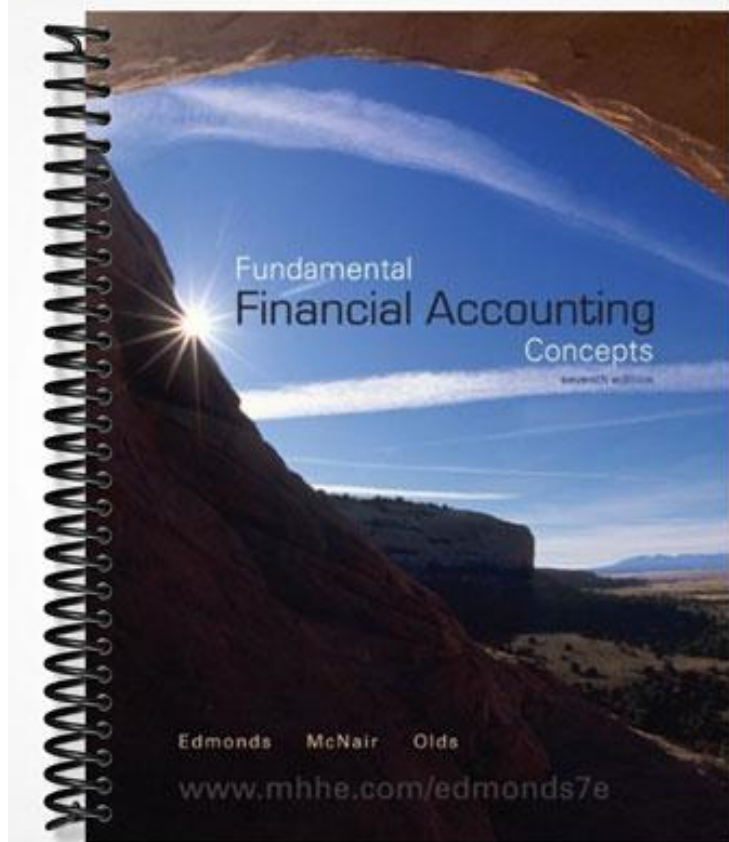


TEST BANK



Chapter 02 Understanding the Accounting Cycle

Short Answer Questions

Indicate how each event affects the elements of financial statements. Use the following letters to record your answer in the box shown below each element. You do not need to enter amounts.

Increase = I Decrease = D No Effect = N

1. Frank Co. performed services for customers on account.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

2. Gonzales Co. collected \$1,000 cash from accounts receivable.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

Chapter 02 - Understanding the Accounting Cycle

3. Sanchez Co. provided \$800 of services for a customer who paid \$500 cash immediately and promised to pay an additional \$300 one month later.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

4. Albertson Co. purchased a \$3,000 machine for cash.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

5. At the end of the accounting period, Snyder Co. recognized accrued salaries.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

Chapter 02 - Understanding the Accounting Cycle

6. At the end of the accounting period, Lantz Co. accrued \$600 of interest revenue on an interest earning account.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

7. When is revenue recognized under accrual accounting?

8. What does the balance in accounts receivable represent?

9. When are expenses recognized under accrual accounting in relation to the payment of cash?

10. What is the effect on the accounting equation of a cash payment to creditors?

11. Why are adjusting entries necessary in an accrual accounting system? What are some common examples?

12. What effect does the recording of revenue normally have on total assets?

13. What effect does providing services on account have on the statement of cash flows? The balance sheet?

14. Describe the purpose of the closing process.

15. Describe the difference between temporary and permanent accounts, and state which ones are closed.

16. Define the accounting cycle and list the stages of the cycle.

17. Explain the meaning of the term, "matching concept."

18. The temporary or nominal accounts are closed prior to the start of the next accounting cycle. In this closing process, the amounts in each of these accounts are transferred to what other account(s)?

19. What is meant by the "fraud triangle"?

20. Discuss the importance of ethics in the accounting profession.

Multiple Choice Questions

21. Bledsoe Company received \$5,000 cash from the issue of stock on January 1, 2011. During 2011 Bledsoe earned \$8,500 of revenue on account. The company collected \$6,000 cash from accounts receivable and paid \$5,400 cash for operating expenses. Based on this information alone, during 2011,

- A. Total assets increased by \$14,100.
- B. Total assets increased by \$600.
- C. Total assets increased by \$8,100.
- D. Total assets did not change.

22. Aaronson Company experienced an accounting event that affected its financial statements as indicated below:

Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
+		NA		+	+		NA		+	NA

Which of the following accounting events could have caused these effects on ABC's statements?

- A. Issued common stock.
- B. Purchased equipment on account.
- C. Earned revenue on account.
- D. Recognized accrued salaries owed to employees.

23. Which of the following choices accurately reflects how the recording of accrued salary expense affects a business's financial statements?

	Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
A.	NA	=	+	+	-	-	-	+	=	NA	NA
B.	NA	=	NA	+	+ -	NA	-	NA	=	NA	NA
C.	NA	=	+	+	-	NA	-	+	=	-	NA
D.	+	=	+	+	NA	NA	-	+	=	-	-OA

24. Which of the following transactions does **not** involve an accrual?

- A. Recording interest earned that will be received in the next period.
- B. Recording operating expense incurred but not yet paid.
- C. Recording salary expense incurred but not yet paid.
- D. Recording the pre-payment of two year's worth of insurance.

25. Sakimoto Company recorded salaries earned by employees but not yet paid. Which of the following represents the effect of this transaction on the financial statements?

	Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
A.	+	=	+	+	NA	+	-	NA	=	+	- OA
B.	NA	=	+	+	-	NA	-	+	=	-	- IA
C.	-	=	NA	+	-	NA	-	+	=	-	NA
D.	NA	=	+	+	-	NA	-	+	=	-	NA

26. Revenue on account amounted to \$5,000. Cash collections of accounts receivable amounted to \$2,300. Expenses for the period were \$2,100. Net income for the period was

- A. \$200.
- B. \$350.
- C. \$3,050.
- D. \$2,900.

27. The recognition of an expense may be accompanied by which of the following?

- A. An increase in assets
- B. A decrease in liabilities
- C. A decrease in revenue
- D. An increase in liabilities

28. Which of the following statements is true in regard to accrual accounting?

- A. Revenue is recorded only when cash is received.
- B. Expenses are recorded when they are incurred.
- C. Revenue is recorded in the period when it is earned.
- D. Both B and C.

29. The term "realization" refers to which of the following?

- A. The closing of an account.
- B. The collection of cash.
- C. The earning of revenue.
- D. The correction of an error.

30. Which of the following events involves a deferral?
- A. Recording interest that has been earned but not received.
 - B. Recording supplies that have been purchased with cash but not yet used.
 - C. Recording revenue that has been earned but not yet collected in cash.
 - D. Recording salaries owed to employees at the end of the year that will be paid during the following year.
31. Recognition of revenue **may** result in which of the following?
- A. A decrease in a liability.
 - B. An increase in a liability.
 - C. An increase in assets.
 - D. A. and C.
32. Mobley Company provided \$25,500 of services on account, and collected \$18,000 from customers during the year. The company also incurred \$17,000 of expenses on account, and paid \$15,400 against its payables. As a result of these events,
- A. total assets would increase
 - B. total liabilities would increase
 - C. total equity would increase
 - D. all of the above are correct
33. Which of the following events would **not** require an end-of-year adjusting entry?
- A. Purchasing supplies for cash
 - B. Providing services on account
 - C. Purchasing a 12-month insurance policy on July 1
 - D. All of the above would require an end-of-year adjustment
34. The entry to recognize work completed on deferred revenue involves which of the following?
- A. An increase in assets and a decrease in liabilities
 - B. An increase in liabilities and a decrease in equity
 - C. A decrease in assets and a decrease in liabilities
 - D. A decrease in liabilities and an increase in equity

35. Jordan Snow Removal Company received a cash advance of \$6,000 on December 1, 2011 to provide services during the months of December, January, and February. The year-end adjustment to recognize the partial expiration of the contract will

- A. increase equity by \$2,000
- B. increase assets by \$2,000
- C. increase liabilities by \$2,000
- D. both A and B

36. The entry to recognize salary expense incurred but not yet paid involves which of the following?

- A. An increase in assets
- B. An increase in liabilities
- C. A decrease in assets
- D. A decrease in liabilities

37. The following accounts and balances were drawn from the records of Jared Company:

Cash	\$8,000
Accounts Payable	\$5,500
Common Stock	\$4,000
Land	\$18,000
Accounts Receivable	\$2,000

Based on this information alone the amount of Jared's retained earnings is

- A. \$9,500.
- B. \$18,500.
- C. \$15,500.
- D. \$22,500.

The following account balances were drawn from the 2011 financial statements of Gwynn Company

Cash	\$2,200	Certificate of Deposit	\$500
A/R	750	Common Stock	?
Land	600	Retained Earnings	2,800
		Revenues	5,100
		Expenses	2,450

38. Based on the above information, what is the balance of Common Stock for Gwynn Company?

- A. \$750
- B. \$1,250
- C. \$3,400
- D. \$6,200

39. Based on the above information, what was the beginning balance (on January 1, 2011) in retained earnings for Gwynn Company?

- A. \$2,650
- B. \$3,400
- C. \$150
- D. \$450

40. Smith Company loaned Jones Company \$10,000 cash. The loan carried a two-year term. In the year that the loan was made,

- A. Jones Company's assets would decrease.
- B. Smith Company would show a cash outflow in the investing activities section of its cash flow statement.
- C. Smith Company's liabilities would increase.
- D. Jones Company would show a cash inflow in the operating activities section of its cash flow statement.

41. During 2011, Davis Company purchased land costing \$2,400 cash. The company earned \$2,000 revenue on account and incurred \$1,100 of operating expenses for which cash was paid.

- As a result of these transactions,
- A. total assets increased by \$2,400.
 - B. total assets increased by \$900.
 - C. total liabilities increased by \$1,100.
 - D. none of these.

42. The balance sheet of Vargas Company shows retained earnings of \$50,000, total liabilities of \$30,000, and common stock \$10,000. Based on this information, you would know that
- A. the amount of ownership claims cannot be determined.
 - B. since the company began, the total amount of net income exceeded total dividends by \$50,000.
 - C. the company obtained most of its assets through borrowing activities.
 - D. Vargas Company has enough cash to pay off its liabilities.

43. The Bloom Company issued stock for \$50,000 cash on January 20, 2011. During 2011, the company recorded revenue on account of \$18,000 and expenses for which cash was paid of \$10,000. Bloom received \$10,200 cash from accounts receivable. The company also purchased land for \$6,000 cash. Based on this information, the amount of change in cash for 2011 was
- A. \$62,200
 - B. \$44,200
 - C. \$50,200
 - D. \$54,200

44. On December 31, the balance sheet of the Falcon Company contained the following accounts and balances:

Cash	\$500	Certificate of Deposit	\$600
Equipment	\$1,250	Common Stock	?
Accounts Payable	\$500	Retained Earnings	\$850

Based on the above information, the balance in Common Stock must be what amount?

- A. \$0
 - B. \$250
 - C. \$1,000
 - D. \$1,100
45. Which of the following would be included in the "cash flow from operating activities" section of the statement of cash flows?
- A. Accrual of salary expense at year-end.
 - B. Cash received from on an interest earning account.
 - C. Payments of cash dividends to the owners of the business.
 - D. Purchase of land for cash.

46. Revenue on account amounted to \$3,000. Cash collections of accounts receivable amounted to \$2,700. Cash paid for expenses was \$2,500. The amount of employee salaries accrued at the end of the year was \$300. Cash flow from operating activities was

- A. \$200.
- B. \$300.
- C. \$500.
- D. None of these.

47. Which of the following accounts would **not** appear on a balance sheet?

- A. Unearned Revenue.
- B. Salaries Payable.
- C. Interest Revenue.
- D. Retained Earnings.

48. Common Stock would appear on which of the following financial statements?

- A. Income statement
- B. Balance sheet
- C. Statement of changes in stockholders' equity
- D. Both B and C

49. Woodward Enterprises had the following events during 2011:

The business issued \$20,000 of common stock to its stockholders.

The business purchased land for \$12,000 cash.

Services were provided to customers for \$16,000 cash.

Services were provided to customers for \$6,000 on account.

The company borrowed \$16,000 from the bank.

Operating expenses of \$12,000 were incurred and paid in cash.

Salary expense of \$800 was accrued.

A dividend of \$4,000 was paid to the owners of Woodward Enterprises.

Assuming the company began operations during 2011, the amount of retained earnings as of December 31, 2011 would be:

- A. \$5,200
- B. \$6,000
- C. \$10,000
- D. \$22,000

50. Which of the following would cause net income on the accrual basis to be different (either higher or lower) than "cash provided by operating activities" on the statement of cash flows?

- A. Acquired \$10,000 cash from the owners.
- B. Incurred operating expenses on account.
- C. Provided services to a customer for cash.
- D. Purchased land for cash.

51. Which of the following would cause net income on the accrual basis to be different than (either higher or lower than) "cash provided by operating activities" on the statement of cash flows?

- A. Accrued interest earned on an interest earning account.
- B. Paid a cash dividend to the stockholders.
- C. Invested cash in an interest earning account.
- D. Purchased land for cash.

52. Ruiz Company provided services for \$15,000 cash during the 2011 accounting period. Ruiz incurred \$12,000 expenses on account during 2011, and by the end of the year, \$3,000 of that amount had been paid with cash. Assuming that these are the only accounting events that affected Ruiz during 2011,

- A. The amount of net income shown on the income statement is \$3,000.
- B. The amount of net income shown on the income statement is \$9,000.
- C. The amount of net loss shown on the income statement is \$3,000.
- D. The amount of net cash flow from operating activities shown on the statement of cash flows is \$6,000.

