting
21	2	Moderate	Reflective	Reporting
22	2	Moderate	Reflective	Reporting
23	2	Moderate	Reflective	Reporting
24	2	Moderate	Reflective	Reporting
25	3	Moderate	Reflective	Reporting
26	3	Moderate	Reflective	Reporting
27	3	Moderate	Reflective	Reporting
28	3	Moderate	Reflective	Reporting
29	3	Moderate	Reflective	Reporting
30	3	Moderate	Reflective	Reporting
31	3	Moderate	Reflective	Reporting
32	3	Moderate	Reflective	Reporting
33	4	Moderate	Reflective	Reporting
34	5	Moderate	Reflective	Reporting
35	5	Moderate	Reflective	Reporting
36	6	Moderate	Analytic	Reporting
37	6	Moderate	Analytic	Reporting

Essay	Learning Goal(s)	Level of Difficulty	AACSB Tag	AICPA Tag
1	1	Moderate	Reflective	Reporting
2	1	Difficult	Reflective	Reporting
3	1	Moderate	Reflective	Reporting
4	2,3,5	Moderate	Reflective	Reporting
5	2,3,4,5	Difficult	Reflective	Reporting
6	2,3,4,5	Difficult	Reflective	Reporting
7	2,3,4,5	Difficult	Reflective	Reporting
8	6	Moderate	Reflective	Risk

Problem (s)	Learning Goal(s)	Level of Difficulty	AACSB Tag	AICPA Tag
1	1	Moderate	Analytic	Reporting
2	1	Difficult	Analytic	Reporting
3	1,2,3,4	Difficult	Analytic	Reporting
4	3,5	Difficult	Analytic	Reporting
5	3,5	Difficult	Analytic	Reporting
6	1,2,3,4,5	Difficult	Analytic	Reporting
7	1,2,3,4,5	Difficult	Analytic	Reporting
8	2,4	Moderate	Analytic	Reporting
9	2,3,4,5	Difficult	Analytic	Reporting

Case	Learning Goal(s)	Level of Difficulty	AACSB Tag	AICPA Tag
1	6	Difficult	Analytic	Risk
2	6	Difficult	Analytic	Risk
3	3,4,5	Difficult	Reflective	Reporting
4	2,3,4,5	Difficult	Reflective	Reporting

Difficulty Ratings Guide:	
Easy	Taken nearly verbatim from the text
Moderate	Using different expression or application of concept
Difficult	Several reasoning steps

MULTIPLE CHOICE

1. The basic financial statements do NOT include __________.
   a. Income statement
   b. Tax return
   c. Balance Sheet
   d. Statement of cash flows

   ANS: B DIF: Easy REF: p. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Communication

2. Which of the following is NOT an element of the financial accounting system?
   a. A set of rules for determining the recording of economic events
   b. A framework for preparing financial statements
   c. A set of rules for the stock exchange
   d. Controls to determine whether errors occur during recording

   ANS: C DIF: Easy REF: p. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Communication

3. The set of rules for determining the recording of economic events are generally referred to as
   a. the financial accounting rule book
   b. generally accepted accounting principles
   c. the accounting equation
   d. accounting controls

   ANS: B DIF: Moderate REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Communication

4. A __________ is an economic event that under generally accepted accounting principles affects an element of the financial statements and must be recorded.
   a. Framework
   b. Controls
   c. Set of rules
   d. Transaction

   ANS: D DIF: Easy REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Communication

5. The statement of cash flows is integrated with the balance sheet because
   a. the cash at the beginning of the period plus or minus the cash flows from operating, investing and financing activities equals the end of period cash reported on the balance sheet
   b. the cash at the beginning of the period plus or minus the net income equals the end of period cash reported on the balance sheet
   c. the cash at the beginning of the period plus or minus assets and liabilities equals the end of period cash reported on the balance sheet
   d. the cash at the beginning of the period plus or minus the cash flows from operating, activities equals the end of period cash reported on the balance sheet

   ANS: A DIF: Easy REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Reflective

6. Which of the following transactions changes the mix of assets only?
   a. Paid for supplies with cash
   b. Borrowed money from Second National Bank
   c. Received money for fees earned
   d. Received a utility bill

   ANS: A DIF: Moderate REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Analytic

7. Better Belly, Inc. had the following assets and liabilities as of September 30, 2003.

Assets	$54,433
Liabilities	$28,416

   What is the stockholders' equity of Better Belly as of September 30, 2003?
   a. $0
   b. $26,017
   c. $82,849
   d. cannot be determined with this information

   ANS: B
   $54,433 - $28,416 = $26,017

   DIF: Moderate REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
   MSC: AACSB Analytic

8. Better Belly, Inc. had the following assets and liabilities as of September 30, 2003.

Assets	$54,433
Liabilities	$28,416

   If assets increased by $3,914 and equity increased by $2,290, what is the increase or decrease in liabilities of Better Belly as of September 30, 2003?
   a. ($1,624)
   b. $1,624
   c. $6,204
   d. ($6,204)

   ANS: B
   $3,914 - $2,290 = $1,624

   DIF: Moderate REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
   MSC: AACSB Analytic

9. Better Belly, Inc. had the following assets and liabilities as of September 30, 2006.

Assets	$54,433
Liabilities	$28,416

If assets increased by $3,914 and equity increased by $2,290 during the year, what is the accounting equation of Better Belly as of September 30, 2007?
a. ($1,624)
b. $1,624
c. $6,204
d. ($6,204)

ANS: B
($54,433 + $3,914) = ($28,416 + $1,624) + ($54,433 - $28,416 + $2,290)
$58,347 = $30,040 + $28,307

DIF: Moderate REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
MSC: AACSB Analytic

10. If Assets have a balance of $50,000, and Stockholders' Equity has a balance of $40,000, then Liabilities must have a balance of __________.
a. $90,000
b. $20,000
c. $40,000
d. $10,000

ANS: D DIF: Moderate REF: P. 54 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

11. An increase in Stockholders' Equity from revenues earned will result in an increase also in __________.
a. Liabilities
b. Assets
c. Stockholders' equity
d. No financial statement element

ANS: B DIF: Moderate REF: P. 54 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

12. If Liabilities have a balance of $10,000 and Stockholders' Equity has a balance of $70,000, then Assets must have a balance of __________.
a. $80,000
b. $60,000
c. $70,000
d. $10,000

ANS: A DIF: Moderate REF: P. 54 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

13. One built in control that transactions are analyzed, recorded, and summarized correctly is the accounting equation must
    a. never change its values.
    b. be independent of the statement of cash flows.
    c. remain in balance.
    d. always add up to one.

ANS: C DIF: Moderate REF: p. 55,56 OBJ: 1
TOP: AICPA FN Reporting MSC: AACSB Reflective

14. The payment of $10,000 for expenses was recorded by Spears Co. as an increase in cash of $10,000, and a decrease in retained earnings of $10,000. What is the effect of this error on the accounting equation?
    a. Total assets will exceed total liabilities and stockholders' equity by $20,000
    b. Total assets will exceed total liabilities and stockholders' equity by $10,000
    c. Total assets will be less than total liabilities and stockholders' equity by $20,000
    d. The error will not affect the accounting equation.

ANS: A DIF: Moderate REF: P. 56 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

15. If a $20,000 purchase of equipment for cash is incorrectly recorded as an increase to equipment and as an increase to cash, at the end of the period, assets will __________.
    a. Exceed liabilities and stockholders' equity by $10,000
    b. Equal liabilities and stockholders' equity
    c. Exceed liabilities and stockholders' equity by $20,000
    d. Exceed liabilities and stockholders' equity by $40,000

ANS: D DIF: Moderate REF: P. 56 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

16. XYZ Company deposited $15,000 in a bank account in return for issuing shares in the corporation. This transaction would affect which two financial statement elements?
    a. Assets and stockholders' equity
    b. Assets and liabilities
    c. Liabilities and stockholders' equity
    d. None of the above

ANS: A DIF: Moderate REF: P. 56 OBJ: 2
TOP: AICPA - FN Reporting MSC: AACSB Reflective

17. A to Z Corporation engaged in the following transaction "Issue shares of stock for $5,000 ." On the Statement of Cash Flows, the transaction would be classified as __________.
    a. Cash Flows from Operating Activities.
    b. Cash Flows from Investing Activities.
    c. Cash Flows from Financing Activities.

ANS: C DIF: Moderate REF: P. 57 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Analytic

18. For EFG Co., the transaction "Borrowing cash from the bank on a note" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: A DIF: Moderate REF: P. 57 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

19. For EFG Co., the transaction "Purchase of capital stock in a new start-up business with cash" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: A DIF: Moderate REF: P. 57 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

20. For EFG Co., the transaction "Purchase of land with cash" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: C DIF: Moderate REF: P. 58,59 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

21. For EFG Co., the transaction "Cash sales to customers" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: A DIF: Moderate REF: P. 59 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

22. For EFG Co., the transaction "Payment of dividends" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: B DIF: Moderate REF: P. 59,60 OBJ: 2
    TOP: AICPA FN - Reporitng MSC: AACSB Reflective

23. For EFG Co., the transaction "Payment of expenses with cash" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: B DIF: Moderate REF: P. 59,60 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

24. For EFG Co., the transaction "Purchase of store equipment for cash" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: C DIF: Moderate REF: P.56-66 OBJ: 2,4
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

25. For EFG Co., the transaction "Payment of quarterly taxes" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: B DIF: Moderate REF: P. 56-66 OBJ: 2,4
    TOP: AICPA FN Reporting MSC: AACSB Reflective

26. For EFG Co., the transaction "Receipt of interest income" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: A DIF: Moderate REF: P. 56-66 OBJ: 2,4
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

27. For EFG Co., the transaction "Payment of store rent" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: B DIF: Moderate REF: P. 56-66 OBJ: 2,4
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

28. For EFG Co., the transaction "Received dividend income" would __________.
    a. Increase the assets
    b. Decrease the assets
    c. Have no effect on the assets

    ANS: A DIF: Moderate REF: P. 56-66 OBJ: 2,4
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

29. A to Z Corporation engaged in the following transaction "Issued a $30,000 note payable to borrow cash from the bank." On the Statement of Cash Flows, the transaction would be classified as __________.
    a. Cash Flows from Operating Activities.
    b. Cash Flows from Investing Activities.
    c. Cash Flows from Financing Activities.

    ANS: C DIF: Moderate REF: P. 57 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

30. Blue Spas Inc. borrows $25,000 cash from the bank on a note. The net affect on assets is __________.
    a. $25,000 increase
    b. $0
    c. $25,000 decrease
    d. $12,500 increase

    ANS: A DIF: Moderate REF: P. 57 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

31. Allen Rebozo creates a new accounting firm, Tax Tips Inc. by giving $30,000 cash for capital stock. The net affect on assets is __________.
    a. $30,000 increase
    b. $0
    c. $30,000 decrease
    d. $15,000 increase

    ANS: A DIF: Moderate REF: P. 57 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

32. A to Z Corporation engaged in the following transaction "Purchased land for $80,000 cash." On the Statement of Cash Flows, the transaction would be classified as __________.
    a. Cash Flows from Operating Activities.
    b. Cash Flows from Investing Activities.
    c. Cash Flows from Financing Activities.

    ANS: B DIF: Moderate REF: P. 58 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

33. Martha Stewart, Inc. buys land for $50,000 cash. The net affect on assets is __________.
    a. $50,000 increase
    b. $0
    c. $50,000 decrease
    d. $25,000 increase

    ANS: B DIF: Moderate REF: P. 58 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

34. A to Z Corporation engaged in the following transaction "Paid $1,000 of expenses." On the Statement of Cash Flows, the transaction would be classified as __________.
    a. Cash Flows from Operating Activities.
    b. Cash Flows from Investing Activities.
    c. Cash Flows from Financing Activities.

    ANS: A DIF: Moderate REF: P. 59 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

35. A to Z Corporation engaged in the following transaction "Earned patient fees of $5,000 ." On the Statement of Cash Flows, the transaction would be classified as __________.
    a. Cash Flows from Operating Activities.
    b. Cash Flows from Investing Activities.
    c. Cash Flows from Financing Activities.

    ANS: A DIF: Moderate REF: P. 59 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

36. CXN Company earns revenues and as a result collects cash. Which of the following financial statement elements are increased?
    a. Cash only
    b. Stockholders' equity only
    c. Liabilities
    d. Cash and stockholders' equity

    ANS: D DIF: Moderate REF: P. 59 OBJ: 2
    TOP: AICPA FN Reporting MSC: AACSB Reflective

37. YUT Company paid a utility bill of $500 and paid rent of $700 in December. By how much would these events reduce stockholders' equity?
   a. $1,200
   b. $500
   c. $850
   d. $700

   ANS: A   DIF: Moderate   REF: P. 59,60   OBJ: 2
   TOP: AICPA FN Reporting   MSC: AACSB Analytic

38. Dividends paid would be an
   a. operating activity
   b. investing activity
   c. financing activity
   d. not be on the statement of cash flows

   ANS: C   DIF: Moderate   REF: P. 59,60   OBJ: 2
   TOP: AICPA - FN - Reporting   MSC: AACSB Reflective

39. A to Z Corporation engaged in the following transaction "Paid a $10,000 cash dividend." On the Statement of Cash Flows, the transaction would be classified as ___________.
   a. Cash Flows from Operating Activities.
   b. Cash Flows from Investing Activities.
   c. Cash Flows from Financing Activities.

   ANS: C   DIF: Moderate   REF: P. 60   OBJ: 2
   TOP: AICPA FN - Reporting   MSC: AACSB Analytic

40. Every cash transaction .
   a. Increases or decreases the asset cash.
   b. Increases or decreases an operating, investing,or financing activity on the statement of cash flow.
   c. Always affects at least one balance sheet account and the statement of cash flows.
   d. A, b, and c are all correct.

   ANS: D   DIF: Moderate   REF: P. 61   OBJ: 2
   TOP: AICPA FN - Reporting   MSC: AACSB Reflective

41. The income statement is linked to the balance sheet through the __________ account. .
   a. Accounts payable account
   b. Capital stock account
   c. Cash account
   d. Retained earnings account

   ANS: D   DIF: Moderate   REF: P. 61   OBJ: 2
   TOP: AICPA FN - Reporting   MSC: AACSB Reflective

42. Which of the following would result in the accounting equation to be in balance but would still be incorrect?
   a. The purchase of land for cash, with the land recorded in the equipment account
   b. The purchase of land for cash with the land not recorded
   c. Cash collected for fees earned
   d. Equipment purchased for cash with the equipment recorded as an asset

   ANS: A   DIF: Difficult   REF: P. 61   OBJ: 2
   TOP: AICPA FN - Reporting   MSC: AACSB Reflective

43. Which of the following would result in no net change of assets?
    a. Stock issued for cash
    b. Expenses paid with cash
    c. Cash collected for fees earned
    d. Land purchased for cash

    ANS: D DIF: Difficult REF: P. 61 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

44. Which of the following would decrease stockholders' equity?
    a. Stock issued for cash
    b. Expenses paid with cash
    c. Repayment of notes payable
    d. Land purchased for cash

    ANS: B DIF: Difficult REF: P. 61,62 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

45. Which of the following are true?
    a. The effect of every transaction is an increase or a decrease in one or more the accounting equation elements
    b. The two sides of the accounting equation are always equal
    c. Stockholders' equity is increased by amounts invested by stockholders
    d. All are true

    ANS: D DIF: Moderate REF: P. 61,62 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

46. _____________ are accounting reports that provide summarized information of the transactions of a company.
    a. accounting equation
    b. economic events
    c. financial statements
    d. transactions

    ANS: C DIF: Easy REF: P. 62 OBJ: 3
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

47. A business increases stockholders' equity by __________.
    a. Earning revenues in excess of expenses
    b. Paying dividends
    c. Buying more assets
    d. Having more expenses than revenues

    ANS: A DIF: Easy REF: P. 62 OBJ: 2
    TOP: AICPA FN - Reporting MSC: AACSB Reflective

48. The order in which the financial statements are normally prepared would be.
    a. balance sheet, cash flows, income statement, retained earnings
    b. income statement, retained earnings, balance sheet, cash flows
    c. cash flows, balance sheet, income statement, retained earnings
    d. balance sheet, income statement, retained earnings, cash flows

    ANS: B DIF: Moderate REF: P. 64 OBJ: 3
    TOP: AICPA - FN - Reporting MSC: AACSB Reflective

49. The order in which expenses are listed on the income statement is determined by
    a. size with the largest expense listed first.
    b. size with the smallest expense listed first.
    c. alphabetical order starting with the a’s and moving down the alphabet.
    d. alphabetical order starting with the z’s and moving up the alphabet.

    ANS: A DIF: Moderate REF: P. 64 OBJ: 3
    TOP: AICPA - FN - Reporting MSC: AACSB Reflective

50. The effect of net income will be to
    a. increase operating activities in the statement of cash flows
    b. increase cash and stockholders’ equity
    c. increase retained earnings and stockholders’ equity
    d. increase cash and operating activities in the statement of cash flows

    ANS: C DIF: Moderate REF: P. 64 OBJ: 3
    TOP: AICPA - FN - Reporting MSC: AACSB Reflective

51. The company has been in operation for only one month and during the month the revenues were $15,642 and operating expenses were $9,425. If the ending balance in retained earnings is $2,717, then the amount of dividends paid was
    a. $3,500
    b. $6,217
    c. $8,934
    d. cannot be determined with the information given

    ANS: A
    $15,642 - $9,425 = $6,217 = net income
    $6,217 - $2,717 = $3,500 = dividends

    DIF: Moderate REF: P. 64 OBJ: 3 TOP: AICPA - FN - Reporting
    MSC: AACSB Reflective

52. The order in which liabilities on the balance sheet should be listed would be
    a. the order that they will be paid in cash
    b. alphabetical order
    c. the size of the liability with the smallest first
    d. the size of the liability with the largest first

    ANS: A DIF: Moderate REF: P. 65 OBJ: 3
    TOP: AICPA - FN - Reporting MSC: AACSB Reflective

53. Which of the following liabilities should be listed first on the balance sheet?
    Accounts payable due in one month $2,000
    Note due within 5 days $1,000
    Note payable due in 6 months $4,000
    a. Accounts payable
    b. Note due in 5 days
    c. Note payable due in 6 months
    d. any order

    ANS: B DIF: Moderate REF: P. 65 OBJ: 3
    TOP: AICPA - FN - Reporting MSC: AACSB Reflective

54. The first month of operation showed the net cash from operating activities to be $3760, the net cash from investing activities to be ($5415), and the ending cash balance to be $2,425. The net cash from financing activities must be
   a. $770
   b. $4,080
   c. ($11,600)
   d. $11,600

   ANS: B
   $3,760 + ($5,415) + financing activity = $2,425
   financing activity = $4,080

   DIF: Moderate REF: P. 65 OBJ: 3 TOP: AICPA - FN - Reporting
   MSC: AACSB Reflective

55. The income statement for August indicates net income of $50,000. The corporation also paid $10,000 in dividends during the same period. If there was no beginning balance in stockholders' equity, what is the ending balance in stockholders' equity?
   a. $40,000
   b. $50,000
   c. $10,000
   d. $60,000

   ANS: A DIF: Moderate REF: P. 63-65 OBJ: 3
   TOP: AICPA FN - Reporting MSC: AACSB Analytic

56. The balance sheet reports the _________ of the entity’s assets, liabilities, and stockholders’ equity.
   a. accounting period total
   b. cumulative total
   c. transaction total

   ANS: B DIF: Moderate REF: P. 66 OBJ: 4
   TOP: AICPA - FN - Reporting MSC: AACSB Reflective

Exhibit 2-1

	Total Assets	**Total Liabilities**
Beginning of the year	$100,000	$ 50,000
End of the year	$500,000	$350,000

57. Refer to Exhibit 2-1. What is net income assuming no stock was issued, and no dividends were paid?
   a. $100,000
   b. $300,000
   c. $150,000
   d. $50,000

   ANS: A DIF: Difficult REF: P. 66-69 OBJ: 5
   TOP: AICPA FN - Reporting MSC: AACSB Analytic

58. Refer to Exhibit 2-1. What is net income assuming no stock was issued, and dividends of $25,000 were paid?
a. $10,000
b. $60,000
c. $125,000
d. $300,000

ANS: C DIF: Difficult REF: P. 66-69 OBJ: 5
TOP: AICPA FN - Reporting MSC: AACSB Analytic

59. Refer to Exhibit 2-1. What is net income assuming $50,000 of stock was issued, and no dividends were paid?
a. $100,000
b. $50,000
c. $70,000
d. $10,000

ANS: B DIF: Difficult REF: P. 66-69 OBJ: 5
TOP: AICPA FN - Reporting MSC: AACSB Analytic