The following accounts and balances were drawn from the records of Hoover Company on December 31, 2011:

Cash	\$1,000	Accounts Receivable	\$850
Dividends	500	Common Stock	975
Land	800	Revenue	800
Accounts Payable	450	Expense	550

53. Total assets on the December 31, 2011 balance sheet would amount to:

- A. \$3,150.
- B. \$3,450.
- C. \$1,800.
- D. \$2,650.

54. The amount of net income shown on the December 31, 2011 income statement would amount to:

- A. \$550.
- B. \$800.
- C. \$50.
- D. \$250.

55. The amount of retained earnings as of January 1, 2011 was:

- A. \$1,475.
- B. \$1,800.
- C. \$1,050.
- D. \$1,225.

Norris Company experienced the following transactions during 2011, its first year in operation.

1. Issued \$6,000 of common stock to stockholders.
2. Provided \$2,400 of services on account.
3. Paid \$1,600 cash for operating expenses.
4. Collected \$1,800 of cash from accounts receivable.
5. Paid a \$100 cash dividend to stockholders.

56. The amount of net income recognized on Norris Company's 2011 income statement is:

- A. \$500.
- B. \$400.
- C. \$800.
- D. \$600.

57. The amount of net cash flow from operating activities shown on Norris Company's 2011 statement of cash flows is

- A. \$200.
- B. \$300.
- C. \$800.
- D. \$400.

58. The total amount of assets shown on Norris Company's 2011 balance sheet is

- A. \$6,200.
- B. \$6,800.
- C. \$6,700.
- D. None of these.

59. The amount of retained earnings appearing on Norris Company's 2011 balance sheet is:

- A. \$200.
- B. \$700.
- C. \$800.
- D. \$6,700.

60. On December 31, 2011, Preston Co. owed \$1,200 in salaries to employees who had worked during December but would be paid in January. If the year-end adjustment is properly recorded on December 31, 2011, what will be the effect of the accrual on the following items for Preston?

	Net Income	Cash Flow from Operating Activities
a.	No effect	No effect
b.	Decrease	Decrease
c.	Increase	No effect
d.	No effect	Increase

- A. Option A
- B. Option B
- C. Option C
- D. Option D

61. Tocca Co. collected a \$5,000 cash advance from a customer on November 1, 2011 for work to be performed over a six-month period beginning on that date.. If the year-end adjustment is properly recorded, what will be the effects of the accrual on Tocca's 2011 financial statements?

- A. Increase assets and increase liabilities
- B. Increase assets and increase revenues
- C. Decrease liabilities and increase revenues
- D. No effect

62. Natchez Company collected \$9,000 on September 1, 2011 from a customer for services to be provided over a one-year period beginning on that date. How much revenue would Natchez Company report related to this contract on its income statement for the year ended December 31, 2011? How much would it report as cash flows from operating activities for 2011?

- A. \$3,000; \$3,000
- B. \$3,000; \$9,000
- C. \$9,000; \$9,000
- D. \$0; \$9,000

63. The matching concept refers to the "matching" of:

- A. expenses and liabilities
- B. expenses and revenues
- C. assets and equity
- D. assets and liabilities

64. The results of the matching process are best reported on which financial statement?

- A. Balance sheet
- B. Income statement
- C. Statement of changes in stockholders' equity
- D. Statement of cash flows

65. Expenses that are matched with the period in which they are incurred are frequently called:

- A. market expenses
- B. matching expenses
- C. period costs
- D. working costs

66. If retained earnings decreased during the year, and no dividends were paid, which of the following must be true?

- A. Expenses for the year exceeded revenues
- B. The company did not have enough cash to pay its expenses
- C. Total equity decreased
- D. Liabilities increased during the year

67. Which of the following correctly states the proper order of the accounting cycle?

- A. Record transactions, adjust accounts, prepare statements, close temporary accounts.
- B. Adjust accounts, record transactions, close temporary accounts, prepare statements.
- C. Prepare statements, record transactions, close temporary accounts, adjust accounts.
- D. Adjust accounts, prepare statements, record transactions, close temporary accounts.

68. The purpose of the accrual basis of accounting is to:

- A. Report revenue when received.
- B. Improve the matching of revenue and expense in the proper period.
- C. Report expenses when cash disbursements are made.
- D. Improve the company's earnings per share.

69. Which of the following financial statement elements is closed at the end of an accounting cycle?

- A. Liabilities
- B. Common stock
- C. Assets
- D. Revenues

70. Which of the following accounts is **not** closed at the end of an accounting cycle?

- A. Liabilities
- B. Revenues
- C. Dividends
- D. Expenses

71. Which of the following financial statement elements contain cumulative information rather than information for the current period only?

- A. Dividends
- B. Revenues
- C. Expenses
- D. Retained Earnings

72. The balance in a revenue account at the beginning of an accounting period will always be

- A. equal to the amount of retained earnings for the previous period.
- B. last period's ending balance.
- C. higher than the previous periods beginning balance.
- D. zero.

73. The accounting principle that guides accountants, when faced with a recognition dilemma, to choose the alternative that produces the lowest net income is referred to as

- A. the matching principle.
- B. internal control.
- C. conservatism.
- D. materiality.

74. Which of the following is **not** a component of the fraud triangle?

- A. Opportunity
- B. Rationalization
- C. Trust
- D. Pressure

75. If a CPA voluntarily discloses information acquired from a client, he or she may be in violation of which of the following principles?

- A. Confidentiality
- B. Conservatism
- C. Materiality
- D. Objective evidence

76. Which of the following is **not** a common feature of ethical misconduct?

- A. The capacity to rationalize.
- B. The existence of pressure leading to an incentive.
- C. The existence of a strong system of internal controls.
- D. The presence of an opportunity.

77. Policies and procedures designed to reduce the opportunities for fraud are often called:

- A. accounting principles
- B. asset source transactions
- C. internal controls
- D. financial systems

78. What action did the U. S. Congress take because of the audit failures at Enron, WorldCom and other companies?

- A. Required publicly-traded companies to be audited by a government agency
- B. Required companies to begin preparing an additional financial statement
- C. Passed the Sarbanes-Oxley Act
- D. Passed an amendment to the Securities and Exchange Act

79. Which of the following describes the effects of a claims exchange transaction on a company's financial statements?

	Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
A.	NA	=	NA	+	NA	NA	-	NA	=	NA	+ OA
B.	+	=	+	+	NA	NA	-	NA	=	NA	+ OA
C.	NA	=	+	+	-	NA	-	+	=	-	NA
D.	All of these could represent the effects of a claims exchange transaction.										

80. Which of the following is an asset source transaction?

- A. Issued common stock.
- B. Paid a cash dividend to stockholders.
- C. Invested cash in an interest earning account.
- D. Accrued salary expense.

81. Which of the following is an asset use transaction?

- A. Purchased machine for cash.
- B. Paid a cash dividend to stockholders.
- C. Invested cash in an interest earning account.
- D. Accrued salary expense.

82. Which of the following is a claims exchange transaction?

- A. Purchased machine for cash.
- B. Paid a cash dividend to stockholders.
- C. Invested cash in an interest earning account.
- D. Accrued salary expense.

83. Which of the following is an asset exchange transaction?

- A. Issued common stock.
- B. Accrued salary expense at the end of the accounting period.
- C. Paid cash dividends to stockholders.
- D. Invested cash in an interest earning account.

84. An increase in cash that is accompanied by an increase in common stock is a/an

- A. claims exchange transaction.
- B. asset source transaction.
- C. asset use transaction.
- D. asset exchange transaction.

85. Which of the following is an example of a claims exchange transaction?

- A. An asset decreases and an equity account decreases.
- B. An asset increases and another asset decreases.
- C. A liability increases and an equity account decreases.
- D. A liability increases and an equity account also increases.

Essay Questions

86. Kelly Company uses accrual accounting. Indicate whether each of the following statements regarding Kelly's accounting system is true or false.

- _____ a) The recognition of accounting events and the realization of cash consequences may occur in different accounting periods.
- _____ b) The cash consequence of a transaction always precedes its accounting recognition.
- _____ c) Recognition is an act of recording an event in the financial statements.
- _____ d) The term accrual applies to events that are recognized after the associated cash is paid or collected.
- _____ e) Kelly is not permitted to make cash sales.

87. Whitmore Co. performed services for a customer on account. Indicate whether each of the following statements about this transaction is true or false.

- _____ a) Assets and equity both increase when the revenue is recognized.
- _____ b) This transaction did not affect cash flows.
- _____ c) The company recorded an increase in revenue and a decrease in accounts receivable.
- _____ d) Recognition of revenue would be delayed until cash was received.
- _____ e) This transaction is an example of an asset source transaction.

88. Dandridge Company collected cash in 2011 from a customer for services to be performed beginning January 2012. Indicate whether each of the following statements about this transaction is true or false.

- a) Dent's 2011 income statement would not be affected by this transaction.
- b) Dent's 2011 statement of cash flows would be affected by this transaction.
- c) This transaction is an asset exchange transaction.
- d) The revenue for the services provided will be recorded in 2012.
- e) This transaction is considered an accrual transaction.

89. Regarding the relationships of revenues and expenses to assets and liabilities, state whether each of the following statements is true or false.

- a) Recording an increase in a revenue account may be associated with an increase in assets.
- b) Recording an increase in a revenue account may be associated with a decrease in liabilities.
- c) An increase in Salaries Expense may be accompanied by a decrease in Salaries Payable.
- d) Recording a decrease in assets may be associated with an increase in an expense account.
- e) Recording an increase in an expense may be associated with a decrease in a revenue account.

90. Wilgus Company paid \$57,000 in January 2012 for salaries that had been earned by employees in December 2011. Indicate whether each of the following statements about financial statement effects of the January 2012 event is true or false.

- _____ a) The income statement for 2012 is not affected because the salaries expense had been recognized at the end of December.
- _____ b) On the 2012 statement of cash flows, cash flows from operating activities decreased.
- _____ c) Payment of the salaries in 2012 decreased a liability.
- _____ d) The statement of changes in stockholders' equity would not be affected because the salaries expense had been recognized at the end of December.
- _____ e) Both assets and equity decreased as a result of this transaction.

91. Indicate whether each of the following statements about the closing process and the accounting cycle is true or false.

- _____ a) The closing process transfers certain account balances to retained earnings at the end of the accounting cycle.
- _____ b) Only accounts that appear on the income statement are closed at the end of each accounting cycle.
- _____ c) Another name for permanent accounts is "nominal accounts."
- _____ d) The permanent accounts contain information that is cumulative in nature.
- _____ e) The retained earnings balance at the end of any given year is equal to that year's net income.

92. Regarding the effects of end-of-period adjustments, state whether each of the following statements is true or false.

- a) Recording the usage of supplies involves a decrease in assets and a decrease in equity.
- b) The accrual of salaries is considered a claims exchange transaction.
- c) Recording services performed on a prepaid contract involves a decrease in liabilities and an increase in assets.
- d) End of period adjustments never affect cash flows.
- e) Failure to record accrued at the end of the year will cause reported income to be higher than it should have been.

93. Indicate whether each of the following statements regarding the four types of accounting events is true or false.

- a) Asset use transactions involve an increase in one asset and a decrease in another asset.
- b) An asset source transaction involves an increase in assets and an increase in a corresponding claims account.
- c) An asset exchange transaction involves an increase in an asset and a decrease in a claims account.
- d) Asset exchange transactions involve an increase in one asset and a decrease in another asset.
- e) Some claims exchange transactions involve an increase in a liability account and a decrease in an equity account.

94. Indicate whether each of the following statements about corporate governance is true or false.

_____ a) The Financial Accounting Standards Board issues a code of ethical behavior by which public accountants must abide.

_____ b) The Sarbanes Oxley Act created the Public Company Accounting Oversight Board (PCAOB).

_____ c) Because of the Sarbanes Oxley Act, many audit firms now provide nonaudit services to audit clients.

_____ d) The fraud triangle identifies opportunity, pressure, and rationalization as the three elements that are typically present when fraud is committed.

_____ e) An executive found guilty of falsely certifying a company's financial statements faces up to a \$5 million fine and 20 years in prison.

True / False Questions

95. The term "recognition" means to report an economic event in the financial statements.

True False

96. Companies that use accrual accounting recognize revenues and expenses at the time that cash is paid or received.

True False

97. The term "accrual" describes an earnings event that is recognized after cash is paid or received.

True False

98. A company may recognize a revenue or expense without a corresponding cash collection or payment in the same accounting period.

True False

99. A payment to an employee in settlement of salaries payable decreases an asset and decreases a liability.

True False

100. An increase in an expense may be accompanied by an increase in a liability.

True False

101. Revenues and liabilities are temporary accounts.

True False

102. In the closing process, the amounts in temporary accounts are moved to retained earnings, a permanent account.

True False

103. Accounts that are closed include expenses, dividends, and unearned revenues.

True False

104. After closing, only balance sheet accounts have non-zero balances.

True False

105. Two of the steps in the accounting cycle are adjusting the accounts and closing the accounts.

True False

106. Cash-basis accounting often fails to match expenses with revenues.

True False

107. The matching concept leads accountants to select the recognition alternative that produces the lowest amount of net income.

True False

108. Adjusting entries never affect a business's cash account.

True False

109. Asset use transactions always involve the payment of cash.

True False

110. The governance of a corporation includes the roles and responsibilities of the board of directors, managers, shareholders, and auditor.

True False

111. The ethical standards for certified public accountants simply require that such accountants comply with applicable laws and regulations.

True False

112. Certified public accountants are obligated to act in a way that serves the public interest.

True False

113. The bankruptcies of Enron and WorldCom both indicated the occurrence of major audit failures.

True False

114. The Sarbanes-Oxley Act includes several significant reforms that affect the auditing profession, but it did not reduce an audit firm's ability to provide non-audit services to its audit clients.