60. Refer to Exhibit 2-1. What is net income assuming $50,000 of stock was issued, and $25,000 of dividends were paid?
a. $75,000
b. $50,000
c. $70,000
d. $10,000

ANS: A DIF: Difficult REF: P. 66-69 OBJ: 5
TOP: AICPA FN - Reporting MSC: AACSB Analytic

61. Declaring and paying cash dividends affects which balance sheet accounts?
a. Cash only
b. Stockholders' equity only
c. Cash and stockholders' equity
d. Cash and capital stock

ANS: C DIF: Easy REF: P. 60 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

62. Buying land for cash affects which balance sheet accounts?
a. Cash only
b. Stockholders' equity only
c. Cash and stockholders' equity
d. Cash and land

ANS: D DIF: Moderate REF: P. 58,59 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

63. Receiving cash for fees earned affects which balance sheet accounts?
a. Cash only
b. Stockholders' equity only
c. Cash and stockholders' equity
d. Cash and capital stock

ANS: C DIF: Moderate REF: P. 59 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

64. At the end of the period, ABC Co. pays dividends. The effect of this transaction is to __________.
 a. Decrease retained earnings and capital stock
 b. Decrease cash and retained earnings
 c. Decrease cash only
 d. Decrease retained earnings only

 ANS: B DIF: Moderate REF: P. 59,60 OBJ: 2
 TOP: AICPA FN - Reporting MSC: AACSB Reflective

65. Paying expenses affects which financial statement elements?
 a. Cash only
 b. Stockholders' equity only
 c. Cash and stockholders' equity
 d. Cash and capital stock

 ANS: C DIF: Moderate REF: P. 59,60 OBJ: 2
 TOP: AICPA FN - Reporting MSC: AACSB Reflective

66. When revenues for a period exceed the expenses used to earn the revenues, the financial condition of the business __________.
 a. May improve in the future
 b. Has remained unchanged
 c. Has declined
 d. Has improved

 ANS: D DIF: Easy REF: P. 67 OBJ: 5
 TOP: AICPA FN - Reporting MSC: AACSB Reflective

67. Young Company has $16,000 in Retained Earnings, $27,000 in Assets, and $5,000 in Liabilities. How much is in Common Stock?
 a. $36,000.
 b. $15,000.
 c. $5,000.
 d. $6,000.

 ANS: D DIF: Moderate REF: P. 66-69 OBJ: 5
 TOP: AICPA FN - Reporting MSC: AACSB Analytic

68. The payment of a liability __________.
 a. Decreases assets and stockholders' equity
 b. Increases assets and decreases liabilities
 c. Decreases assets and increase liabilities
 d. Decreases assets and decreases liabilities

 ANS: D DIF: Moderate REF: P. 66-69 OBJ: 5
 TOP: AICPA FN - Reporting MSC: AACSB Reflective

69. Which of the following transactions results in an increase in revenues?
 a. Sale of land for cash equal to the land's historical cost
 b. Sale of merchandise inventory for cash
 c. Receipt of cash from the sale of stock
 d. Receipt of cash from a bank loan

 ANS: B DIF: Moderate REF: P. 66-69 OBJ: 5
 TOP: AICPA FN - Reporting MSC: AACSB Reflective

70. Analyzing comparative financial statements by computing percentages of each item is called __________.
    a. The income statement
    b. Horizontal analysis
    c. Percentage basis accounting
    d. Vertical analysis

    ANS: D DIF: Easy REF: P. 69 OBJ: 6
    TOP: AICPA FN - Risk MSC: AACSB Analytic

71. ___________ computes the percentages of each item within a statement to a total within the statement.
    a. Vertical analysis
    b. Horizontal analysis
    c. Accounting equation
    d. Balance sheet analysis

    ANS: A DIF: Easy REF: P. 69 OBJ: 6
    TOP: AICPA FN - Reporting MSC: AACSB Analytic

72. Which type of analysis might indicate whether the cost of sales had increase as a percentage of sales from one year to another?
    a. Horizontal analysis
    b. Vertical analysis
    c. Accounting equation
    d. Balance sheet analysis

    ANS: B DIF: Moderate REF: P. 70 OBJ: 6
    TOP: AACSB FN - Risk MSC: AACSB Analytic

TRUE/FALSE

1. The basic elements of a financial accounting system include a framework for preparing financial statements.

   ANS: T DIF: Moderate REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Reflective

2. The accounting equation is expressed as follows: Assets = Liabilities - Stockholders' Equity

   ANS: F DIF: Moderate REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Analytic

3. Any given transaction must affect all three parts of the accounting equation.

   ANS: F DIF: Moderate REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Analytic

4. The accounting equation can be expressed: Assets - Liabilities = Stockholders' Equity

   ANS: T DIF: Moderate REF: P. 54 OBJ: 1
   TOP: AICPA FN - Reporting MSC: AACSB Analytic

5. The two sides of the accounting equation do NOT have to be equal.

ANS: F DIF: Moderate REF: P. 54 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Reflective

6. The effect of every transaction is an increase or a decrease in one or more of the accounting equation elements.

ANS: T DIF: Moderate REF: P. 54 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

7. A transaction can affect at most two elements of the accounting equation.

ANS: F DIF: Moderate REF: P. 54 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

8. A company may show a positive net income but be headed for bankruptcy.

ANS: T DIF: Moderate REF: P. 55 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Reflective

9. A business receives $10,000 cash for a sale of merchandise, and records this receipt of cash as an increase in equipment by mistake. The accounting equation is still in balance.

ANS: T DIF: Moderate REF: P. 56 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

10. It is possible for a transaction to change the makeup of assets, but to NOT affect assets in total.

ANS: T DIF: Moderate REF: P. 56 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

11. Equality of the accounting equation means that no errors have occurred.

ANS: F DIF: Moderate REF: P. 56 OBJ: 1
TOP: AICPA FN - Reporting MSC: AACSB Analytic

12. When capital stock is issued by a corporation for cash, both the income statement and the balance sheet are affected.

ANS: F DIF: Moderate REF: P. 57 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

13. Borrowing money from the bank will increase liabilities.

ANS: T DIF: Moderate REF: P. 57,58 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

14. Purchasing land for cash will have no effect on stockholders' equity.

ANS: T DIF: Moderate REF: P. 58 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

15. Fees earned and paid in cash will increase operating activity cash flows as well as retained earnings..

ANS: T DIF: Moderate REF: P. 59 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

16. Miscellaneous expenses are expenses that have an undetermined amount to be paid.

ANS: F DIF: Moderate REF: P. 59 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

17. Dividends are distributions of business earnings to stockholders.

ANS: T DIF: Moderate REF: P. 59 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

18. The payment of utilities expense in cash would affect the operating activities in the statement of cash flows and the income statement but not the balance sheet.

ANS: F DIF: Moderate REF: P. 59,60 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

19. The payment of a cash dividend increases total assets.

ANS: F DIF: Moderate REF: P. 59,60 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

20. International accounting standards require the same four financial statements that are required under U.S. GAAP.

ANS: T DIF: Moderate REF: P. 61 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

21. International accounting standards require two years of historical information be provided while three years are required under U.S. GAAP.

ANS: F DIF: Moderate REF: P. 61 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

22. Revenues increase stockholders' equity.

ANS: T DIF: Moderate REF: P. 62 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

23. Stockholders' equity is decreased by stockholders' investments.

ANS: F DIF: Moderate REF: P. 62 OBJ: 2
TOP: AICPA FN - Reporting MSC: AACSB Reflective

24. Normally, the first financial statement to be prepared is the cash flows statement

ANS: F DIF: Moderate REF: P. 64 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

25. Normally, the last financial statement to be prepared is the statement of retained earnings.

ANS: F DIF: Moderate REF: P. 64 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

26. The income statement is prepared before the balance sheet.

ANS: T DIF: Moderate REF: P. 64 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

27. The statement of retained earnings must be prepared before the balance sheet.

ANS: T DIF: Moderate REF: P. 64 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

28. Normally expenses are reported under the heading “Miscellaneous Expenses”.

ANS: F DIF: Moderate REF: P. 64 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

29. The beginning balance of the retained earnings is zero when a company is beginning operations.

ANS: T DIF: Moderate REF: P. 64 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

30. Accounts payable is always listed first under the liabilities section of the balance sheet.

ANS: F DIF: Moderate REF: P. 65 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

31. The statement of cash flows lists the net cash from operating activities, net cash from research activities and net cash from financing activities to determine the net change in cash.

ANS: F DIF: Moderate REF: P. 65 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

32. The cash flows from operating activities and net income are related and are not normally equal..

ANS: T DIF: Moderate REF: P. 65 OBJ: 3
TOP: AICPA FN - Reporting MSC: AACSB Reflective

33. The ending balances of the accounts from one accounting period become the beginning balances of the next period.

ANS: T DIF: Moderate REF: P. 66 OBJ: 4
TOP: AICPA FN - Reporting MSC: AACSB Reflective

34. An increase in net income suggests that a company’s operations are profitable and that the company is growing.

ANS: F DIF: Moderate REF: P. 67 OBJ: 5
TOP: AICPA FN - Reporting MSC: AACSB Reflective

35. By keeping a running total of the effects of transactions, the accounting equation provides a framework for summarizing the effects of a series of transactions.

ANS: T DIF: Moderate REF: P. 67,68 OBJ: 5
TOP: AICPA FN - Reporting MSC: AACSB Reflective

36. In vertical analysis, each item on the income statement is shown a s a percentage of total assets..

ANS: F DIF: Moderate REF: P. 69 OBJ: 6
TOP: AICPA FN - Reporting MSC: AACSB Analytic

37. Horizontal analysis shows the percentage of each item within a statement to a total in the statement.

ANS: F DIF: Moderate REF: P. 69 OBJ: 6
TOP: AICPA FN - Reporting MSC: AACSB Analytic

ESSAY

1. What are the basic elements of a financial accounting system?

ANS:
A financial accounting system is designed to produce financial statements. The basic elements of a financial accounting system include:

(1) A set of rules for determining what, when, and the amount that should be recorded for economic events
(2) A framework for preparing financial statements
(3) One or more controls to determine whether errors may have arisen in the recording process.

DIF: Moderate REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
MSC: AACSB Reflective

2. The accounting equation "Assets = Liabilities + Stockholders' Equity" is affected by transactions. Is it possible to have a transaction that only impacts one financial element of the equation? Two elements? Give examples.

ANS:
Yes to both questions. Examples include: (1) increase cash and decrease equipment; (2) increase cash and increase stockholders' equity.