True False

115. A business's internal controls are designed to reduce the probability of occurrence of fraud.

True False

116. Providing services to customers on account is an asset source transaction.

True False

117. An adjusting entry that decreases unearned revenue and increases service revenue is a claims exchange transaction.

True False

118. Sometimes the recognition of revenue is accompanied by an increase in liabilities.

True False

119. The collection of an account receivable is a claims exchange transaction.

True False

120. An adjusting entry to accrue salary expense is a claims exchange transaction.

True False

Essay Questions

121. Horizon Corporation began business operations and experienced the following transactions during 2011:

- 1) Issued common stock for \$10,000 cash.
- 2) Provided services to customers for \$25,000 on account.
- 3) Purchased \$500 of supplies on account.
- 4) Paid \$6,000 cash to rent office space for a 12-month period beginning June 1.
- 5) Collected \$23,000 cash from customers.
- 6) Paid cash for \$18,000 of operating expenses.
- 7) Adjusted the accounting records to reflect that there was \$150 of supplies remaining on hand at year-end.
- 8) Recorded an end-of-year adjustment to recognize rent expense.

Required:

- a) Record the above transactions on a horizontal statements model, reflecting their effect on the different financial statements.
- b) Prepare Horizon Corporation's income statement, balance sheet and statement of cash flows for the year ended December 31, 2011.

122. The following transactions apply to Brunswick Corporation.

- 1) Issued common stock for \$35,000 cash.
- 2) Provided services to customers for \$18,000 on account.
- 3) Purchased land for \$18,000 cash.
- 4) Paid \$9,000 for operating expenses.
- 5) Collected \$15,000 cash from customers.
- 6) Accrued \$400 of salary expense at year end.
- 7) Paid \$2,500 dividends to stockholders.

Required:

- a) Identify the effect on the statement of cash flows for each of the above transactions.
- b) Classify the above accounting events into one of four types of transactions (asset source, asset use, asset exchange, claims exchange).

123. Record each of the following events in the horizontal statements model. After each event, record the corresponding **end-of-year adjustment** that would be necessary.

- a) Paid \$18,000 for a 1-year lease beginning April 1.
- b) Paid \$1,500 to purchase supplies. At year end, \$540 of supplies remained.
- c) Received a \$24,000 cash advance for a 6-month contract beginning on Sept. 1.

124. The following data were taken from the accounting records of Lorenzo Company. Except where indicated, the balances are as of December 31, 2011 before closing entries have been made.

Service revenue	29,000
Retained earnings, January 1, 2011	37,260
Salaries expense	12,500
Other operating expense	6,700
Common stock	43,000
Cash flow from operating activities	8,400
Dividends	2,000
Insurance expense	800
Rent expense	6,000
Unearned revenue	3,600

Required:

- a) List the accounts that should be closed at the end of 2011.
- b) Prepare an income statement for Lorenzo Company for 2011.
- c) What is the balance in retained earnings after closing entries have been made?

125. For each of the following transactions, indicate the type by entering AS for asset source transactions, AU for asset use transactions, AE for asset exchange transactions, and CE for claims exchange transactions.

- 1) ___ Paid \$10,000 for a plot of land.
- 2) ___ Recorded the accrual of \$1,000 in salaries to be paid later.
- 3) ___ Issued common stock for \$20,000 in cash.
- 4) ___ Earned revenue to be collected next year.
- 5) ___ Paid \$2,000 in dividends to its stockholders.
- 6) ___ Received cash from customers in #4 above.
- 7) ___ Paid the salaries accrued in #2 above.
- 8) ___ Borrowed money from a local bank.

126. Classify each of the following transactions for the purpose of the statement of cash flow as operating activities (OA), investing activities (IA), financing activities (FA), or not reported on the statement of cash flows (NA).

- 1) ___ Made adjusting entry to recognize interest revenue on investments.
- 2) ___ Borrowed funds from the bank.
- 3) ___ Paid rent for the month.
- 4) ___ Paid cash to settle accrued salary expense.
- 5) ___ Issued common stock for \$30,000 cash.
- 6) ___ Collected accounts receivable.
- 7) ___ Purchased land.

127. Jack Grimes started a consulting business, Grimes Consulting, on January 1, 2011 by issuing \$7,000 of common stock. In addition, the following events occurred in 2011.

Provided services on account, \$25,500.

Paid cash for \$11,500 in operating expenses.

Collected \$9,000 of the revenue that was previously recorded on account.

Paid a cash dividend of \$4,000 to the stockholders.

Required:

a) Show the effects of the above transactions on the accounting equation.

Assets = Liabilities + Common Stock + Retained Earnings

1)

2)

3)

4)

5)

b) Prepare an income statement and statement of cash flows for 2011.

128. Thiessen Company started its business by issuing \$6,000 of common stock on January 1, 2011. The company performed \$18,000 of service for customers on account in 2011. It collected \$12,500 of this amount in 2011, recorded expenses on account of \$14,500, paid \$11,000 of the payables owed, and paid a \$300 dividend to the stockholders.

Required:

a) What is the amount of total assets at the end of 2011?

b) What is the amount of cash on hand at the end of 2011?

c) What is the net income for 2011?

d) Prepare a balance sheet for 2011.

129. The Palin Corporation was started on January 1, 2011, with the issuance of \$10,000 of stock. During 2011, the company provided \$15,000 of services on account and collected \$9,000 of that amount. Palin incurred \$11,500 of expenses, and paid \$10,000 of that amount during 2011. On December 31, 2011, Palin paid investors a \$400 cash dividend and accrued \$1,000 of salary expense.

Required: 1) What is the net income for year ending December 31, 2011?

2) Prepare Palin Corporation's Statement of Cash Flows for the year ended December 31, 2011.

3) What is the balance in Palin's retained earnings account after closing entries are made on December 31, 2011?

4) What is Palin's cash balance on December 31, 2011?

130. (a) At January 1, 2011, accounts receivable was \$20,000. Cash collected on accounts receivable during 2011 was \$15,000. At December 31, 2011, accounts receivable was \$30,000. What were the revenues earned on account during 2011?

(b) At January 1, 2011, accounts payable was \$17,000. During 2011, expenses on account were \$28,000. At December 31, 2011, accounts payable was \$15,000.

What was the amount of cash paid on accounts payable during 2011?

(c) At January 1, 2011, the balance in the retained earnings account was \$7,200. During 2011, revenue earned was \$19,800 and expenses incurred were \$7,400. At December 31, 2011, the balance in the retained earnings account was \$11,500.

What was the amount of cash dividends paid to stockholders during 2011?

(d) At January 1, 2011, the balance in the supplies account was \$450. At December 31, 2011, the company counted \$600 of supplies on hand. The company reported supplies expense in 2011 of \$2,300.

What was the total of supplies purchases during 2011?

131. Washington Co. began operations on January 1, 2011, by issuing \$10,000 in common stock to the stockholders. On April 1, 2011, Link accepted an advance of \$18,000 to provide services for a one-year period beginning April 1. During 2011, services in the amount of \$16,000 were provided to customers on account, and 75% of this amount was collected by year-end. During 2011, expenses incurred on account were \$12,000, and 60% of this amount was paid by year-end. During the year, Washington paid \$600 to purchase supplies. By year-end, \$480 of the supplies had been used. Dividends to stockholders were \$1,000 during the year. During 2011, Washington paid salaries of \$14,000, and on December 31, 2011, the company accrued salaries of \$1,200.

- 1) What would Washington report for service revenue for 2011?
- 2) What would Washington report for salaries expense for 2011?
- 3) What would Washington report for supplies expense for 2011?
- 4) What would the amount be for net cash flows from operating activities for 2011?
- 5) What is the net income for 2011?
- 6) What would the balance in the retained earnings account be at December 31, 2011?

132. In a company's annual report, the reader will find a company's income statement, statement of changes in stockholder's equity, balance sheet, and statement of cash flows. These financial statements can help the reader to answer specific questions. Identify which financial statement would be most useful in answering the following questions. If more than one financial statement can answer the question, please identify all applicable statements.

- 1) What was the amount of cash dividends paid to the stockholders during the most recent year?
- 2) What was the total amount of land owned by the company?
- 3) What was the total amount of cash borrowed by the company during the most recent year?
- 4) What were the types of claims that the company has against its assets?
- 5) What was the total amount of cash received by the issuance of common stock?
- 6) Was the company profitable during the most recent year?
- 7) How much cash was collected from accounts receivable during the current year?
- 8) What was the total revenue earned by the company during the most recent year?
- 9) What was the ending balance of retained earnings?
- 10) What was the amount of change in the cash balance during the current year?

133. The following events apply to Behren's Placement Agency for 2011.

- (1). Issued stock for \$14,000 cash.
- (2). On May 1, paid \$6,000 for one year's rent in advance.
- (3). Purchased on account \$500 of supplies to be used in the business.
- (4). Performed services of \$8,000 and received cash.
- (5). At December 31, an inventory of supplies showed that \$60 of supplies were still unused.
- (6). At December 31, adjusted the records for the expired rent.

Required: Draw an accounting equation and record the effects of the above events under the appropriate account headings.

Accounting Equation

Event No.	
(1).	_____
(2).	_____
(3).	_____
(4).	_____
(5).	_____
(6).	_____

134. Using the form below, record each of the following 2011 transactions for Morris Corporation:

- a) Nov. 1. Received cash from clients for services to be performed over the next six months, \$6,000.
- b) Nov. 1. Paid \$600 for a 12-month insurance policy.
- c) Dec. 31. Recorded expiration of two months of the insurance.
- d) Dec. 31. Earned \$2,000 of the amount received from clients in November.

		Assets				=	Liabilities			Equity				
Cash	+	Accts Rec.	+	Ppd. Ins.	+	Equip	=	Accts Pay	+	Unearned Rev	+	Common Stock	+	Retained Earnings
a.														
b.														
c.														
d.														

135. In a company's annual report, the reader will find a company's income statement, statement of changes in stockholders' equity, balance sheet, and statement of cash flows. These financial statements can help the reader to answer specific questions. Identify which financial statement would be most useful in answering the following questions. If more than one financial statement can answer the question, please identify all applicable statements.

- 1) What was the amount of cash dividends paid to the stockholders during the most recent year?
- 2) What was the total amount of land owned by the company?
- 3) What was the total amount of cash borrowed by the company during the most recent year?
- 4) What were the types of claims that the company had against its assets?
- 5) What was the total amount of cash received by the issuance of common stock in the current year?
- 6) Was the company profitable during the most recent year?
- 7) How much cash was collected from accounts receivable during the current year?
- 8) What was the total revenue earned by the company during the most recent year?
- 9) What was the ending balance of retained earnings?
- 10) What was the amount of change in the cash balance during the current year?

136. The following transactions apply to Fillmore Company.

- 1) Issued common stock for \$21,000 cash
- 2) Provided services to customers for \$28,000 on account
- 3) Purchased land for \$18,000 cash
- 4) Incurred \$9,000 of operating expenses on credit
- 5) Collected \$15,000 cash from customers
- 6) Paid \$7,000 on accounts payable
- 7) Paid \$2,500 dividends to stockholders

Required:

- a) Identify the effect on the Statement of Cash Flows, if any, for each of the above transactions. Indicate whether each transaction involves operating, investing, or financing activities and the amount of increase or decrease.
- b) Classify the above accounting events into one of four types of transactions (asset source, asset use, asset exchange, claims exchange).

Event	(a) Effect on Statement of Cash Flows	(b) Transaction Type
1		
2		
3		
4		
5		
6		
7		

137. Danielle McLynn started a consulting business, McLynn Consulting, on January 1, 2011, and the business engaged in the following transactions during the year:

1. Issued \$7,000 of common stock for cash
2. Provided services on account, \$25,500
3. Incurred \$11,500 of operating expense, but only paid \$5,000 of this amount
4. Collected \$9,000 of the revenue that was previously recorded on account
5. Paid a cash dividend of \$4,000 to the stockholders

Required:

- a) Show the effects of the above transactions on the accounting equation.

Assets = Liabilities + Common Stock + Retained Earnings

- 1)
- 2)
- 3)
- 4)
- 5)

- b) Prepare an income statement and statement of cash flows for 2011.

138. Pearson Company was founded in 2011 and engaged in the following transactions:

1. issued common stock for cash
2. purchased supplies on account
3. collected cash from a customer for services to be provided over a period of 1 year
4. paid a cash dividend to stockholders
5. purchased a 2-year fire insurance policy
6. provided services to customers on account
7. collected cash from accounts receivable
8. paid cash for various operating expenses
9. paid rent in advance for 3 months at a time

Required:

- a) For which of these transactions would adjusting entries be required at the end of the year?
- b) Explain the reason why adjusting entries are required before financial statements can be prepared.

139. Tom started his business by issuing \$2,000 of common stock on January 1, 2011. Tom performed \$8,000 of service on account in 2011, and he collected \$6,000 of this amount by year end. He paid operating expenses of \$4,500 and paid a \$500 dividend to the stockholders.

Required:

- a) What is the amount of total assets at the end of 2011?
- b) What is the amount of cash on hand at the end of 2011?
- c) What is the net income for 2011?
- d) Prepare a balance sheet for 2011.

140. The effects of transactions occurring during 2011 and their related end-of-year adjustments have been recorded below using the accounting equation.

	Cash	+	Accts Recv.	+	Prepaid Insurance	+	Land	=	LIABILITIES	+	Unearned Revenue	+	EQUITY	+	Retained Earnings
								=	Accts Payable				Cont. Capital		
1.	+20,000												+20,000		
2.	-5,000						+5,000								
3.			+12,000												+12,000
4.	+8,000										+8,000				
5.	+8,000		-8,000												
6.	-1,200				+1,200										
7.								+6,000							-6,000
8.	+5,000						-5,000								
9.					-1,000										-1,000
10.											-5,000				+5,000
Totals	<u>34,800</u>		<u>4,000</u>		<u>200</u>		<u>0</u>		<u>6,000</u>		<u>3,000</u>		<u>20,000</u>		<u>10,000</u>

Required:

With your knowledge of transaction analysis using an accounting equation,

- Prepare an income statement for 2011, and
- Prepare a statement of cash flows for 2011.