DIF: Difficult REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
MSC: AACSB Reflective

3. What are the three built in controls that transactions have been analyzed, reported and summarized correctly?

   ANS:
   A financial accounting system is designed to produce financial statements. The basic elements of a financial accounting system include:

   (1) The accounting equation must be in balance.
   (2) The ending balance in cash in the statement of cash flows is the same as the cash shown under assets on the balance sheet.
   (3) The net income on the income statement must be the same as the net effects of revenues and expenses under retained earnings.

   DIF: Moderate REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
   MSC: AACSB Reflective

4. Explain how the four financial statements are linked.

   ANS:
   A financial accounting system is designed to produce 4 financial statements. The income statement, statement of retained earnings, and statement of cash flows are linked to an element of the balance sheet.
   (1) The income statement shows the net effects of revenues and expenses which effects the retained earnings on the balance sheet.
   (2) The statement of retained earnings reflects the net income and dividends paid and shows how retained earnings in the balance sheet moves from the beginning balance to the ending balance.
   (3) The statement of cash flows explains how the cash balance in the balance sheet moves from the beginning balance to the ending balance by looking a t the cash effects of operating, investing and financing activities.

   DIF: Moderate REF: P. 61-69 OBJ: 2,3,5 TOP: AICPA FN - Reporting
   MSC: AACSB Reflective

5. How can a company earn a large net income and have a small balance in retained earnings?

   ANS:
   The company may pay out most of their earnings in dividends.

   DIF: Difficult REF: P. 56-69 OBJ: 2,3,4,5 TOP: AICPA FN - Reporting
   MSC: AACSB Reflective

6. Suppose that your business had $100,000 of current liabilities that must be paid within the next few months and your current assets only totaled $70,000 and sales are slow. Identify two ways to finance the extra amount needed to pay your current liabilities.

   ANS:
   The business could issue more stock and receive equity financing or the company could borrow money on a note and receive debt financing.

   DIF: Difficult REF: P. 56 - 69 OBJ: 2,3,4,5 TOP: AICPA FN - Reporting
   MSC: AACSB Reflective

7. If you cold pick a single source of cash for your business (from the statement of cash flows), what would it be and why?

   ANS:
   Cash can be generated from operating activities, investing activities, and financing activities. The most desirable source of cash is from operations. Operations are continuing and will continue to generate cash. Business can finance its own growth and there is less risk of not being able to pay liabilities.

   DIF: Difficult REF: P. 65-69 OBJ: 2,3,4,5 TOP: AICPA FN - Reporting
   MSC: AACSB Reflective

8. Describe how vertical analysis can be used to analyze and evaluate a company's performance.

   ANS:
   By computing percentages of each item within a statement to a total for (or within) the statement, these percentages can be compared from year-to-year.

   In the balance sheet, each asset item is stated as a percent of the total assets. Each liability and stockholders' equity item is stated as a percent of total liabilities and stockholders' equity.

   In the income statement, each item is stated as a percent of sales.

   DIF: Moderate REF: P. 69,70,71 OBJ: 6 TOP: AICPA FN - Risk
   MSC: AACSB Reflective

PROBLEM

1. Determine the missing amount for each of the following:

ASSETS	=	**LIABILITIES**	+	**STOCKHOLDERS' EQUITY**
X		$45,000		$158,000
$294,000		X		$172,000
$96,000		$35,000		X

   ANS:

ASSETS	=	**LIABILITIES**	+	**STOCKHOLDERS' EQUITY**
X= $203,000		$45,000		$158,000
$294,000		X= $122,000		$172,000
$96,000		$35,000		X = $61,000

   DIF: Moderate REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
   MSC: AACSB Analytic

2. Determine the missing amounts on the following summaries of the balance sheet and income statement data for Barron, Inc.

	Barron, Inc.
December 31, 2006:	
Assets	$ 556, 602
Liabilities	(a)
Stockholders' equity	(b)
Increase (decrease) in assets, liabilities, and stockholders' equity during 2007:	
Assets	$42,116
Liabilities	$26,633
Stockholders' equity	$15,483
December 31, 2007:	
Assets	(c)
Liabilities	$441,856
Stockholders' equity	(d)

ANS:

	Barron, Inc.
December 31, 2006:	
Assets	$ 556, 602
Liabilities	(a) = $415,223
Stockholders' equity	(b)=$141,379
Increase (decrease) in assets, liabilities, and stockholders' equity during 2007:	
Assets	$42,116
Liabilities	$26,633
Stockholders' equity	$15,483
December 31, 2007:	
Assets	(c)=$598,718
Liabilities	$441,856
Stockholders' equity	(d)= $156,862

a = $441,856 - $26,633 = $415,223
b = $556,602 - $415,223 = $141,379
c = $556,602 + 42,116 = $598,718
d = $598,718 - $441,856 = $156,862

DIF: Difficult REF: P. 54 OBJ: 1 TOP: AICPA FN - Reporting
MSC: AACSB Analytic

3. **Part A**
Indicate the effect of each transaction during the month of October 2006 and the balances for the accounting equation after all transactions have been recorded. An accounting equation has been provided.

a. Opened a business bank account for Ole, Inc., with an initial deposit of $40,000 in exchange for capital stock.
b. Paid rent on the office building for the month of $2,000
c. Received cash for fees earned of $5,000
d. Purchased equipment $7,000
e. Borrowed $20,000 by issuing a note payable
f. Paid salaries for the month $1,000
g. Received cash for fees earned of $8,000
h. Paid dividends, $3,000
i. Paid interest on the note, $100

Assets = Liabilities + Stockholders' Equity					
	Cash	**Equipment**	**Notes Payable**	**Capital Stock**	**Retained Earnings**
a.					
b.					
c.					
d.					
e.					
f.					
g.					
h.					
i.					
Bal.					

Part B

Using the information from Part A, prepare (1) an income statement, (2) a statement of retained earnings, (3) a balance sheet, and (4) a statement of cash flows for the month of October.

Ole, Inc. **Income Statement**		

Ole, Inc. **Statement of Retained Earnings**		

Ole, Inc. **Balance Sheet**		

Ole, Inc. **Statement of Cash Flows**		

ANS:

Part A

Assets = Liabilities + Stockholders' Equity					
	Cash	**Equipment**	**Notes Payable**	**Capital Stock**	**Retained Earnings**
a.	40,000			40,000	
b.	-2,000				-2,000 Rent Expense
c.	5,000				5,000 Fees Earned
d.	-7,000	7,000			
e.	20,000		20,000		
f.	-1,000				-1,000 Salaries Expense
g.	8,000				8,000 Fees Earned
h.	-3,000				-3,000 Dividends
i.	-100				-100 Interest Expense
Bal.	59,900	7,000	20,000	40,000	6,900

Part B

Ole, Inc. Income Statement For the Month Ended October 31, 2006		
Revenues:		
Fees Earned		$13,000
Expenses:		
Rent Expense	$2,000	
Salaries Expense	1,000	
Interest Expense	100	
Total Expenses		3,100
Net Income		$ 9,900

Ole, Inc. Statement of Retained Earnings For the Month Ended October 31, 2006		
Retained Earnings, October 1,2006 Add: Net Income		0 $9,900
Less Dividends		(3,000)
Retained Earnings, October 31, 2006		$6,900

Ole, Inc. Balance Sheet October 31, 2006		
Assets		
Cash	$59,900	
Equipment	7,000	
Total Assets		$66,900
Liabilities		
Liabilities		
Notes Payable		$20,000
Stockholders' Equity		
Capital Stock	$40,000	
Retained Earnings	6,900	46,900
Total liabilities and Stockholders' Equity		$66,900

Ole, Inc. Statement of Cash Flows For the Month Ended October 31, 2006		
Cash flows from operating activities:		
Cash receipts from operating activities		$13,000
Cash payments for operating activities		3,100
Net cash flows from operating activities		$ 9,900
Cash flows from investing activities:		
Cash payments for equipment		(7,000)
Cash flows from financing activities:		
Cash receipts from issuing capital stock	$40,000	
Cash receipts from note payable	20,000	
Cash payments for dividends	(3,000)	
Net cash flows from financing activities		57,000
Cash as of October 31, 2006		$ 59,900

DIF: Difficult REF: P. 54-66 OBJ: 1,2,3,4 TOP: AICPA FN - Reporting
MSC: AACSB Analytic

4. The financial statements of Weems, Inc. are shown below. By analyzing the interrelationships between the financial statements, fill in the amounts left blank for **(a)** through **(n)**.

Weems, Inc. Income Statement For the Month Ended October 31, 2006		
Revenues:		
Fees Earned		**(a)**
Expenses:		
Rent Expense	$2,000	
Salaries Expense	**(b)**	
Utility Expense	500	
Interest Expense	250	
Miscellaneous Expense	250	
Total Expenses		5,000
Net Income		**(c)**

Weems, Inc. Statement of Retained Earnings For the Month Ended October 31, 2006		
Retained Earnings, October 1, 2006		0
Add: Net Income		$19,000
Less Dividends		**(d)**
Retained Earnings, October 31, 2006		$17,000

Weems, Inc. Balance Sheet October 31, 2006		
Assets		
Cash	$47,000	
Equipment	(e)	
Total Assets		(f)
Liabilities		
Liabilities		
Notes Payable		$10,000
Stockholders' Equity		
Capital Stock	$45,000	
Retained Earnings	(g)	(h)
Total liabilities and Stockholders' Equity		$72,000

Weems, Inc. Statement of Cash Flows For the Month Ended October 31, 2006		
Cash flows from operating activities:		
Cash receipts from operating activities		$ (i)
Cash payments for operating activities		5,000
Net cash flows from operating activities		$ (j)
Cash flows from investing activities:		
Cash payments for equipment		(k)
Cash flows from financing activities:		
Cash receipts from issuing capital stock		
Cash receipts from note payable		
Cash payments for dividends	(l)	
Net cash flows from financing activities		(m)
Cash as of October 31, 2006		$ (n)

ANS:

(a)	24,000	(b)	2,000	(c)	19,000	(d)	2,000	(e)	25,000
(f)	72,000	(g)	17,000	(h)	62,000	(i)	24,000	(j)	19,000
(k)	(25,000)	(l)	2,000	(m)	53,000	(n)	47,000		

DIF: Difficult REF: P. 62-65, 66-69 OBJ: 3,5
TOP: AICPA FN - Reporting MSC: AACSB Analytic

5. The following amounts (in alphabetical order) were taken from the accounting records of Wolfe Consulting, Inc., as of December 31, 2006. Wolfe began operations on January 1, 2006.

Capital stock	$12,500
Cash	49,375
Dividends	31,250
Fees earned	422,875
Interest expense	6,000
Land	156,125
Miscellaneous expense	9,375
Notes payable	50,000
Rent expense	45,000
Retained earnings (on 1/1/2006)	0
Salaries expense	100,000
Taxes expense	37,500
Utilities expense	50,000

Prepare (1) an income statement, (2) a statement of retained earnings, (3) a balance sheet, and (4) a statement of cash flows for the year ending December 31, 2006.

Wolfe Consulting, Inc. **Income Statement**		

Wolfe Consulting, Inc. Statement of Retained Earnings		

Wolfe Consulting, Inc. Balance Sheet		

Wolfe Consulting, Inc. Statement of Cash Flows		

ANS:

Wolfe Consulting, Inc. Income Statement For the Year Ended December 31, 2006		
Revenues:		
Fees Earned		$422,875
Expenses:		
Salaries Expense	$100,000	
Utilities Expense	50,000	
Rent Expense	45,000	
Tax Expense	37,500	
Miscellaneous Expense	9,375	
Interest Expense	6,000	
Total Expenses		247,875
Net Income		$175,000

Wolfe Consulting, Inc. Statement of Retained Earnings For the Year Ended December 31, 2006		
Retained Earnings, January 1, 2006		$ 0
Add: Net Income		$175,000
Less Dividends		31,250
Retained Earnings, December 31, 2006		$143,750

Wolfe Consulting, Inc. Balance Sheet December 31, 2006		
Assets		
Cash	$ 49,375	
Land	156,875	
Total Assets		$206,250
Liabilities		
Liabilities		
Notes Payable		50,000
Stockholders' Equity		
Capital Stock		12,500
Retained Earnings		143,750
Total liabilities and Stockholders' Equity		$206,250

Wolfe Consulting, Inc. Statement of Cash Flows For the Year Ended December 31, 2006		
Cash flows from operating activities:		
Cash receipts from operating activities		$422,875
Cash payments for operating activities		247,875
Net cash flows from operating activities		$175,000
Cash flows from investing activities:		
Cash payments for land		(156,875)
Cash flows from financing activities:		
Cash receipts from issuing capital stock	$12,500	
Cash receipts from note payable	50,000	
Cash payments for dividends	(31,250)	
Net cash flows from financing activities		31,250
Cash as of December 31, 2006		$ 49,375

DIF: Difficult REF: P. 62-65, 66-69 OBJ: 3,5
TOP: AICPA FN - Reporting MSC: AACSB Analytic

6. Lou's Laundry and Dry Cleaning incorporated and started business on January 1, 2006. Although excellent with laundry and dry cleaning, the owner knows nothing about accounting. The owner has hired you to perform the accounting and record-keeping for his business.

Part A

Enter the following transactions into the following accounting equation provided.

Jan.	2	Lou's Laundry and Dry Cleaning began business by depositing $30,000 in a checking account in the name of Lou's Laundry and Dry Cleaning, Inc. Capital stock is issued.
	2	Borrowed $6,000 from City Bank for 5 years and signed a promissory note with an annual interest rate of 9%.
	3	Purchased equipment from Washers Wholesale, $16,200.
	3	Purchased supplies costing $3,000 from Suds 'n Stuff with cash.
	4	Paid one month's rent for business space in Pine Plaza, $1,000.
	12	Services provided to customers during the first half of January totaled $6,700. All services were paid for in cash.
	13	Paid employees for the first two weeks in January, $1,120.
	28	Paid wages for January 15 – 28, $1,120.
	31	Services provided the second half of January totaled $16,500. All services were paid for in cash.
	31	Received and paid the utility bill, $500.
	31	Received and paid the telephone bill, $250.
	31	Declared and paid dividends to the stockholders, $2,140.

Assets = Liabilities + Stockholders' Equity							
	Cash	**Supplies**	**Equipment**	**Notes Payable**	**Capital Stock**	**Retained Earnings**	**Type of Retained Earnings Transaction**

Part B
Using the information from Part A, prepare (1) an income statement, (2) a statement of retained earnings, (3) a balance sheet, and (4) a statement of cash flows.

Lou's Laundry and Dry Cleaning, Inc. **Income Statement**		

Lou's Laundry and Dry Cleaning, Inc. **Statement of Retained Earnings**		

Lou's Laundry and Dry Cleaning, Inc.
Balance Sheet

Lou's Laundry and Dry Cleaning, Inc. Statement of Cash Flows		

ANS:

Part A

Assets = Liabilities + Stockholders' Equity							
Jan.	**Cash**	**Supplies**	**Equipment**	**Notes Payable**	**Capital Stock**	**Retained Earnings**	**Type of Retained Earnings Transaction**
2	30,000				30,000		
2	6,000			6,000			
3	(16,200)		16,200				
3	(3,000)	3,000					
4	(1,000)					(1,000)	Rent expense
12	6,700					6,700	Revenue
13	(1,120)					(1,120)	Salary expense
28	(1,120)					(1,120)	Salary expense
31	16,500					16,500	Revenue
31	(500)					(500)	Utility expense
31	(250)					(250)	Telephone expense
31	(2,140)					(2,140)	Dividends
Bal.	33,870	3,000	16,200	6,000	30,000	17,070	

Part B

Lou's Laundry and Dry Cleaning, Inc. Income Statement For the month ended January 31, 2006		
Revenues:		$23,200
Expenses:		
Salary expense	2240	
Rent expense	1000	
Utility expense	500	
Telephone expense	250	
Total expenses		3,990
Net income		$19,210

Lou's Laundry and Dry Cleaning, Inc. Statement of Retained Earnings For the month ended January 31, 2006		
Beginning Retained Earnings,January 1, 2006		$0
Add: Net income		19,210
Less: Dividends		2,140
Ending Retained Earnings, December 31, 2006		$17,070

Lou's Laundry and Dry Cleaning, Inc. Balance Sheet January 31, 2006		
Assets		
Cash	$33,870	
Supplies	3,000	
Equipment	16,200	
Total Assets		$53,070
Liabilities		
Notes Payable		$6,000
Stockholders' Equity		
Capital Stock	$30,000	
Retained Earnings	17,070	
Total Stockholders' Equity		47,070
Total Liabilities and Stockholders' Equity		$53,070

Lou's Laundry and Dry Cleaning, Inc. Statement of Cash Flows For the Month Ended January 31, 2006		
Cash flows from operating activities:		
Cash receipts from operating activities		$23,200
Cash payments for operating activities		3,990
Net cash flows from operating activities		$19,210
Cash flows from investing activities:		
Cash payments for supplies	($ 3,000)	
Cash payments for equipment	(16,200)	
Net cash flows from investing activities		(19,200)
Cash flows from financing activities:		
Cash receipts from issuing capital stock	$30,000	
Cash receipts from note payable	6,000	
Cash payments for dividends	(2,140)	
Net cash flows from financing activities		33,860
Cash as of January 31, 2006		$33,870

DIF: Difficult REF: P. 54-69 OBJ: 1,2,3,4,5 TOP: AICPA FN - Reporting
MSC: AACSB Analytic

7. Mac's Mobile Wash incorporated and started business on September 1, 2006. Mac brings his big rig truck to companies to wash their semi-trucks. Although excellent with washing semis, the owner knows nothing about accounting. The owner has hired you to perform the accounting and record-keeping for his business.

Part A
Enter the following transactions into the accounting equation provided.

Sep.	2	Mac's Mobile Wash began business by depositing $50,000 in a checking account in the name of Mac's Mobile Wash, Inc. Capital stock was issued.
	2	Borrowed $8,000 from City Bank for 5 years and signed a promissory note with an annual interest rate of 9%.
	3	Purchased equipment from Washers Wholesale, $26,200.
	3	Purchased supplies costing $3,000 from Suds 'n Stuff for cash.
	4	Paid one month's rent for business space in U-STOR-IT, $1,000 (record this as an expense,).
	5	Paid $4,200 for advertising to appear in the Pine Press newspaper this month.
	12	Services provided to customers during the first half of September totaled $7,700 cash.
	12	Paid employees for hours worked during the first two weeks of September, $1,500.
	20	Borrowed another $4,000 from City Bank.
	28	Paid wages for September 15 – 28, $1,500.
	30	Services provided the second half of September totaled $16,500 cash.
	30	Received and paid the water bill, $750.
	30	Declared and paid dividends to the stockholders, $2,000.

Assets = Liabilities + Stockholders' Equity							
	Cash	Supplies	Equipment	Notes Payable	Capital Stock	Retained Earnings	Type of Retained Earnings Transaction

Part B
Using the information from Part A, prepare (1) an income statement, (2) a statement of retained earnings, (3) a balance sheet, and (4) a statement of cash flows.

Mac's Mobile Wash, Inc. Income Statement		

Mac's Mobile Wash, Inc. **Statement of Retained Earnings**		

Mac's Mobile Wash, Inc. **Balance Sheet**		

Mac's Mobile Wash, Inc. Statement of Cash Flows		

Part C
Use the ending balances from Part B. Now, assume it is the next month (month two) for Mac's Mobile Wash, Inc. Following are the transactions for October. Record these transactions in the accounting equation provided.

Oct.	1	Paid $1,000 on the note payable (assume that there is no interest charge).
	2	Received $2,000 cash for services (washes)
	5	Purchased additional supplies of $1,500 (the supplies from September have not been used up)
	10	Received $500 cash for services (washes)
	15	Paid employees for hours worked during the first two weeks of October, $1,500.
	18	Received $2,000 cash for services (washes).
	20	Issued an additional $10,000 capital stock for cash.
	31	Services (washes) provided the second half of September totaled $10,500 cash.
	31	Received and paid the water bill $950.
	31	Paid this month's rent for business space in U-STOR-IT, $1,000
	31	Paid employees for hours worked during the last two weeks of October, $1,500.

Assets = Liabilities + Stockholders' Equity							
	Cash	Supplies	Equipment	Notes Payable	Capital Stock	Retained Earnings	Type of Retained Earnings Transaction
Beg. Bal.	46,050	3,000	26,200	12,000	50,000	13,250	

Part D
Using the completed accounting equation from Part C, prepare (1) an income statement, (2) a statement of retained earnings, (3) a balance sheet, and (4) a statement of cash flows.