Chapter 02 - Understanding the Accounting Cycle

141. Pocono Corporation began business operations and experienced the following transactions during 2011:

- 1) Issued common stock for \$10,000 cash.
- 2) Provided services to customers for \$40,000 on account.
- 3) Incurred \$18,000 of operating expenses on account.
- 4) Collected \$23,000 cash from customers.
- 5) Paid \$15,000 on accounts payable.

Required:

Record the above transactions on a horizontal statements model to reflect their effect on Pocono's financial statements.

Event	Cash	+	Accounts Rec.	=	Accounts Pay	+	Common Stock	+	Retained Earnings	Cash Flows
1										
2										
3										
4										
5										
Totals										

142. Indicate for each of the following items if the item would be reported on the income statement (IS), statement of changes in equity (CE), balance sheet (BS), or statement of cash flows (CF). Some items may appear on more than one statement, if so, identify all applicable statements.

- 1) Prepaid insurance
- 2) Dividends paid to stockholders
- 3) Interest revenue
- 4) Accounts payable
- 5) Salaries expense
- 6) Amount of retained earnings at the end of the accounting period
- 7) Unearned subscription revenue
- 8) Cash flows from operating activities
- 9) Beginning common stock
- 10) Issued stock to investors for cash
- 11) Salaries payable
- 12) Accounts receivable

143. Classify each of the following transactions for the purpose of the statement of cash flows as operating activities (OA), investing activities (IA), financing activities (FA), or not reported on the statement of cash flows (NA).

- 1) ____ Made adjusting entry to accrue salary expense at the end of the year
- 2) ____ Borrowed funds from the bank
- 3) ____ Paid rent for the month
- 4) ____ Paid cash to settle accounts payable
- 5) ____ Issued common stock for \$30,000 cash
- 6) ____ Collected accounts receivable
- 7) ____ Paid cash to acquire land

144. Tuttle Company shows the following transactions for the accounting period ending December 31, 2011:

- 1) Sold books to customers for \$34,000 on account
- 2) Collected \$28,000 from customers
- 3) Issued common stock for \$8,000 cash
- 4) Prepaid four months rent for \$4,400 on October 1, 2011
- 5) Purchase supplies for \$10,500 cash
- 6) Physical count shows \$3,250 of supplies left over on December 31, 2011
- 7) Recorded adjustment for prepaid rent used

Show how the above transactions and year end adjustments affect the financial statements on the accounting equation:

	Accts. Rec. +	Ppd. Rent +	Supplies	=	Common Stock +	Retained Earnings
1)						
2)						
3)						
4)						
5)						
6)						
7)						

145. For each of the following transactions, indicate the type by entering "AS" for asset source transaction, "AU" for asset use transaction, "AE" for asset exchange transaction, and "CE" for claims exchange transaction.

- 1) ___ The company paid \$10,000 for a plot of land.
- 2) ___ Recorded the accrual of \$1,000 in salaries to be paid later.
- 3) ___ The company issued common stock for \$20,000 in cash.
- 4) ___ The business incurred operating expense on account.
- 5) ___ The business paid off its accounts payable.
- 6) ___ The business earned revenue to be collected next year.
- 7) ___ The company paid \$2,000 in dividends to its stockholders.
- 8) ___ The business received cash from customers in #6 above.
- 9) ___ Paid the salaries accrued in #2 above.
- 10) ___ Borrowed money from a local bank.

146. Tell whether each of the following events are asset source (AS), asset use (AU), asset exchange (AE), or claims exchange (CE) transactions.

- ___ 1) Issued common stock to investors for \$8,000 cash
- ___ 2) Paid one year's rent in advance
- ___ 3) Provided services to customers and received \$35,000 cash
- ___ 4) Paid creditors \$10,000
- ___ 5) Received \$3,000 of revenue in advance
- ___ 6) Provided services to customers on account, \$12,000
- ___ 7) Collected \$2,000 from accounts receivable
- ___ 8) Recognized accrued salary expense of \$2,000
- ___ 9) Borrowed \$6,000 from creditors
- ___ 10) Adjusted the records for supplies used of \$800

Chapter 02 Understanding the Accounting Cycle **Answer Key**

Short Answer Questions

Indicate how each event affects the elements of financial statements. Use the following letters to record your answer in the box shown below each element. You do not need to enter amounts.

Increase = I Decrease = D No Effect = N

1. Frank Co. performed services for customers on account.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

(I) (N) (I) (I) (N) (I) (N)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

Chapter 02 - Understanding the Accounting Cycle

2. Gonzales Co. collected \$1,000 cash from accounts receivable.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

(N) (N) (N) (N) (N) (N) (I)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

3. Sanchez Co. provided \$800 of services for a customer who paid \$500 cash immediately and promised to pay an additional \$300 one month later.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

(I) (N) (I) (I) (N) (I) (I)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

Chapter 02 - Understanding the Accounting Cycle

4. Albertson Co. purchased a \$3,000 machine for cash.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

(N) (N) (N) (N) (N) (N) (D)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

5. At the end of the accounting period, Snyder Co. recognized accrued salaries.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

(N) (I) (D) (N) (I) (D) (N)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

Chapter 02 - Understanding the Accounting Cycle

6. At the end of the accounting period, Lantz Co. accrued \$600 of interest revenue on an interest earning account.

Assets	Liabilities	Equity	Revenues	Expenses	Net Income	Cash

(I) (N) (I) (I) (N) (I) (N)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

7. When is revenue recognized under accrual accounting?

Revenue is recognized when it is earned; i.e. when the services are performed.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

8. What does the balance in accounts receivable represent?

The balance in accounts receivable represents the amount of future cash receipts that is due from customers. In other words, it is the amount to be collected from customers who previously received goods or services on account.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

9. When are expenses recognized under accrual accounting in relation to the payment of cash?

Expenses are recognized when they are incurred, regardless of when cash is paid. In accrual transactions, that means that expenses are recorded before cash payments, and in deferral transactions they are recorded after cash payments.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

10. What is the effect on the accounting equation of a cash payment to creditors?

Assets decrease; liabilities decrease

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

11. Why are adjusting entries necessary in an accrual accounting system? What are some common examples?

Adjusting entries are necessary in order to recognize revenues and expenses that should be recognized in the current year, but have not yet been recorded. Some common adjusting entries include recognizing accrued salaries expense, accrued interest revenue, and accrued expense, such as prepaid rent.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 2

12. What effect does the recording of revenue normally have on total assets?

The recording of revenue normally has the effect of increasing total assets (usually cash or accounts receivable).

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 2

13. What effect does providing services on account have on the statement of cash flows? The balance sheet?

There is no effect on the statement of cash flows when services are performed on account. Assets and equity will increase on the balance sheet.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 3

14. Describe the purpose of the closing process.

The purpose of the closing process is to bring the balance of the nominal (temporary) accounts to zero at the end of an accounting period and to update the retained earnings account.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

15. Describe the difference between temporary and permanent accounts, and state which ones are closed.

Temporary (nominal) accounts collect information about a single period only; they are closed at the end of that period. Permanent accounts include the balance sheet accounts (assets, liabilities, common stock and retained earnings), and their balances roll forward each year rather than being closed out.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

16. Define the accounting cycle and list the stages of the cycle.

The accounting cycle is a series of steps or procedures that occur repeatedly throughout the life of a business. The three stages described to this point in the course include (1) recording transactions, (2) preparing statements and (3) closing temporary accounts.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

17. Explain the meaning of the term, "matching concept."

The "matching concept" refers to the process of "matching" the expenses with the revenues that they produce in the appropriate time period. This matching is largely done through the adjusting process. For example, the accrual of salary expense has the effect of matching the correct portion of salary expense to the accounting period in which the employees contributed to producing revenue. Matching means that expenses should be recognized in the same accounting period as the revenues that they helped a business to earn.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

18. The temporary or nominal accounts are closed prior to the start of the next accounting cycle. In this closing process, the amounts in each of these accounts are transferred to what other account(s)?

Retained Earnings

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Knowledge
Difficulty: Easy
Learning Objective: 5

19. What is meant by the "fraud triangle"?

Auditors have identified three elements that are commonly present in instances of criminal and ethical misconduct. The first of these elements is the availability of opportunity. The second is the existence of some kind of pressure leading to an incentive. The third is the capacity to rationalize the behavior. These three elements are often shown in the form of a triangle.

AACSB: Analytic, Communications, Ethics
AICPA BB: Legal
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 7

20. Discuss the importance of ethics in the accounting profession.

Because the users of accounting information depend on that information for making decisions, auditors must be trustworthy and credible. The management of a business is ultimately responsible for the financial statements; therefore, the accounting personnel of the business must also conduct themselves in a highly ethical manner.

AACSB: Analytic, Communications, Ethics
AICPA BB: Industry
AICPA FN: Decision Making
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 7

Multiple Choice Questions

21. Bledsoe Company received \$5,000 cash from the issue of stock on January 1, 2011. During 2011 Bledsoe earned \$8,500 of revenue on account. The company collected \$6,000 cash from accounts receivable and paid \$5,400 cash for operating expenses. Based on this information alone, during 2011,

- A. Total assets increased by \$14,100.
- B. Total assets increased by \$600.
- C. Total assets increased by \$8,100.**
- D. Total assets did not change.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

22. Aaronson Company experienced an accounting event that affected its financial statements as indicated below:

Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
+		NA		+	+		NA		+	NA

Which of the following accounting events could have caused these effects on ABC's statements?

- A. Issued common stock.
- B. Purchased equipment on account.
- C. Earned revenue on account.**
- D. Recognized accrued salaries owed to employees.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

23. Which of the following choices accurately reflects how the recording of accrued salary expense affects a business's financial statements?

	Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
A.	NA	=	+	+	-	-	-	+	=	NA	NA
B.	NA	=	NA	+	+ -	NA	-	NA	=	NA	NA
C.	NA	=	+	+	-	NA	-	+	=	-	NA
D.	+	=	+	+	NA	NA	-	+	=	-	-OA

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Comprehension
 Difficulty: Medium
 Learning Objective: 1

24. Which of the following transactions does **not** involve an accrual?

- A. Recording interest earned that will be received in the next period.
- B. Recording operating expense incurred but not yet paid.
- C. Recording salary expense incurred but not yet paid.
- D.** Recording the pre-payment of two year's worth of insurance.

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Comprehension
 Difficulty: Hard
 Learning Objective: 1

25. Sakimoto Company recorded salaries earned by employees but not yet paid. Which of the following represents the effect of this transaction on the financial statements?

	Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
A.	+	=	+	+	NA	+	-	NA	=	+	- OA
B.	NA	=	+	+	-	NA	-	+	=	-	- IA
C.	-	=	NA	+	-	NA	-	+	=	-	NA
<u>D.</u>	NA	=	+	+	-	NA	-	+	=	-	NA

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Comprehension
 Difficulty: Medium
 Learning Objective: 1

26. Revenue on account amounted to \$5,000. Cash collections of accounts receivable amounted to \$2,300. Expenses for the period were \$2,100. Net income for the period was

- A. \$200.
- B. \$350.
- C. \$3,050.
- D.** \$2,900.

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Comprehension
 Difficulty: Medium
 Learning Objective: 1

27. The recognition of an expense may be accompanied by which of the following?

- A. An increase in assets
- B. A decrease in liabilities
- C. A decrease in revenue
- D.** An increase in liabilities

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Comprehension
 Difficulty: Medium
 Learning Objective: 1

28. Which of the following statements is true in regard to accrual accounting?

- A. Revenue is recorded only when cash is received.
- B. Expenses are recorded when they are incurred.
- C. Revenue is recorded in the period when it is earned.
- D.** Both B and C.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

29. The term "realization" refers to which of the following?

- A. The closing of an account.
- B.** The collection of cash.
- C. The earning of revenue.
- D. The correction of an error.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

30. Which of the following events involves a deferral?

- A. Recording interest that has been earned but not received.
- B.** Recording supplies that have been purchased with cash but not yet used.
- C. Recording revenue that has been earned but not yet collected in cash.
- D. Recording salaries owed to employees at the end of the year that will be paid during the following year.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

31. Recognition of revenue **may** result in which of the following?

- A. A decrease in a liability.
- B. An increase in a liability.
- C. An increase in assets.
- D.** A. and C.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Hard
Learning Objective: 1

32. Mobley Company provided \$25,500 of services on account, and collected \$18,000 from customers during the year. The company also incurred \$17,000 of expenses on account, and paid \$15,400 against its payables. As a result of these events,

- A. total assets would increase
- B. total liabilities would increase
- C. total equity would increase
- D.** all of the above are correct

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Hard
Learning Objective: 1

33. Which of the following events would **not** require an end-of-year adjusting entry?

- A. Purchasing supplies for cash
- B.** Providing services on account
- C. Purchasing a 12-month insurance policy on July 1
- D. All of the above would require an end-of-year adjustment

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Hard
Learning Objective: 2

34. The entry to recognize work completed on deferred revenue involves which of the following?

- A. An increase in assets and a decrease in liabilities
- B. An increase in liabilities and a decrease in equity
- C. A decrease in assets and a decrease in liabilities
- D.** A decrease in liabilities and an increase in equity

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 2

35. Jordan Snow Removal Company received a cash advance of \$6,000 on December 1, 2011 to provide services during the months of December, January, and February. The year-end adjustment to recognize the partial expiration of the contract will

- A.** increase equity by \$2,000
- B. increase assets by \$2,000
- C. increase liabilities by \$2,000
- D. both A and B

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 2

36. The entry to recognize salary expense incurred but not yet paid involves which of the following?

- A. An increase in assets
- B.** An increase in liabilities
- C. A decrease in assets
- D. A decrease in liabilities

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 2

Chapter 02 - Understanding the Accounting Cycle

37. The following accounts and balances were drawn from the records of Jared Company:

Cash	\$8,000
Accounts Payable	\$5,500
Common Stock	\$4,000
Land	\$18,000
Accounts Receivable	\$2,000

Based on this information alone the amount of Jared's retained earnings is

- A. \$9,500.
- B. \$18,500.**
- C. \$15,500.
- D. \$22,500.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 3

The following account balances were drawn from the 2011 financial statements of Gwynn Company

Cash	\$2,200	Certificate of Deposit	\$500
A/R	750	Common Stock	?
Land	600	Retained Earnings	2,800
		Revenues	5,100
		Expenses	2,450

38. Based on the above information, what is the balance of Common Stock for Gwynn Company?

- A. \$750
- B. \$1,250**
- C. \$3,400
- D. \$6,200

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 3

39. Based on the above information, what was the beginning balance (on January 1, 2011) in retained earnings for Gwynn Company?