Mac's Mobile Wash, Inc. Income Statement		

Mac's Mobile Wash, Inc.
Statement of Retained Earnings

Mac's Mobile Wash, Inc.
Balance Sheet

Mac's Mobile Wash, Inc.
Statement of Cash Flows

ANS:
Part A

Assets = Liabilities + Stockholders' Equity							
	Cash	**Supplies**	**Equipment**	**Notes Payable**	**Capital Stock**	**Retained Earnings**	**Type of Retained Earnings Transaction**
2	50,000				50,000		
2	8,000			8,000			
3	(26,200)		26,200				
3	(3,000)	3,000					
4	(1,000)					(1,000)	Rent expense
5	(4,200)					(4,200)	Advertising expense
12	7,700					7,700	Revenue
14	(1,500)					(1,500)	Salary expense
20	4,000			4,000			
28	(1,500)					(1,500)	Salary expense
30	16,500					16,500	Revenue
30	(750)					(750)	Water expense
30	(2,000)					(2,000)	Dividends
Bal.	46,050	3,000	26,200	12,000	50,000	13,250	

Part B

Mac's Mobile Wash, Inc. Income Statement For the Month Ended September 30, 2006		
Revenues:		$24,200
Expenses:		
Advertising expense	$4,200	
Salary expense	3,000	
Rent expense	1,000	
Water expense	750	
Total expenses		8,950
Net income		$15,250

Mac's Mobile Wash, Inc. Statement of Retained Earnings For the Month Ended September 30, 2006		
Beginning Retained Earnings, September 1, 2006		$0
Add: Net income		15,250
Less: Dividends		2,000
Ending Retained Earnings, September 30, 2006		$13,250

Mac's Mobile Wash, Inc. Balance Sheet September 30, 2006		
Assets		
Cash		$46,050
Supplies		3,000
Equipment		26,200
Total Assets		$75,250
Liabilities		
Note payable		$12,000
Stockholders' Equity		
Capital Stock		50,000
Retained earnings		13,250
Total liabilities and Stockholders' Equity		$75,250

Mac's Mobile Wash, Inc. Statement of Cash Flows For the Month Ended September 30, 2006		
Cash flows from operating activities:		
Cash receipts from operating activities		$24,200
Cash payments for operating activities		8,950
Net cash flows from operating activities		$15,250
Cash flows from investing activities:		
Cash payments for supplies	($ 3,000)	
Cash payments for equipment	(26,200)	
Net cash flows from investing activities		(29,200)
Cash flows from financing activities:		
Cash receipts from issuing capital stock	$50,000	
Cash receipts from note payable	12,000	
Cash payments for dividends	(2,000)	
Net cash flows from financing activities		60,000
Cash as of September 30, 2006		$46,050

Part C

Assets = Liabilities + Stockholders' Equity							
	Cash	Supplies	Equipment	Notes Payable	Capital Stock	Retained Earnings	Type of Retained Earnings Transaction
Beg. Bal.	46,050	3,000	26,200	12,000	50,000	13,250	
1	(1,000)			(1,000)			
2	2,000					2,000	Revenue
5	(1,500)	1,500					
10	500					500	Revenue
15	(1,500)					(1,500)	Salary expense
18	2,000					2,000	Revenue
20	10,000				10,000		
31	10,500					10,500	Revenue
31	(950)					(950)	Water expense
31	(1,000)					(1,000)	Rent expense
31	(1,500)					(1,500)	Salary expense
Bal.	63,600	4,500	26,200	11,000	60,000	23,300	

Part D

Mac's Mobile Wash, Inc. Income Statement For the Month Ended October 31, 2006		
Revenues:		$15,000
Expenses:		
Salary expense	$3,000	
Rent expense	1,000	
Water expense	950	
Total expenses		$ 4,950
Net income		$10,050

Mac's Mobile Wash, Inc. Statement of Retained Earnings For the Month Ended October 31, 2006		
Beginning Retained Earnings, October 1, 2006		$13,250
Add: Net income		10,050
Less: Dividends		$ 0
Ending Retained Earnings, October, 31, 2006		$23,300

Mac's Mobile Wash, Inc. Balance Sheet October 31, 2006		
Assets		
Cash	$63,600	
Supplies	4,500	
Equipment	26,200	
Total Assets		$94,300
Liabilities		
Note payable		$11,000
Stockholders' Equity		
Capital Stock		60,000
Retained earnings		23,300
Total liabilities and Stockholders' Equity		$94,300

Mac's Mobile Wash, Inc. Statement of Cash Flows For the Month Ended October 31, 2006		
Cash flows from operating activities:		
Cash receipts from operating activities		$15,000
Cash payments for operating activities		4,950
Net cash flows from operating activities		$10,050
Cash flows from investing activities:		
Cash payments for supplies		($ 1,500)
Cash flows from financing activities:		
Cash receipts from issuing capital stock	$10,000	
Cash payment on note payable	(1,000)	
Net cash flows from financing activities		9,000
Net increase in cash		$17,550
October 1, 2006 cash balance		46,050
October 31, 2006 cash balance		$63,600

DIF: Difficult REF: P. 54- 69 OBJ: 1,2,3,4,5 TOP: AICPA FN - Reporting
MSC: AACSB Analytic

8. WillSell Realty Corporation had the following balance sheet amounts. Place these amounts into the appropriate spots in the accounting equation provided and determine the balance of Building.

Accounts Payable	$ 6,000
Accounts Receivable	1,000
Building	**?**
Cash	3,000
Capital Stock	$19,000
Equipment	6,000
Land	8,000
Retained Earnings	2,000

Assets = Liabilities + Stockholders' Equity							
Cash	**Accounts Receivable**	**Building**	**Land**	**Equipment**	**Accounts Payable**	**Capital Stock**	**Retained Earnings**

ANS:

Assets = Liabilities + Stockholders' Equity							
Cash	**Accounts Receivable**	**Building**	**Land**	**Equipment**	**Accounts Payable**	**Capital Stock**	**Retained Earnings**
3,000	1,000	9,000	8,000	6,000	6,000	19,000	2,000

DIF: Moderate REF: P. 56-62, 65-66 OBJ: 2,4
TOP: AICPA FN - Reporting MSC: AACSB Analytic

9. The following are included in Ace Auto Parts, Inc.'s December 31, 2006 balance sheet:

Accounts Receivable	$ 50,000
Building	100,000
Cash	60,000
Land	130,000
Accounts Payable	40,000
Notes Payable	70,000
Stockholders' Equity	**?**

Below are the balances for December 31, 2007

Accounts Receivable	$ 75,000
Building	100,000
Cash	150,000
Land	130,000
Accounts Payable	60,000
Notes Payable	50,000
Stockholders' Equity	**?**

Analyze the changes in these balances and determine net income for 2005, assuming that the only change to stockholders' equity is from net income.

ANS:

	Assets	=	Liabilities	+	Stockholder's Equity
	50,000		40,000		
	100,000				
	60,000				
	130,000		70,000		
Bal. 12/31/2006	340,000		110,000		230,000

	Assets	=	Liabilities	+	Stockholder's Equity
	75,000				
	100,000				
	150,000		60,000		
	130,000		50,000		
Bal. 12/31/2007	455,000		110,000		345,000

Stockholders' Equity ending balance	$345,000
Stockholders' Equity beginning balance	230,000
Change - Net income	$115,000

DIF: Difficult REF: P. 56 -69 OBJ: 2,3,4,5 TOP: AICPA FN - Reporting
MSC: AACSB Analytic

CASE

PepsiCo's Financial Statements

Answer the following question(s) using these selected portions of PepsiCo's financial statements.

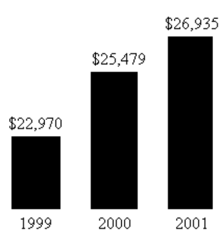
Consolidated Statement of Income

Fiscal years ended December 29, 2001, December 30, 2000 and December 25, 1999 — PepsiCo, Inc. and Subsidiaries

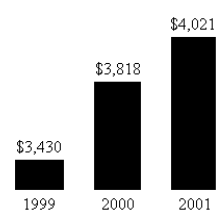
(in millions except per share amounts)	2001	2000	1999
Net Sales			
New PepsiCo	**$26,935**	$25,479	$22,970
Bottling operations	–	–	2,123
Total Net Sales	**26,935**	25,479	25,093
Costs and Expenses			
Cost of sales	**10,754**	10,226	10,326
Selling, general and administrative expenses	**11,608**	11,104	11,018
Amortization of intangible assets	**165**	147	193
Merger-related costs	**356**	–	–
Other impairment and restructuring charges	**31**	184	73
Total Costs and Expenses	**22,914**	21,661	21,610
Operating Profit			
New PepsiCo	**4,021**	3,818	3,430
Bottling operations and equity investments	–	–	53
Total Operating Profit	**4,021**	3,818	3,483
Bottling equity income and transaction gains/(losses), net	**160**	130	1,083
Interest expense	**(219)**	(272)	(421)
Interest income	**67**	85	130
Income Before Income Taxes	**4,029**	3,761	4,275
Provision for Income Taxes	**1,367**	1,218	1,770
Net Income	**$ 2,662**	$ 2,543	$ 2,505
Net Income Per Common Share			
Basic	**$ 1.51**	$ 1.45	$ 1.41
Diluted	**$ 1.47**	$ 1.42	$ 1.38

See accompanying notes to consolidated financial statements.

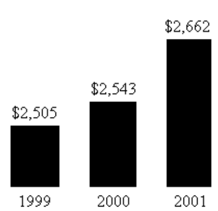
New PepsiCo Net Sales



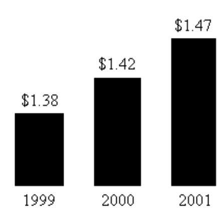
New PepsiCo Operating Profit



Net Income



Earnings Per Share



Consolidated Statement of Cash Flows

PepsiCo, Inc. and Subsidiaries

Fiscal years ended December 29, 2001, December 30, 2000 and December 25, 1999

(in millions)	**2001**	2000	1999
Operating Activities			
Net income	**$ 2,662**	$ 2,543	$ 2,505
Adjustments to reconcile net income to net cash provided by operating activities bottling equity income and transaction (gains)/losses, net	**(160)**	(130)	(1,083)
Depreciation and amortization	**1,082**	1,093	1,156
Merger-related costs	**356**	–	–
Other impairment and restructuring charges	**31**	184	73
Cash payments for merger-related costs and other restructuring charges	**(273)**	(38)	(98)
Deferred income taxes	**162**	33	573
Deferred compensation – ESOP	**48**	36	32
Other noncash charges and credits, net	**209**	303	368
Changes in operating working capital, excluding effects of acquisitions and dispositions			
Accounts and notes receivable	**7**	(52)	(141)
Inventories	**(75)**	(51)	(202)
Prepaid expenses and other current assets	**(6)**	(35)	(209)
Accounts payable and other current liabilities	**(236)**	219	357
Income taxes payable	**394**	335	274
Net change in operating working capital	**84**	416	79
Net Cash Provided by Operating Activities	**4,201**	4,440	3,605
Investing Activities			
Capital spending	**(1,324)**	(1,352)	(1,341)
Acquisitions and investments in unconsolidated affiliates	**(432)**	(98)	(430)
Sales of businesses	**–**	33	513
Sales of property, plant and equipment	**–**	57	130
Short-term investments, by original maturity			
More than three months – purchases	**(2,537)**	(4,950)	(2,209)
More than three months – maturities	**2,078**	4,585	2,220
Three months or less, net	**(41)**	(9)	12
Other, net	**(381)**	(262)	(67)
Net Cash Used for Investing Activities	**(2,637)**	(1,996)	(1,172)
Financing Activities			
Proceeds from issuances of long-term debt	**324**	130	3,480
Payments of long-term debt	**(573)**	(879)	(1,216)
Short-term borrowings, by original maturity			
More than three months – proceeds	**788**	198	3,699
More than three months – payments	**(483)**	(155)	(2,758)
Three months or less, net	**(397)**	1	(2,814)
Cash dividends paid	**(994)**	(949)	(935)
Share repurchases – common	**(1,716)**	(1,430)	(1,285)
Share repurchases – preferred	**(10)**	–	–
Quaker share repurchases	**(5)**	(254)	(382)
Proceeds from reissuance of shares	**524**	–	–
Proceeds from exercises of stock options	**623**	690	383
Net Cash Used for Financing Activities	**(1,919)**	(2,648)	(1,828)
Effect of exchange rate changes on cash and cash equivalents	–	(4)	3
Net (Decrease)/Increase in Cash and Cash Equivalents	**(355)**	(208)	608
Cash and Cash Equivalents, Beginning of Year	**1,038**	1,246	638
Cash and Cash Equivalents, End of Year	**$ 683**	$ 1,038	$1,246
Supplemental Cash Flow Information			
Interest paid	**$ 159**	$ 226	$ 384
Income taxes paid	**$ 857**	$876	$ 689
Acquisitions:			
Fair value of assets acquired	**$ 604**	$ 80	$ 717
Cash paid and debt issued	**(432)**	(98)	(438)
Liabilities assumed	**$ 172**	$(18)	$ 279

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

December 29, 2001 and December 30, 2000 PepsiCo, Inc. and Subsidiaries

(in millions except per share amounts)	2001	2000
ASSETS		
Current Assets		
Cash and cash equivalents	**$ 683**	$ 1,038
Short-term investments, at cost	**966**	467
	1,649	1,505
Accounts and notes receivable, net	**2,142**	2,129
Inventories	**1,310**	1,192
Prepaid expenses and other current assets	**752**	791
Total Current Assets	**5,853**	5,617
Property, Plant and Equipment, net	**6,876**	6,558
Intangible Assets, net	**4,841**	4,714
Investments in Unconsolidated Affiliates	**2,871**	2,979
Other Assets	**1,254**	889
Total Assets	**$21,695**	$20,757
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Short-term borrowings	**$ 354**	$ 202
Accounts payable and other current liabilities	**4,461**	4,529
Income taxes payable	**183**	64
Total Current Liabilities	**4,998**	4,795
Long-Term Debt	**2,651**	3,009
Other Liabilities	**3,876**	3,960
Deferred Income Taxes	**1,496**	1,367
Preferred Stock, no par value	**26**	49
Deferred Compensation – preferred	**–**	(27)
Common stock, par value 12/3¢ per share (issued 1,782 and 2,029 shares, respectively)	**30**	34
Capital in excess of par value	**13**	375
Deferred compensation	**–**	(21)
Retained earnings	**11,519**	16,510
Accumulated other comprehensive loss	**(1,646)**	(1,374)
	9,916	15,524
Less: repurchased common stock, at cost (26 and 280 shares, respectively)	**(1,268)**	(7,920)
Total Common Shareholders' Equity	**8,648**	7,604
Total Liabilities and Shareholders' Equity	**$21,695**	$20,757

See accompanying notes to consolidated financial statements.

Consolidated Statement of Common Shareholders' Equity

PepsiCo, Inc. and Subsidiaries

Fiscal years ended December 29, 2001, December 30, 2000 and December 25, 1999

	2001		2000		1999	
(in millions)	Shares	Amount	Shares	Amount	Shares	Amount
Common Stock						
Balance, beginning of year	**2,029**	**$ 34**	2,030	$ 34	2,037	$ 34
Share repurchases	–	–	(9)	–	(13)	–
Stock option exercises	**6**	–	–	–	–	–
Quaker stock option exercises	**3**	–	8	–	6	–
Shares issued to effect merger	**(256)**	**(4)**	–	–	–	–
Balance, end of year	**1,782**	**30**	2,029	34	2,030	34
Capital in Excess of Par Value						
Balance, beginning of year		**375**		559		904
Share repurchases		–		(236)		(370)
Stock option exercises (a)		**82**		52		(21)
Reissued shares		**150**		–		–
Shares issued to effect merger		**(595)**		–		–
Other		**1**		–		46
Balance, end of year		**13**		375		559
Deferred Compensation						
Balance, beginning of year		**(21)**		(45)		(68)
Net activity		**21**		24		23
Balance, end of year		–		(21)		(45)
Retained Earnings						
Balance, beginning of year		**16,510**		14,921		13,356
Net income		**2,662**		2,543		2,505
Shares issued to effect merger		**(6,644)**		–		–
Cash dividends declared – common		**(1,005)**		(950)		(936)
Cash dividends declared – preferred		**(4)**		(4)		(4)
Balance, end of year		**11,519**		16,510		14,921
Accumulated Other Comprehensive Loss						
Balance, beginning of year		**(1,374)**		(1,085)		(1,139)
Currency translation adjustment (CTA)		**(218)**		(289)		(136)
CTA reclassification adjustment		–		–		175
Cash flow hedges, net of tax:						
Cumulative effect of accounting change		**3**		–		–
Derivative (losses)/gains, net		**(21)**		–		–
Minimum pension liability adjustment, net of tax		**(38)**		(2)		17
Other		**2**		2		(2)
Balance, end of year		**(1,646)**		(1,374)		(1,085)
Repurchased Common Stock						
Balance, beginning of year	**(280)**	**(7,920)**	(271)	(7,306)	(255)	(6,535)
Shares repurchased	**(35)**	**(1,716)**	(38)	(1,430)	(36)	(1,285)
Stock option exercises	**20**	**751**	29	816	20	514
Reissued shares	**13**	**374**	–	–	–	–
Shares issued to effect merger	**256**	**7,243**	–	–	–	–
Balance, end of year	**(26)**	**(1,268)**	(280)	(7,920)	(271)	(7,306)
Total Common Shareholders' Equity		**$ 8,648**		$ 7,604		$ 7,078

(a) Includes total tax benefit of $212 in 2001, $177 in 2000 and $105 in 1999.

See accompanying notes to consolidated financial statements.

Note 1– Summary of Significant Accounting Policies

On August 2, 2001, we completed our merger transaction, which resulted in The Quaker Oats Company (Quaker) becoming a wholly-owned subsidiary of PepsiCo. As a result, we restated all prior period consolidated financial statements presented to reflect the combined results of operations, financial position and cash flows of both companies as if they had always been merged. See Note 2.

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect reported amounts of assets, liabilities, revenues, expenses and disclosure of contingent assets and liabilities. Actual results could differ from these estimates.

Tabular dollars are in millions, except per share amounts. All per share amounts reflect common per share amounts, assume dilution unless noted, and are based on unrounded amounts. Certain reclassifications were made to the 2000 and 1999 amounts to conform to the 2001 presentation.

Items Affecting Comparability

Our fiscal year ends on the last Saturday in December and, as a result, a fifty-third week is added every five or six years. The fiscal year ended December 30, 2000 consisted of fifty-three weeks. The fifty-third week increased 2000 net sales by an estimated $294 million, operating profit by an estimated $62 million and net income by an estimated $44 million or $0.02 per share. See Note 21 for the impact on our business segments.

The consolidated financial statements subsequent to the dates of the bottling transactions described in Note 10 are not comparable to the consolidated financial statements presented for prior periods as certain bottling operations that were previously consolidated are now accounted for under the equity method. In addition, the merger costs described in Note 2, other impairment and restructuring charges described in Note 3, and the income tax adjustment described in Note 14 affect comparability.

Principles of Consolidation

The financial statements include the consolidated accounts of PepsiCo, Inc. and its controlled affiliates. Intercompany balances and transactions have been eliminated. Investments in unconsolidated affiliates over which we exercise significant influence, but not control, are accounted for by the equity method. Our definition of control for majority owned affiliates considers the exercisability of the minority interest rights, and consolidation would be precluded to the extent that the minority interest holds substantive participating rights. Our share of the net income or loss of unconsolidated affiliates accounted for by the equity method is included in consolidated net income.

Issuances of Subsidiary Stock

The issuance of stock by one of our subsidiaries to third parties reduces our proportionate ownership interest in the subsidiary. Unless the issuance of such stock is part of a broader corporate reorganization, we recognize a gain or loss equal to the difference between the issuance price per share and our carrying amount per share. Such gain or loss, net of the related tax, is recognized in consolidated net income when the transaction occurs.

Revenue Recognition

We recognize revenue when products are delivered to customers consistent with sales terms. Sales terms generally do not allow a right of return.

Marketing Costs
Marketing costs are reported in selling, general and administrative expenses and include costs of advertising, promotional programs and other marketing activities. Advertising expenses were $1.7 billion in 2001 and 2000 and $1.6 billion in 1999. Deferred advertising expense classified as prepaid expenses in the Consolidated Balance Sheet was $111 million in 2001 and $127 million in 2000. Deferred advertising costs are expensed in the year first used and consist of:
- media and personal service prepayments,
- promotional materials in inventory, and
- production costs of future media advertising.

We classify promotional payments to customers, including cooperative advertising, as either a reduction of net sales or as marketing costs. During 2000 and 2001, the Financial Accounting Standards Board's (FASB) Emerging Issues Task Force (EITF) addressed various issues related to the income statement classification of certain promotional payments, including consideration from a vendor to a reseller or another party that purchases the vendor's products. EITF 01-9, *Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products,* was issued in November 2001 and codified earlier pronouncements. Primarily effective for 2002, adoption of EITF 01-9 will reduce our net sales by $3.4 billion in 2001, $3.1 billion in 2000 and $2.9 billion in 1999, with selling, general and administrative expenses reduced by the same amounts.