- A. \$2,650
- B. \$3,400
- C. \$150**
- D. \$450

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Hard
Learning Objective: 3

40. Smith Company loaned Jones Company \$10,000 cash. The loan carried a two-year term. In the year that the loan was made,

- A. Jones Company's assets would decrease.
- B. Smith Company would show a cash outflow in the investing activities section of its cash flow statement.**
- C. Smith Company's liabilities would increase.
- D. Jones Company would show a cash inflow in the operating activities section of its cash flow statement.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 3

41. During 2011, Davis Company purchased land costing \$2,400 cash. The company earned \$2,000 revenue on account and incurred \$1,100 of operating expenses for which cash was paid. As a result of these transactions,
- A. total assets increased by \$2,400.
 - B.** total assets increased by \$900.
 - C. total liabilities increased by \$1,100.
 - D. none of these.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 3

42. The balance sheet of Vargas Company shows retained earnings of \$50,000, total liabilities of \$30,000, and common stock \$10,000. Based on this information, you would know that
- A. the amount of ownership claims cannot be determined.
 - B.** since the company began, the total amount of net income exceeded total dividends by \$50,000.
 - C. the company obtained most of its assets through borrowing activities.
 - D. Vargas Company has enough cash to pay off its liabilities.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 3

43. The Bloom Company issued stock for \$50,000 cash on January 20, 2011. During 2011, the company recorded revenue on account of \$18,000 and expenses for which cash was paid of \$10,000. Bloom received \$10,200 cash from accounts receivable. The company also purchased land for \$6,000 cash. Based on this information, the amount of change in cash for 2011 was
- A. \$62,200
 - B. \$44,200**
 - C. \$50,200
 - D. \$54,200

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 3

44. On December 31, the balance sheet of the Falcon Company contained the following accounts and balances:

Cash	\$500	Certificate of Deposit	\$600
Equipment	\$1,250	Common Stock	?
Accounts Payable	\$500	Retained Earnings	\$850

Based on the above information, the balance in Common Stock must be what amount?

- A. \$0
- B. \$250
- C. \$1,000**
- D. \$1,100

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 3

45. Which of the following would be included in the "cash flow from operating activities" section of the statement of cash flows?

- A. Accrual of salary expense at year-end.
- B.** Cash received from on an interest earning account.
- C. Payments of cash dividends to the owners of the business.
- D. Purchase of land for cash.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Knowledge
Difficulty: Medium
Learning Objective: 4

46. Revenue on account amounted to \$3,000. Cash collections of accounts receivable amounted to \$2,700. Cash paid for expenses was \$2,500. The amount of employee salaries accrued at the end of the year was \$300. Cash flow from operating activities was

- A.** \$200.
- B. \$300.
- C. \$500.
- D. None of these.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

47. Which of the following accounts would **not** appear on a balance sheet?

- A. Unearned Revenue.
- B. Salaries Payable.
- C.** Interest Revenue.
- D. Retained Earnings.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Knowledge
Difficulty: Easy
Learning Objective: 4

48. Common Stock would appear on which of the following financial statements?

- A. Income statement
- B. Balance sheet
- C. Statement of changes in stockholders' equity
- D.** Both B and C

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Knowledge
Difficulty: Medium
Learning Objective: 4

49. Woodward Enterprises had the following events during 2011:

The business issued \$20,000 of common stock to its stockholders.

The business purchased land for \$12,000 cash.

Services were provided to customers for \$16,000 cash.

Services were provided to customers for \$6,000 on account.

The company borrowed \$16,000 from the bank.

Operating expenses of \$12,000 were incurred and paid in cash.

Salary expense of \$800 was accrued.

A dividend of \$4,000 was paid to the owners of Woodward Enterprises.

Assuming the company began operations during 2011, the amount of retained earnings as of December 31, 2011 would be:

- A.** \$5,200
- B. \$6,000
- C. \$10,000
- D. \$22,000

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

50. Which of the following would cause net income on the accrual basis to be different (either higher or lower) than "cash provided by operating activities" on the statement of cash flows?

- A. Acquired \$10,000 cash from the owners.
- B.** Incurred operating expenses on account.
- C. Provided services to a customer for cash.
- D. Purchased land for cash.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

51. Which of the following would cause net income on the accrual basis to be different than (either higher or lower than) "cash provided by operating activities" on the statement of cash flows?

- A.** Accrued interest earned on an interest earning account.
- B. Paid a cash dividend to the stockholders.
- C. Invested cash in an interest earning account.
- D. Purchased land for cash.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

52. Ruiz Company provided services for \$15,000 cash during the 2011 accounting period. Ruiz incurred \$12,000 expenses on account during 2011, and by the end of the year, \$3,000 of that amount had been paid with cash. Assuming that these are the only accounting events that affected Ruiz during 2011,

- A.** The amount of net income shown on the income statement is \$3,000.
- B. The amount of net income shown on the income statement is \$9,000.
- C. The amount of net loss shown on the income statement is \$3,000.
- D. The amount of net cash flow from operating activities shown on the statement of cash flows is \$6,000.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Easy
Learning Objective: 4

The following accounts and balances were drawn from the records of Hoover Company on December 31, 2011:

Cash	\$1,000	Accounts Receivable	\$850
Dividends	500	Common Stock	975
Land	800	Revenue	800
Accounts Payable	450	Expense	550

53. Total assets on the December 31, 2011 balance sheet would amount to:

- A. \$3,150.
- B. \$3,450.
- C. \$1,800.
- D.** \$2,650.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting, Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

54. The amount of net income shown on the December 31, 2011 income statement would amount to:

- A. \$550.
- B. \$800.
- C. \$50.
- D.** \$250.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting, Measurement
Bloom's: Analysis
Difficulty: Easy
Learning Objective: 4

55. The amount of retained earnings as of January 1, 2011 was:

- A.** \$1,475.
- B. \$1,800.
- C. \$1,050.
- D. \$1,225.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting, Measurement
Bloom's: Analysis
Difficulty: Hard
Learning Objective: 4

Norris Company experienced the following transactions during 2011, its first year in operation.

1. Issued \$6,000 of common stock to stockholders.
2. Provided \$2,400 of services on account.
3. Paid \$1,600 cash for operating expenses.
4. Collected \$1,800 of cash from accounts receivable.
5. Paid a \$100 cash dividend to stockholders.

Chapter 02 - Understanding the Accounting Cycle

56. The amount of net income recognized on Norris Company's 2011 income statement is:

- A. \$500.
- B. \$400.
- C. \$800.**
- D. \$600.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement, Reporting
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

57. The amount of net cash flow from operating activities shown on Norris Company's 2011 statement of cash flows is

- A. \$200.**
- B. \$300.
- C. \$800.
- D. \$400.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement, Reporting
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

58. The total amount of assets shown on Norris Company's 2011 balance sheet is

- A. \$6,200.
- B. \$6,800.
- C. \$6,700.**
- D. None of these.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement, Reporting
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

Chapter 02 - Understanding the Accounting Cycle

59. The amount of retained earnings appearing on Norris Company's 2011 balance sheet is:

- A. \$200.
- B. \$700.**
- C. \$800.
- D. \$6,700.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement, Reporting
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

60. On December 31, 2011, Preston Co. owed \$1,200 in salaries to employees who had worked during December but would be paid in January. If the year-end adjustment is properly recorded on December 31, 2011, what will be the effect of the accrual on the following items for Preston?

	Net Income	Cash Flow from Operating Activities
a.	No effect	No effect
b.	Decrease	Decrease
c.	Increase	No effect
d.	No effect	Increase

- A. Option A
- B. Option B
- C. Option C**
- D. Option D

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 4

61. Tocca Co. collected a \$5,000 cash advance from a customer on November 1, 2011 for work to be performed over a six-month period beginning on that date.. If the year-end adjustment is properly recorded, what will be the effects of the accrual on Tocca's 2011 financial statements?
- A. Increase assets and increase liabilities
 - B. Increase assets and increase revenues
 - C. Decrease liabilities and increase revenues**
 - D. No effect

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 4

62. Natchez Company collected \$9,000 on September 1, 2011 from a customer for services to be provided over a one-year period beginning on that date. How much revenue would Natchez Company report related to this contract on its income statement for the year ended December 31, 2011? How much would it report as cash flows from operating activities for 2011?
- A. \$3,000; \$3,000
 - B. \$3,000; \$9,000**
 - C. \$9,000; \$9,000
 - D. \$0; \$9,000

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement, Reporting
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 4

63. The matching concept refers to the "matching" of:
- A. expenses and liabilities
 - B. expenses and revenues**
 - C. assets and equity
 - D. assets and liabilities

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5

64. The results of the matching process are best reported on which financial statement?

- A. Balance sheet
- B. Income statement**
- C. Statement of changes in stockholders' equity
- D. Statement of cash flows

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

65. Expenses that are matched with the period in which they are incurred are frequently called:

- A. market expenses
- B. matching expenses
- C. period costs**
- D. working costs

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5

66. If retained earnings decreased during the year, and no dividends were paid, which of the following must be true?

- A. Expenses for the year exceeded revenues**
- B. The company did not have enough cash to pay its expenses
- C. Total equity decreased
- D. Liabilities increased during the year

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Medium
Learning Objective: 5

67. Which of the following correctly states the proper order of the accounting cycle?
- A.** Record transactions, adjust accounts, prepare statements, close temporary accounts.
 - B. Adjust accounts, record transactions, close temporary accounts, prepare statements.
 - C. Prepare statements, record transactions, close temporary accounts, adjust accounts.
 - D. Adjust accounts, prepare statements, record transactions, close temporary accounts.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

68. The purpose of the accrual basis of accounting is to:
- A. Report revenue when received.
 - B.** Improve the matching of revenue and expense in the proper period.
 - C. Report expenses when cash disbursements are made.
 - D. Improve the company's earnings per share.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

69. Which of the following financial statement elements is closed at the end of an accounting cycle?
- A. Liabilities
 - B. Common stock
 - C. Assets
 - D.** Revenues

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5

70. Which of the following accounts is **not** closed at the end of an accounting cycle?

- A.** Liabilities
- B. Revenues
- C. Dividends
- D. Expenses

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

71. Which of the following financial statement elements contain cumulative information rather than information for the current period only?

- A. Dividends
- B. Revenues
- C. Expenses
- D.** Retained Earnings

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

72. The balance in a revenue account at the beginning of an accounting period will always be

- A. equal to the amount of retained earnings for the previous period.
- B. last period's ending balance.
- C. higher than the previous periods beginning balance.
- D.** zero.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

73. The accounting principle that guides accountants, when faced with a recognition dilemma, to choose the alternative that produces the lowest net income is referred to as

- A. the matching principle.
- B. internal control.
- C. conservatism.**
- D. materiality.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

74. Which of the following is **not** a component of the fraud triangle?

- A. Opportunity
- B. Rationalization
- C. Trust**
- D. Pressure

AACSB: Ethics
AICPA BB: Legal, Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 7

75. If a CPA voluntarily discloses information acquired from a client, he or she may be in violation of which of the following principles?

- A. Confidentiality**
- B. Conservatism
- C. Materiality
- D. Objective evidence

AACSB: Ethics
AICPA BB: Critical Thinking
AICPA FN: Decision Making
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 7

76. Which of the following is **not** a common feature of ethical misconduct?

- A. The capacity to rationalize.
- B. The existence of pressure leading to an incentive.
- C.** The existence of a strong system of internal controls.
- D. The presence of an opportunity.

AACSB: Ethics
AICPA BB: Critical Thinking
AICPA FN: Decision Making
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 7

77. Policies and procedures designed to reduce the opportunities for fraud are often called:

- A. accounting principles
- B. asset source transactions
- C.** internal controls
- D. financial systems

AACSB: Ethics
AICPA BB: Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 7

78. What action did the U. S. Congress take because of the audit failures at Enron, WorldCom and other companies?

- A. Required publicly-traded companies to be audited by a government agency
- B. Required companies to begin preparing an additional financial statement
- C.** Passed the Sarbanes-Oxley Act
- D. Passed an amendment to the Securities and Exchange Act

AACSB: Reflective Thinking
AICPA BB: Legal, Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Knowledge
Difficulty: Easy
Learning Objective: 7

79. Which of the following describes the effects of a claims exchange transaction on a company's financial statements?

	Assets	=	Liab.	+	Equity	Rev.	-	Exp.	=	Net Inc.	Cash Flow
A.	NA	=	NA	+	NA	NA	-	NA	=	NA	+ OA
B.	+	=	+	+	NA	NA	-	NA	=	NA	+ OA
C.	NA	=	+	+	-	NA	-	+	=	-	NA
D.	All of these could represent the effects of a claims exchange transaction.										

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Application
 Difficulty: Medium
 Learning Objective: 6

80. Which of the following is an asset source transaction?

- A.** Issued common stock.
- B. Paid a cash dividend to stockholders.
- C. Invested cash in an interest earning account.
- D. Accrued salary expense.

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Comprehension
 Difficulty: Medium
 Learning Objective: 6

81. Which of the following is an asset use transaction?

- A. Purchased machine for cash.
- B.** Paid a cash dividend to stockholders.
- C. Invested cash in an interest earning account.
- D. Accrued salary expense.

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Application
 Difficulty: Medium
 Learning Objective: 6

82. Which of the following is a claims exchange transaction?

- A. Purchased machine for cash.
- B. Paid a cash dividend to stockholders.
- C. Invested cash in an interest earning account.
- D.** Accrued salary expense.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6

83. Which of the following is an asset exchange transaction?

- A. Issued common stock.
- B. Accrued salary expense at the end of the accounting period.
- C. Paid cash dividends to stockholders.
- D.** Invested cash in an interest earning account.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6

84. An increase in cash that is accompanied by an increase in common stock is a/an

- A. claims exchange transaction.
- B.** asset source transaction.
- C. asset use transaction.
- D. asset exchange transaction.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6

85. Which of the following is an example of a claims exchange transaction?

- A. An asset decreases and an equity account decreases.
- B. An asset increases and another asset decreases.
- C.** A liability increases and an equity account decreases.
- D. A liability increases and an equity account also increases.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6

Essay Questions

86. Kelly Company uses accrual accounting. Indicate whether each of the following statements regarding Kelly's accounting system is true or false.

- _____ a) The recognition of accounting events and the realization of cash consequences may occur in different accounting periods.
- _____ b) The cash consequence of a transaction always precedes its accounting recognition.
- _____ c) Recognition is an act of recording an event in the financial statements.
- _____ d) The term accrual applies to events that are recognized after the associated cash is paid or collected.
- _____ e) Kelly is not permitted to make cash sales.

a) T b) F c) T d) F e) F

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1

87. Whitmore Co. performed services for a customer on account. Indicate whether each of the following statements about this transaction is true or false.

- a) Assets and equity both increase when the revenue is recognized.
- b) This transaction did not affect cash flows.
- c) The company recorded an increase in revenue and a decrease in accounts receivable.
- d) Recognition of revenue would be delayed until cash was received.
- e) This transaction is an example of an asset source transaction.

a) T b) T c) F d) F e) T

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1 and 6

88. Dandridge Company collected cash in 2011 from a customer for services to be performed beginning January 2012. Indicate whether each of the following statements about this transaction is true or false.

- a) Dent's 2011 income statement would not be affected by this transaction.
- b) Dent's 2011 statement of cash flows would be affected by this transaction.
- c) This transaction is an asset exchange transaction.
- d) The revenue for the services provided will be recorded in 2012.
- e) This transaction is considered an accrual transaction.

a) T b) T c) F d) T e) F

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting, Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1 and 6

89. Regarding the relationships of revenues and expenses to assets and liabilities, state whether each of the following statements is true or false.

_____ a) Recording an increase in a revenue account may be associated with an increase in assets.

_____ b) Recording an increase in a revenue account may be associated with a decrease in liabilities.

_____ c) An increase in Salaries Expense may be accompanied by a decrease in Salaries Payable.

_____ d) Recording a decrease in assets may be associated with an increase in an expense account.

_____ e) Recording an increase in an expense may be associated with a decrease in a revenue account.

a) T b) T c) F d) T e) F

AACSB: Reflective Thinking, Analytic

AICPA BB: Critical Thinking

AICPA FN: Measurement

Bloom's: Comprehension

Difficulty: Medium

Learning Objective: 4

90. Wilgus Company paid \$57,000 in January 2012 for salaries that had been earned by employees in December 2011. Indicate whether each of the following statements about financial statement effects of the January 2012 event is true or false.

_____ a) The income statement for 2012 is not affected because the salaries expense had been recognized at the end of December.

_____ b) On the 2012 statement of cash flows, cash flows from operating activities decreased.

_____ c) Payment of the salaries in 2012 decreased a liability.

_____ d) The statement of changes in stockholders' equity would not be affected because the salaries expense had been recognized at the end of December.

_____ e) Both assets and equity decreased as a result of this transaction.

a) T b) T c) T d) T e) F

AACSB: Analytic

AICPA BB: Critical Thinking

AICPA FN: Measurement, Reporting

Bloom's: Application

Difficulty: Medium

Learning Objective: 4 and 5

Chapter 02 - Understanding the Accounting Cycle

91. Indicate whether each of the following statements about the closing process and the accounting cycle is true or false.

_____ a) The closing process transfers certain account balances to retained earnings at the end of the accounting cycle.

_____ b) Only accounts that appear on the income statement are closed at the end of each accounting cycle.

_____ c) Another name for permanent accounts is "nominal accounts."

_____ d) The permanent accounts contain information that is cumulative in nature.

_____ e) The retained earnings balance at the end of any given year is equal to that year's net income.

a) T b) F c) F d) T e) F

AACSB: Reflective Thinking, Analytic

AICPA BB: Critical Thinking

AICPA FN: Measurement

Bloom's: Comprehension

Difficulty: Medium

Learning Objective: 5

92. Regarding the effects of end-of-period adjustments, state whether each of the following statements is true or false.

_____ a) Recording the usage of supplies involves a decrease in assets and a decrease in equity.

_____ b) The accrual of salaries is considered a claims exchange transaction.

_____ c) Recording services performed on a prepaid contract involves a decrease in liabilities and an increase in assets.

_____ d) End of period adjustments never affect cash flows.

_____ e) Failure to record accrued at the end of the year will cause reported income to be higher than it should have been.

a) T b) T c) F d) T e) T

AACSB: Reflective Thinking, Analytic

AICPA BB: Critical Thinking

AICPA FN: Measurement

Bloom's: Analysis

Difficulty: Medium

Learning Objective: 2

93. Indicate whether each of the following statements regarding the four types of accounting events is true or false.

- _____ a) Asset use transactions involve an increase in one asset and a decrease in another asset.
- _____ b) An asset source transaction involves an increase in assets and an increase in a corresponding claims account.
- _____ c) An asset exchange transaction involves an increase in an asset and a decrease in a claims account.
- _____ d) Asset exchange transactions involve an increase in one asset and a decrease in another asset.
- _____ e) Some claims exchange transactions involve an increase in a liability account and a decrease in an equity account.

a) F b) T c) F d) T e) T

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1

94. Indicate whether each of the following statements about corporate governance is true or false.

- _____ a) The Financial Accounting Standards Board issues a code of ethical behavior by which public accountants must abide.
- _____ b) The Sarbanes Oxley Act created the Public Company Accounting Oversight Board (PCAOB).
- _____ c) Because of the Sarbanes Oxley Act, many audit firms now provide nonaudit services to audit clients.
- _____ d) The fraud triangle identifies opportunity, pressure, and rationalization as the three elements that are typically present when fraud is committed.
- _____ e) An executive found guilty of falsely certifying a company's financial statements faces up to a \$5 million fine and 20 years in prison.

a) F b) T c) F d) T e) T

AACSB: Reflective Thinking
AICPA BB: Legal
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 7

Chapter 02 - Understanding the Accounting Cycle

True / False Questions

95. The term "recognition" means to report an economic event in the financial statements.

TRUE

*AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Knowledge
Difficulty: Easy
Learning Objective: 1*

96. Companies that use accrual accounting recognize revenues and expenses at the time that cash is paid or received.

FALSE

*AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1*

97. The term "accrual" describes an earnings event that is recognized after cash is paid or received.

FALSE

*AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1*

98. A company may recognize a revenue or expense without a corresponding cash collection or payment in the same accounting period.

TRUE

*AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1*

99. A payment to an employee in settlement of salaries payable decreases an asset and decreases a liability.

TRUE

*AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1*

100. An increase in an expense may be accompanied by an increase in a liability.

TRUE

*AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 1 and 3*

101. Revenues and liabilities are temporary accounts.

FALSE

*AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5*

102. In the closing process, the amounts in temporary accounts are moved to retained earnings, a permanent account.

TRUE

AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5

103. Accounts that are closed include expenses, dividends, and unearned revenues.

FALSE

AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

104. After closing, only balance sheet accounts have non-zero balances.

TRUE

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

105. Two of the steps in the accounting cycle are adjusting the accounts and closing the accounts.

TRUE

AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5

Chapter 02 - Understanding the Accounting Cycle

106. Cash-basis accounting often fails to match expenses with revenues.

TRUE

AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 5

107. The matching concept leads accountants to select the recognition alternative that produces the lowest amount of net income.

FALSE

AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

108. Adjusting entries never affect a business's cash account.

TRUE

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 5

109. Asset use transactions always involve the payment of cash.

FALSE

AACSB: Reflective Thinking, Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 6

110. The governance of a corporation includes the roles and responsibilities of the board of directors, managers, shareholders, and auditor.

TRUE

AACSB: Reflective Thinking
AICPA BB: Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 8

111. The ethical standards for certified public accountants simply require that such accountants comply with applicable laws and regulations.

FALSE

AACSB: Reflective Thinking, Ethics
AICPA BB: Critical Thinking
AICPA FN: Decision Making
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 8

112. Certified public accountants are obligated to act in a way that serves the public interest.

TRUE

AACSB: Reflective Thinking, Ethics
AICPA BB: Critical Thinking
AICPA FN: Decision Making
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 8

113. The bankruptcies of Enron and WorldCom both indicated the occurrence of major audit failures.

TRUE

AACSB: Reflective Thinking, Ethics
AICPA BB: Legal, Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 8

114. The Sarbanes-Oxley Act includes several significant reforms that affect the auditing profession, but it did not reduce an audit firm's ability to provide non-audit services to its audit clients.

FALSE

AACSB: Analytic, Ethics
AICPA BB: Legal, Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 8

115. A business's internal controls are designed to reduce the probability of occurrence of fraud.

TRUE

AACSB: Reflective Thinking, Ethics
AICPA BB: Critical Thinking
AICPA FN: Risk Analysis
Bloom's: Comprehension
Difficulty: Easy
Learning Objective: 8

116. Providing services to customers on account is an asset source transaction.

TRUE

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Easy
Learning Objective: 6

117. An adjusting entry that decreases unearned revenue and increases service revenue is a claims exchange transaction.

TRUE

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6

118. Sometimes the recognition of revenue is accompanied by an increase in liabilities.

FALSE

*AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6*

119. The collection of an account receivable is a claims exchange transaction.

FALSE

*AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6*

120. An adjusting entry to accrue salary expense is a claims exchange transaction.

TRUE

*AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 6*

Essay Questions

121. Horizon Corporation began business operations and experienced the following transactions during 2011:

- 1) Issued common stock for \$10,000 cash.
- 2) Provided services to customers for \$25,000 on account.
- 3) Purchased \$500 of supplies on account.
- 4) Paid \$6,000 cash to rent office space for a 12-month period beginning June 1.
- 5) Collected \$23,000 cash from customers.
- 6) Paid cash for \$18,000 of operating expenses.
- 7) Adjusted the accounting records to reflect that there was \$150 of supplies remaining on hand at year-end.
- 8) Recorded an end-of-year adjustment to recognize rent expense.

Required:

- a) Record the above transactions on a horizontal statements model, reflecting their effect on the different financial statements.
- b) Prepare Horizon Corporation's income statement, balance sheet and statement of cash flows for the year ended December 31, 2011.

Chapter 02 - Understanding the Accounting Cycle

Horizon Company Accounting Equation																
Event	Assets				=	Liab.	+	Equity		Rev.	-	Exp.	=	NI	CF	
	Cash	AR	Supplies	Ppd. Rent		AP		Comm. Stock	Ret. Earn.							
1	10,000							10,000							10,000	FA
2		25,000							25,000	25,000				25,000		
3			500			500										
4	(6,000)			6,000											(6,000)	OA
5	23,000	(23,000)													23,000	OA
6	(18,000)							(18,000)			18,000			(18,000)	(18,000)	OA
7			(350)					(350)			350			(350)		
8				(3,500)				(3,500)			3,500			(3,500)		

a)

Horizon Company
Income Statement

For the Year Ended December 31, 2011

Revenue	\$	25,000
Operating expense	\$	(18,000)
Rent expense	\$	(3,500)
Supplies expense		<u>(350)</u>
Net Income	\$	<u><u>3,150</u></u>

b)

Chapter 02 - Understanding the Accounting Cycle

Horizon Company
Balance Sheet
As of December 31, 2011

Assets			
Cash	9,000		
Accounts receivable	2,000		
Supplies	150		
Prepaid rent	\$ 2,500	\$	<u>13,650</u>
Liabilities			500
Equity			
Common Stock	\$ 10,000		
Retained Earnings	<u>3,150</u>		
Total Equity			<u>13,150</u>
Total Liabilities and Equity		\$	<u>13,650</u>

Horizon Corporation
Statement of Cash Flows
For the Year Ended December 31, 2011

Cash Flows from operating activities			
Cash receipts from revenue	\$ 23,000		
Cash payments for rent	\$ (6,000)		
Cash payment for operating expenses	<u>(18,000)</u>		
Net cash flow from operating activities		\$	(1,000)
Cash flows from financing activities			
Cash receipt from issuance of stock			<u>10,000</u>
Net increase in cash			9,000
Plus: Beginning cash balance			<u>-</u>
Ending cash balance		\$	<u>9,000</u>

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Hard
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

122. The following transactions apply to Brunswick Corporation.

- 1) Issued common stock for \$35,000 cash.
- 2) Provided services to customers for \$18,000 on account.
- 3) Purchased land for \$18,000 cash.
- 4) Paid \$9,000 for operating expenses.
- 5) Collected \$15,000 cash from customers.
- 6) Accrued \$400 of salary expense at year end.
- 7) Paid \$2,500 dividends to stockholders.

Required:

- a) Identify the effect on the statement of cash flows for each of the above transactions.
- b) Classify the above accounting events into one of four types of transactions (asset source, asset use, asset exchange, claims exchange).