Distribution Costs
Distribution costs are reported in either cost of sales or selling, general and administrative expenses depending on the distribution method, and include the costs of shipping and handling activities. Shipping and handling expenses classified as selling, general and administrative expenses were $2.6 billion in 2001, $2.5 billion in 2000 and $2.4 billion in 1999.

Research and Development Costs
Research and development costs are expensed in the year incurred. Research and development costs were $206 million in 2001, $207 million in 2000 and $187 million in 1999.

Stock-Based Compensation
We measure stock-based compensation cost as the excess of the quoted market price of PepsiCo common stock at the grant date over the amount the employee must pay for the stock (exercise price). Our policy is to generally grant stock options with an exercise price equal to the stock price at the date of grant, and accordingly, no compensation cost is recognized. Under certain prior incentive programs, compensation cost for cash payments expected to be paid to employees in lieu of stock options was based on the grant date value and recognized over the vesting period of the award.

Pension and Postretirement Benefits
Our pension plans cover substantially all full-time U.S. employees and certain international employees. Benefits depend on years of service and earnings or are based on stated amounts for each year of service. Our postretirement plans provide medical and life insurance benefits principally to U.S. retirees and their dependents. Employees are eligible for benefits if they meet age and service requirements and qualify for retirement benefits. Plans generally use a measurement date of September 30. The pre-merger Quaker plans used a measurement date of December 31. Prior service costs are amortized on a straight-line basis over the average remaining service period of employees expected to receive benefits.

Derivative Instruments and Hedging

We manage risks associated with commodity prices, foreign exchange rates, interest rates and our stock price and may use derivatives to hedge these risks. Hedging transactions are executed in accordance with our policies. As a matter of policy, we do not use derivative instruments unless there is an underlying exposure and, therefore, we do not use derivative instruments for trading or speculative purposes. Any change in the value of our derivative instruments would be substantially offset by an opposite change in the value of the underlying hedged items. All derivative instruments are recognized in our Consolidated Balance Sheet at fair value. The fair value of our derivative instruments is generally based on quoted market prices. There is no significant concentration of credit risk or activity with any of the counterparties.

Using qualifying criteria defined in Statement of Financial Accounting Standards No. (SFAS) 133, *Accounting for Derivative Instruments and Hedging Activities*, derivative instruments are designated and accounted for as either fair value or cash flow hedges. Our evaluations of hedge effectiveness are subject to assumptions based on the terms and timing of the underlying exposures. For a fair value hedge, both the effective and ineffective portions of the change in fair value of the derivative instrument, along with an adjustment to the carrying amount of the hedged item for fair value changes attributable to the hedged risk, are recognized in earnings. For a cash flow hedge, changes in the fair value of a derivative instrument that is highly effective are deferred in accumulated other comprehensive income or loss until the underlying hedged item is recognized in earnings. The ineffective portion is recognized in earnings immediately. If a fair value or cash flow hedge was to cease to qualify for hedge accounting or be terminated, it would continue to be carried on the balance sheet at fair value until settled, but hedge accounting would be discontinued prospectively. If a forecasted transaction were no longer probable of occurring, amounts previously deferred in accumulated other comprehensive income would be recognized immediately in earnings.

We are subject to market risk with respect to the cost of commodities because our ability to recover increased costs through higher pricing may be limited by the competitive environment in which we operate. We manage this risk primarily through the use of fixed-price purchase orders, pricing agreements, geographic diversity and derivative instruments. Derivative instruments, including futures, options and swaps, are used to hedge fluctuations in prices of a portion of anticipated commodity purchases, primarily corn, oats, natural gas, heating oil, vegetable oil and packaging materials. Our use of derivative instruments is not significant to our commodity purchases. Derivative instruments designated as hedges of anticipated commodity purchases are accounted for generally as cash flow hedges. The earnings impact from commodity hedges is classified as either cost of sales or selling, general and administrative expenses consistent with the expense classification of the underlying hedged items.

International operations constitute about one-fifth of our annual business segment operating profit. Operating in international markets involves exposure to movements in foreign exchange rates, primarily the Mexican peso, British pound, Canadian dollar, euro and Brazilian real, which principally impacts the translation of our international operating profit into U.S. dollars. On occasion, we may enter into derivative financial instruments, as necessary, to reduce the effect of foreign exchange rate changes. We manage the use of foreign exchange derivatives centrally. Derivative instruments designated as foreign exchange hedges are generally accounted for as fair value hedges. The earnings impact from these hedges is classified as either cost of sales or selling, general and administrative expenses consistent with the expense classification of the underlying hedged items.

We centrally manage our debt and investment portfolios considering investment opportunities and risks, tax consequences and overall financing strategies. We use interest rate and currency swaps to effectively change the interest rate and currency of specific debt issuances, with the objective of reducing our overall borrowing costs. These swaps are entered into concurrently with the issuance of the debt that they are intended to modify. The notional amount, interest payment and maturity date of the swaps match the principal, interest payment and maturity date of the related debt. Our credit risk related to interest rate and currency swaps is considered low because such swaps are entered into only with strong creditworthy counterparties, are generally settled on a net basis and are of relatively short duration. Interest rate and currency swaps are designated as hedges of underlying fixed rate obligations and accounted for as fair value hedges. The earnings impact from these hedges is classified as interest expense.

The portion of our deferred compensation liability, which is based on our stock price, is subject to market risk. Prepaid forward contracts with financial institutions are used to hedge this risk and are accounted for as natural hedges. The earnings impact from these hedges is classified as selling, general and administrative expenses consistent with the expense classification of the deferred compensation liability. Prior to the adoption of SFAS 133, the earnings impact from these equity derivative contracts was classified as interest income.

The cash flows related to the above derivative instruments are classified in the Consolidated Statement of Cash Flows in a manner consistent with those of the transactions being hedged.

Cash Equivalents and Short-Term Investments

Cash equivalents represent funds temporarily invested with original maturities of three months or less. All other investment portfolios are primarily classified as short-term investments.

Inventories
Inventories are valued at the lower of cost (computed on the average, first-in, first-out (FIFO) or last-in, first-out (LIFO) method) or at net realizable value.

Property,Plant and Equipment
Property, plant and equipment are stated at cost. Depreciation is calculated primarily on a straight-line basis. Buildings and improvements are depreciated over their estimated useful lives, generally ranging from 15 to 40 years. Machinery and equipment (including fleet) are depreciated over their estimated useful lives, generally ranging from 5 to 15 years.

Intangible Assets
Goodwill, the excess of our investments in unconsolidated affiliates over our equity in the underlying net assets of these investments, and trademarks and brands are amortized on a straight-line basis over their estimated useful lives, generally ranging from 20 to 40 years. Other identifiable intangibles are amortized on a straight-line basis over their estimated useful lives, generally ranging from 5 to 20 years.

Asset Impairment
All long-lived assets, including goodwill, investments in unconsolidated affiliates and other identifiable intangibles, are evaluated for impairment on the basis of undiscounted cash flows whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impaired asset is written down to its estimated fair market value based on the best information available. Estimated fair market value is generally measured by discounting estimated future cash flows. Considerable management judgment is necessary to estimate discounted future cash flows.

The depreciation or amortization periods for long-lived assets to be held and used are periodically evaluated to determine whether events or circumstances have occurred that warrant revision to the useful lives.

Income Taxes
Deferred taxes are recorded to give recognition to temporary differences between the tax bases of assets or liabilities and their reported amounts in the financial statements. Deferred tax assets generally represent items that can be used as a tax deduction or credit in future years. Deferred tax liabilities generally represent items for which we have taken a tax deduction, but have not yet recorded in the Consolidated Statement of Income. Valuation allowances are established for deferred tax assets where the amount of expected future taxable income from operations does not support the realization of these deferred tax assets.

Deferred tax liabilities are not recognized for temporary differences related to investments in foreign subsidiaries and in unconsolidated foreign affiliates that are essentially permanent in duration. It would not be practicable to determine the amount of any such deferred tax liabilities.

1. Refer to PepsiCo's Financial Statements. Prepare a comparative vertical analysis for the balance sheets for 2001 and 2000 for the asset accounts. Make sure that your total = 100%.

ANS:

	2001	**2000***
Cash	3.1%	5.0%
Short term investments	4.5%	2.2%
Accounts Receivable	9.9%	10.3%
Inventory	6.0%	5.7%
Prepaid expenses	3.5%	3.8%
Property Plant and Equipment	31.7%	31.6%
Intangible assets	22.3%	22.7%
Investments in Unconsolidated Affiliates	13.2%	14.4%
Other assets	5.8%	4.2%

*Note: 2000 off due to rounding.

DIF: Difficult REF: P. 69-71 OBJ: 6 TOP: AICPA FN - Risk
MSC: AACSB Analytic

2. Refer to PepsiCo's Financial Statements. Prepare vertical analysis for PepsiCo for 2001 for the following:
   Net sales
   Cost of sales
   Gross Profit (you may have to compute this number)
   Operating Profit
   Net Income

ANS:

	2001
Net sales	100.0%
Cost of sales	40.0%
Gross Profit	60.0%
Operating Profit	14.9%
Net Income	9.9%

DIF: Difficult REF: P. 69-71 OBJ: 6 TOP: AICPA FN - Risk
MSC: AACSB Analytic

3. Refer to PepsiCo's Financial Statements and answer the following questions:

(a) Did PepsiCo issue any stock in 2001? If so, how much and where might this information be found?
(b) Did PepsiCo repurchase any stock in 2001? If so, how much and where might this information be found?

ANS:

(a) No. The information is in the Stockholders' Equity section of the Balance sheet.
(b) No. The information is in the Stockholders' Equity section of the Balance sheet.

DIF: Difficult REF: P. 62-69 OBJ: 3,4,5 TOP: AICPA FN - Reporting
MSC: AACSB Reflective

4. Refer to PepsiCo's Financial Statements. PepsiCo's cash balance decreased from 2000 to 2001. Just looking at the balance sheet, do you think this a good or bad thing? What other short-term asset accounts might you consider in answering this question?

ANS:
Cash declined, but there is a subtotal of cash and short -term investments that shows an increase from 2000 to 2001. It appears that there is a better usage of funds, by placing more in an area that will earn a return.

DIF: Difficult REF: P. 56-69 OBJ: 2,3,4,5 TOP: AICPA FN - Reporting
MSC: AACSB Reflective