(a) Event	Cash Flow	(b) Transaction Type
1	\$35,000 FA	Asset Source
2	NA	Asset Source
3	(\$18,000) IA	Asset Use
4	(\$9,000) OA	Asset Use
5	\$15,000 OA	Asset Source
6	NA	Claims Exchange
7	(\$2,500) FA	Asset Source

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Medium
Learning Objective: 3
Learning Objective: 4
Learning Objective: 6

Chapter 02 - Understanding the Accounting Cycle

123. Record each of the following events in the horizontal statements model. After each event, record the corresponding **end-of-year adjustment** that would be necessary.

- a) Paid \$18,000 for a 1-year lease beginning April 1.
- b) Paid \$1,500 to purchase supplies. At year end, \$540 of supplies remained.
- c) Received a \$24,000 cash advance for a 6-month contract beginning on Sept. 1.

Event	Assets			=	Liab.	+	Equity	Rev.	-	Exp.	=	NI	CF	
	Cash	Supplies	Ppd. Rent		Unearned Rev.		Ret. Eam.							
a)	(18,000)		18,000										(18,000)	O A
			(13,500)				(13,500)			13,500		(13,500)		
b)	(1,500)	1,500											(1,500)	O A
		(960)					(960)			960		(960)		
c)	24,000				24,000								24,000	O A
					(16,000)		16,000	16,000				16,000		

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Reporting
 Bloom's: Application
 Difficulty: Hard
 Learning Objective: 1
 Learning Objective: 2
 Learning Objective: 3

124. The following data were taken from the accounting records of Lorenzo Company. Except where indicated, the balances are as of December 31, 2011 before closing entries have been made.

Service revenue	29,000
Retained earnings, January 1, 2011	37,260
Salaries expense	12,500
Other operating expense	6,700
Common stock	43,000
Cash flow from operating activities	8,400
Dividends	2,000
Insurance expense	800
Rent expense	6,000
Unearned revenue	3,600

Required:

- a) List the accounts that should be closed at the end of 2011.
- b) Prepare an income statement for Lorenzo Company for 2011.
- c) What is the balance in retained earnings after closing entries have been made?

Chapter 02 - Understanding the Accounting Cycle

a) Service revenue, salaries expense, other operating expense, dividends, interest expense, rent expense

Lorenzo Company
Income Statement
For the year ended December 31, 2011

Service revenue		\$ 29,000
Operating expenses		
Salaries expense	12,500	
Rent expense	6,000	
Other operating expense	6,700	
Insurance expense	<u>800</u>	<u>(26,000)</u>
Net Income		<u>\$ 3,000</u>

b)

c. $\$37,260 + 3,000 - 2,000 = 38,260$

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Medium
Learning Objective: 4
Learning Objective: 5

125. For each of the following transactions, indicate the type by entering AS for asset source transactions, AU for asset use transactions, AE for asset exchange transactions, and CE for claims exchange transactions.

- 1) ___ Paid \$10,000 for a plot of land.
- 2) ___ Recorded the accrual of \$1,000 in salaries to be paid later.
- 3) ___ Issued common stock for \$20,000 in cash.
- 4) ___ Earned revenue to be collected next year.
- 5) ___ Paid \$2,000 in dividends to its stockholders.
- 6) ___ Received cash from customers in #4 above.
- 7) ___ Paid the salaries accrued in #2 above.
- 8) ___ Borrowed money from a local bank.

1) AE 2) CE 3) AS 4) AS 5) AU 6) AE 7) AU 8) AS

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Application
Difficulty: Easy
Learning Objective: 6

126. Classify each of the following transactions for the purpose of the statement of cash flow as operating activities (OA), investing activities (IA), financing activities (FA), or not reported on the statement of cash flows (NA).

- 1) ___ Made adjusting entry to recognize interest revenue on investments.
- 2) ___ Borrowed funds from the bank.
- 3) ___ Paid rent for the month.
- 4) ___ Paid cash to settle accrued salary expense.
- 5) ___ Issued common stock for \$30,000 cash.
- 6) ___ Collected accounts receivable.
- 7) ___ Purchased land.

1) NA 2) FA 3) OA 4) OA 5) FA 6) OA 7) IA

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Medium
Learning Objective: 4

127. Jack Grimes started a consulting business, Grimes Consulting, on January 1, 2011 by issuing \$7,000 of common stock. In addition, the following events occurred in 2011.

Provided services on account, \$25,500.

Paid cash for \$11,500 in operating expenses.

Collected \$9,000 of the revenue that was previously recorded on account.

Paid a cash dividend of \$4,000 to the stockholders.

Required:

a) Show the effects of the above transactions on the accounting equation.

Assets = Liabilities + Common Stock + Retained Earnings

1)

2)

3)

4)

5)

b) Prepare an income statement and statement of cash flows for 2011.

Chapter 02 - Understanding the Accounting Cycle

a)

	ASSETS	=	LIABILITIES	+	EQUITY
1)	+\$ 7,000				+\$7,000
2)	+\$25,500				+25,500
3)	-11,500				-11,500
4)	+ 9,000				
	- 9,000				
5)	<u>- 4,000</u>				<u>- 4,000</u>
Total	<u>\$17,000</u>	=	<u>0</u>	+	<u>\$17,000</u>

Grimes Consulting
Income Statement

For the Year Ended December 31, 2011

Revenue	\$	25,500
Expense		<u>(11,500)</u>
Net Income	\$	<u>14,000</u>

b)

Grimes Consulting
Statement of Cash Flows

For the Year Ended December 31, 2011

Cash Flows from operating activities		
Cash receipts from customers	\$	9,000
Cash payment for expenses		<u>(11,500)</u>
Net cash flow from operating activities	\$	(2,500)
Cash flow from investing activities		
		-
Cash flows from financing activities		
Cash receipt from issuance of stock		7,000
Cash payment for dividends		<u>(4,000)</u>
Net cash flow from financing activities	\$	<u>3,000</u>
Net increase in cash		500
Plus: Beginning cash balance		<u>-</u>
Ending cash balance	\$	<u>500</u>

Chapter 02 - Understanding the Accounting Cycle

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Hard
Learning Objective: 1
Learning Objective: 4

128. Thiessen Company started its business by issuing \$6,000 of common stock on January 1, 2011. The company performed \$18,000 of service for customers on account in 2011. It collected \$12,500 of this amount in 2011, recorded expenses on account of \$14,500, paid \$11,000 of the payables owed, and paid a \$300 dividend to the stockholders.

Required:

- What is the amount of total assets at the end of 2011?
- What is the amount of cash on hand at the end of 2011?
- What is the net income for 2011?
- Prepare a balance sheet for 2011.

- $\$6,000 + 18,000 - 11,000 - 300 = \$12,700$ Total assets
- $\$6,000 + 12,500 - 11,000 - 300 = \$7,200$ Cash on hand
- $\$18,000 - 14,500 = \$3,500$ Net income

Thiessen Company

Balance Sheet

As of December 31, 2011

Assets		
Cash	7,200	
Accounts receivable	5,500	
Total Assets		<u>\$ 12,700</u>
Liabilities		
Accounts payable		3,500
Equity		
Common Stock	\$ 6,000	
Retained Earnings	<u>3,200</u>	
Total Equity		<u>9,200</u>
Total Liabilities and Equity		<u>\$ 12,700</u>

d)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Hard
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

129. The Palin Corporation was started on January 1, 2011, with the issuance of \$10,000 of stock. During 2011, the company provided \$15,000 of services on account and collected \$9,000 of that amount. Palin incurred \$11,500 of expenses, and paid \$10,000 of that amount during 2011. On December 31, 2011, Palin paid investors a \$400 cash dividend and accrued \$1,000 of salary expense.

Required: 1) What is the net income for year ending December 31, 2011?

2) Prepare Palin Corporation's Statement of Cash Flows for the year ended December 31, 2011.

3) What is the balance in Palin's retained earnings account after closing entries are made on December 31, 2011?

4) What is Palin's cash balance on December 31, 2011?

1) Net income: \$2,500 (\$15,000 - 11,500 - 1,000)

Palin Corporation		
Statement of Cash Flows		
For the Year Ended December 31, 2011		
Cash Flows from operating activities		
Cash receipts from customers	\$ 9,000	
Cash payments for expenses	<u>(10,000)</u>	
Net cash flow from operating activities		\$ (1,000)
Cash flows from investing activities		
		-
Cash flows from financing activities		
Cash receipt from issuance of stock	\$ 10,000	
Cash dividend paid to owners	<u>(400)</u>	
Net cash flow from financing activities		<u>9,600</u>
Net increase in cash		8,600
Plus: Beginning cash balance		<u>-</u>
Ending cash balance		<u><u>\$ 8,600</u></u>

2) Retained earnings: \$2,100 (\$2,500 - 400)

4) Cash balance: \$18,600 (\$10,000 + 10,000 + 9,000 - 10,000 - 400)

Chapter 02 - Understanding the Accounting Cycle

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Analysis
Difficulty: Hard
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

130. (a) At January 1, 2011, accounts receivable was \$20,000. Cash collected on accounts receivable during 2011 was \$15,000. At December 31, 2011, accounts receivable was \$30,000. What were the revenues earned on account during 2011?

(b) At January 1, 2011, accounts payable was \$17,000. During 2011, expenses on account were \$28,000. At December 31, 2011, accounts payable was \$15,000.

What was the amount of cash paid on accounts payable during 2011?

(c) At January 1, 2011, the balance in the retained earnings account was \$7,200. During 2011, revenue earned was \$19,800 and expenses incurred were \$7,400. At December 31, 2011, the balance in the retained earnings account was \$11,500.

What was the amount of cash dividends paid to stockholders during 2011?

(d) At January 1, 2011, the balance in the supplies account was \$450. At December 31, 2011, the company counted \$600 of supplies on hand. The company reported supplies expense in 2011 of \$2,300.

What was the total of supplies purchases during 2011?

(a) \$25,000 ($\$20,000 + X - 15,000 = 30,000$)

(b) \$30,000 ($\$17,000 + 28,000 - X = 15,000$)

(c) \$8,100 ($\$7,200 + 12,400 - X = 11,500$)

(d) \$2,450 ($\$2,300 + 600 - 450$)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Analysis
Difficulty: Hard
Learning Objective: 2

131. Washington Co. began operations on January 1, 2011, by issuing \$10,000 in common stock to the stockholders. On April 1, 2011, Link accepted an advance of \$18,000 to provide services for a one-year period beginning April 1. During 2011, services in the amount of \$16,000 were provided to customers on account, and 75% of this amount was collected by year-end. During 2011, expenses incurred on account were \$12,000, and 60% of this amount was paid by year-end. During the year, Washington paid \$600 to purchase supplies. By year-end, \$480 of the supplies had been used. Dividends to stockholders were \$1,000 during the year. During 2011, Washington paid salaries of \$14,000, and on December 31, 2011, the company accrued salaries of \$1,200.

- 1) What would Washington report for service revenue for 2011?
- 2) What would Washington report for salaries expense for 2011?
- 3) What would Washington report for supplies expense for 2011?
- 4) What would the amount be for net cash flows from operating activities for 2011?
- 5) What is the net income for 2011?
- 6) What would the balance in the retained earnings account be at December 31, 2011?

1) $\$13,500 + 16,000 = \$29,500$

2) $\$14,000 + 1,200 = \$15,200$

3) \$480

4) $\$18,000 + 12,000 - 7,200 - 600 - 14,000 = \$8,200$

5) $\$29,500 - 12,000 - 15,200 - 480 = \$1,820$

6) $\$1,820 - 1,000 = \820

AACSB: Analytic

AICPA BB: Critical Thinking

AICPA FN: Measurement, Reporting

Bloom's: Analysis

Difficulty: Hard

Learning Objective: 1

Learning Objective: 2

Learning Objective: 3

Learning Objective: 4

132. In a company's annual report, the reader will find a company's income statement, statement of changes in stockholder's equity, balance sheet, and statement of cash flows. These financial statements can help the reader to answer specific questions. Identify which financial statement would be most useful in answering the following questions. If more than one financial statement can answer the question, please identify all applicable statements.

- 1) What was the amount of cash dividends paid to the stockholders during the most recent year?
- 2) What was the total amount of land owned by the company?
- 3) What was the total amount of cash borrowed by the company during the most recent year?
- 4) What were the types of claims that the company has against its assets?
- 5) What was the total amount of cash received by the issuance of common stock?
- 6) Was the company profitable during the most recent year?
- 7) How much cash was collected from accounts receivable during the current year?
- 8) What was the total revenue earned by the company during the most recent year?
- 9) What was the ending balance of retained earnings?
- 10) What was the amount of change in the cash balance during the current year?

- 1) Statement of cash flows and statement of changes in stockholder's equity.
- 2) Balance sheet.
- 3) Statement of cash flows.
- 4) Balance sheet.
- 5) Statement of cash flows and statement of changes in stockholder's equity.
- 6) Income statement and statement of changes in stockholder's equity.
- 7) Statement of cash flows.
- 8) Income statement.
- 9) Balance sheet & statement of changes in stockholder's equity.
- 10) Statement of cash flows.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 4

133. The following events apply to Behren's Placement Agency for 2011.

- (1). Issued stock for \$14,000 cash.
- (2). On May 1, paid \$6,000 for one year's rent in advance.
- (3). Purchased on account \$500 of supplies to be used in the business.
- (4). Performed services of \$8,000 and received cash.
- (5). At December 31, an inventory of supplies showed that \$60 of supplies were still unused.
- (6). At December 31, adjusted the records for the expired rent.

Required: Draw an accounting equation and record the effects of the above events under the appropriate account headings.

Accounting Equation

Event No.	
(1).	_____
(2).	_____
(3).	_____
(4).	_____
(5).	_____
(6).	_____

Event No.		Assets	=	Liabilities	+	Equity
(1).	Cash	+14,000				+14,000
(2).	Cash	- 6,000				
	PP Rent	+ 6,000				
(3).	Supplies	+ 500		+ 500	A/P	
(4).	Cash	+ 8,000				+ 8,000
(5).	Supplies	- 440				- 440
(6).	PP Rent	- 4,000				- 4,000
	Totals	<u>18,060</u>	=	<u>500</u>		<u>17,560</u>

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Application
 Difficulty: Medium
 Learning Objective: 1
 Learning Objective: 2

Chapter 02 - Understanding the Accounting Cycle

134. Using the form below, record each of the following 2011 transactions for Morris Corporation:

- a) Nov. 1. Received cash from clients for services to be performed over the next six months, \$6,000.
- b) Nov. 1. Paid \$600 for a 12-month insurance policy.
- c) Dec. 31. Recorded expiration of two months of the insurance.
- d) Dec. 31. Earned \$2,000 of the amount received from clients in November.

	Cash	+	Accts Rec.	+	Assets Ppd. Ins.	+	Equip	=	Accts Pay	+	Liabilities Unearned Rev	+	Common Stock	+	Equity Retained Earnings
a.															
b.															
c.															
d.															

	Cash	+	Accts Rec.	+	Assets Ppd. Ins.	+	Equip	=	Accts Pay	+	Liabilities Unearned Rev	+	Common Stock	+	Equity Retained Earnings
a.	+6,000										+6,000				
b.	(600)				+600										
c.					(100)										(100)
d.											(2,000)				+2,000

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement
 Bloom's: Application
 Difficulty: Medium
 Learning Objective: 1
 Learning Objective: 2

135. In a company's annual report, the reader will find a company's income statement, statement of changes in stockholders' equity, balance sheet, and statement of cash flows. These financial statements can help the reader to answer specific questions. Identify which financial statement would be most useful in answering the following questions. If more than one financial statement can answer the question, please identify all applicable statements.

- 1) What was the amount of cash dividends paid to the stockholders during the most recent year?
- 2) What was the total amount of land owned by the company?
- 3) What was the total amount of cash borrowed by the company during the most recent year?
- 4) What were the types of claims that the company had against its assets?
- 5) What was the total amount of cash received by the issuance of common stock in the current year?
- 6) Was the company profitable during the most recent year?
- 7) How much cash was collected from accounts receivable during the current year?
- 8) What was the total revenue earned by the company during the most recent year?
- 9) What was the ending balance of retained earnings?
- 10) What was the amount of change in the cash balance during the current year?

- 1) Statement of cash flows and statement of changes in stockholders' equity.
- 2) Balance sheet.
- 3) Statement of cash flows.
- 4) Balance sheet.
- 5) Statement of cash flows and statement of changes in stockholders' equity.
- 6) Income statement and statement of changes in stockholders' equity.
- 7) Statement of cash flows.
- 8) Income statement.
- 9) Balance sheet & statement of changes in stockholders' equity.
- 10) Statement of cash flows.

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 4

136. The following transactions apply to Fillmore Company.

- 1) Issued common stock for \$21,000 cash
- 2) Provided services to customers for \$28,000 on account
- 3) Purchased land for \$18,000 cash
- 4) Incurred \$9,000 of operating expenses on credit
- 5) Collected \$15,000 cash from customers
- 6) Paid \$7,000 on accounts payable
- 7) Paid \$2,500 dividends to stockholders

Required:

a) Identify the effect on the Statement of Cash Flows, if any, for each of the above transactions. Indicate whether each transaction involves operating, investing, or financing activities and the amount of increase or decrease.

b) Classify the above accounting events into one of four types of transactions (asset source, asset use, asset exchange, claims exchange).

Event	(a) Effect on Statement of Cash Flows	(b) Transaction Type
1		
2		
3		
4		
5		
6		
7		

a) Event	Cash Flow	b) Transaction Type
1	21,000 FA	Asset Source
2	NA	Asset Source
3	(18,000) IA	Asset Exchange
4	NA	Claims Exchange
5	15,000 OA	Asset Exchange
6	(7,000) OA	Asset Use
7	(2,500) FA	Asset Use

Chapter 02 - Understanding the Accounting Cycle

AACSB: Analytic

AICPA BB: Critical Thinking

AICPA FN: Reporting, Measurement

Bloom's: Comprehension

Difficulty: Medium

Learning Objective: 1

Learning Objective: 4

Learning Objective: 6

137. Danielle McLynn started a consulting business, McLynn Consulting, on January 1, 2011, and the business engaged in the following transactions during the year:

1. Issued \$7,000 of common stock for cash
2. Provided services on account, \$25,500
3. Incurred \$11,500 of operating expense, but only paid \$5,000 of this amount
4. Collected \$9,000 of the revenue that was previously recorded on account
5. Paid a cash dividend of \$4,000 to the stockholders

Required:

- a) Show the effects of the above transactions on the accounting equation.

Assets = Liabilities + Common Stock + Retained Earnings

- 1)
- 2)
- 3)
- 4)
- 5)

- b) Prepare an income statement and statement of cash flows for 2011.

Chapter 02 - Understanding the Accounting Cycle

	ASSETS	=	LIABILITIES	+	EQUITY
1)	+\$ 7,000				+\$7,000
2)	+\$25,500				+25,500
3)	- 5,000		+\$6,500		-11,500
4)	+ 9,000				
	- 9,000				
5)	- 4,000				- 4,000
Total	<u>\$23,500</u>	=	<u>\$6,500</u>	+	<u>\$17,000</u>

a)

McLynn Consulting
Income Statement

For the Year Ended December 31, 2011

Revenue	\$ 25,500
Salary expense	<u>(11,500)</u>
Net Income	<u>\$ 14,000</u>

McLynn Consulting
Statement of Cash Flows

For the Year Ended December 31, 2011

Cash Flows from operating activities		
Cash receipts from customers	\$ 9,000	
Cash payments for expenses	<u>(5,000)</u>	
Net cash flow from operating activities		\$ 4,000
Cash flows from investing activities		-
Cash flows from financing activities		
Cash receipt from owners	\$ 7,000	
Cash dividend paid to owners	<u>(4,000)</u>	
Net cash flow from financing activities		<u>3,000</u>
Net increase in cash		7,000
Plus: Beginning cash balance		<u>-</u>
Ending cash balance		<u>\$ 7,000</u>

b)

Chapter 02 - Understanding the Accounting Cycle

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Application
Difficulty: Hard
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

138. Pearson Company was founded in 2011 and engaged in the following transactions:

1. issued common stock for cash
2. purchased supplies on account
3. collected cash from a customer for services to be provided over a period of 1 year
4. paid a cash dividend to stockholders
5. purchased a 2-year fire insurance policy
6. provided services to customers on account
7. collected cash from accounts receivable
8. paid cash for various operating expenses
9. paid rent in advance for 3 months at a time

Required:

- a) For which of these transactions would adjusting entries be required at the end of the year?
- b) Explain the reason why adjusting entries are required before financial statements can be prepared.

- a) Adjusting entries are required for transactions 2, 3, 5, and 9
- b) Adjusting entries are required at the end of an accounting period to properly match expenses with revenues. Transactions that involve deferrals and accruals require adjusting entries to bring account balances up to date.

AACSB: Analytic
AICPA BB: Communication
AICPA FN: Measurement
Bloom's: Application
Difficulty: Medium
Learning Objective: 2

139. Tom started his business by issuing \$2,000 of common stock on January 1, 2011. Tom performed \$8,000 of service on account in 2011, and he collected \$6,000 of this amount by year end. He paid operating expenses of \$4,500 and paid a \$500 dividend to the stockholders.

Required:

- a) What is the amount of total assets at the end of 2011?
- b) What is the amount of cash on hand at the end of 2011?
- c) What is the net income for 2011?
- d) Prepare a balance sheet for 2011.

- a) $+\$2,000 + \$8,000 + \$6,000 - \$6,000 - \$4,500 - \$500 = \$5,000$ Total assets
- b) \$3,000
- c) \$3,500

Balance Sheet
As of December 31, 2011

Assets		
Cash	\$	3,000
Accounts receivable		2,000
Total Assets	\$	5,000
Liabilities		-
Equity		
Common Stock	\$	2,000
Retained Earnings		3,000
Total Equity		5,000
Total Liabilities and Equity	\$	5,000

d)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement, Reporting
Bloom's: Application
Difficulty: Medium
Learning Objective: 1
Learning Objective: 2

Chapter 02 - Understanding the Accounting Cycle

140. The effects of transactions occurring during 2011 and their related end-of-year adjustments have been recorded below using the accounting equation.

	Cash	+	Accts Recv.	+	Prepaid Insurance	+	Land	=	LIABILITIES	+	Unearned Revenue	+	EQUITY	+	Retained Earnings
								=	Accts Payable				Cont. Capital		
1.	+20,000												+20,000		
2.	-5,000						+5,000								
3.			+12,000												+12,000
4.	+8,000										+8,000				
5.	+8,000		-8,000												
6.	-1,200				+1,200										
7.								+6,000							-6,000
8.	+5,000						-5,000								
9.					-1,000										-1,000
10.											-5,000				+5,000
Totals	<u>34,800</u>		<u>4,000</u>		<u>200</u>		<u>0</u>		<u>6,000</u>		<u>3,000</u>		<u>20,000</u>		<u>10,000</u>

Required:

With your knowledge of transaction analysis using an accounting equation,

- Prepare an income statement for 2011, and
- Prepare a statement of cash flows for 2011.

Chapter 02 - Understanding the Accounting Cycle

Income Statement	
For the Year Ended December 31, 2011	
Revenue	\$ 17,000
Operating expense	\$ (6,000)
Insurance expense	<u>(1,000)</u>
Net Income	<u>\$ 16,000</u>

a)

Statement of Cash Flows	
For the Year Ended December 31, 2011	
Cash Flows from operating activities	
Cash receipts from customers	\$ 16,000
Cash payments for expenses	<u>(1,200)</u>
Net cash flow from operating activities	\$ 14,800
Cash flows from investing activities	
Cash paid to purchase land	\$ (5,000)
Cash receipts from sale of land	<u>5,000</u>
Net cash flow from investing activities	\$ -
Cash flows from financing activities	
Cash receipt from owners	20,000
Net increase in cash	34,800
Plus: Beginning cash balance	<u>-</u>
Ending cash balance	<u>\$ 34,800</u>

b)

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Analysis
Difficulty: Hard
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

Chapter 02 - Understanding the Accounting Cycle

141. Pocono Corporation began business operations and experienced the following transactions during 2011:

- 1) Issued common stock for \$10,000 cash.
- 2) Provided services to customers for \$40,000 on account.
- 3) Incurred \$18,000 of operating expenses on account.
- 4) Collected \$23,000 cash from customers.
- 5) Paid \$15,000 on accounts payable.

Required:

Record the above transactions on a horizontal statements model to reflect their effect on Pocono's financial statements.

Event	Cash	+	Accounts Rec.	=	Accounts Pay	+	Common Stock	+	Retained Earnings	Cash Flows
1										
2										
3										
4										
5										
Totals										

	Cash	+	Acc Rec	=	Acc Pay	+	C Stk	+	Ret Earn	Cash Flows
1	10,000						10,000			10,000 FA
2			40,000					40,000		
3					18,000			(18,000)		
4	23,000		(23,000)							23,000 OA
5	(15,000)				(15,000)					(15,000) OA
Totals	18,000		17,000		3,000		10,000		22,000	18,000

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Measurement, Reporting
 Bloom's: Comprehension
 Difficulty: Easy
 Learning Objective: 1

142. Indicate for each of the following items if the item would be reported on the income statement (IS), statement of changes in equity (CE), balance sheet (BS), or statement of cash flows (CF). Some items may appear on more than one statement, if so, identify all applicable statements.

- 1) Prepaid insurance
- 2) Dividends paid to stockholders
- 3) Interest revenue
- 4) Accounts payable
- 5) Salaries expense
- 6) Amount of retained earnings at the end of the accounting period
- 7) Unearned subscription revenue
- 8) Cash flows from operating activities
- 9) Beginning common stock
- 10) Issued stock to investors for cash
- 11) Salaries payable
- 12) Accounts receivable

1) BS 2) CE and CF 3) IS 4) BS 5) IS 6) BS and CE 7) BS 8) CF 9) CE 10) CE and CF 11) BS
12) BS

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

Chapter 02 - Understanding the Accounting Cycle

143. Classify each of the following transactions for the purpose of the statement of cash flows as operating activities (OA), investing activities (IA), financing activities (FA), or not reported on the statement of cash flows (NA).

- 1) _____ Made adjusting entry to accrue salary expense at the end of the year
- 2) _____ Borrowed funds from the bank
- 3) _____ Paid rent for the month
- 4) _____ Paid cash to settle accounts payable
- 5) _____ Issued common stock for \$30,000 cash
- 6) _____ Collected accounts receivable
- 7) _____ Paid cash to acquire land

1) NA 2) FA 3) OA 4) OA 5) FA 6) OA 7) IA

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Reporting
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 1
Learning Objective: 3
Learning Objective: 4

144. Tuttle Company shows the following transactions for the accounting period ending December 31, 2011:

- 1) Sold books to customers for \$34,000 on account
- 2) Collected \$28,000 from customers
- 3) Issued common stock for \$8,000 cash
- 4) Prepaid four months rent for \$4,400 on October 1, 2011
- 5) Purchase supplies for \$10,500 cash
- 6) Physical count shows \$3,250 of supplies left over on December 31, 2011
- 7) Recorded adjustment for prepaid rent used

Show how the above transactions and year end adjustments affect the financial statements on the accounting equation:

	Cash +	Accts. Rec. +	Ppd. Rent +	Supplies	=	Common Stock +	Retained Earnings
1)							
2)							
3)							
4)							
5)							
6)							
7)							

	Cash +	Accts. Rec. +	Ppd. Rent +	Supplies	=	Common Stock +	Retained Earnings
1)		34,000					34,000
2)	28,000	(28,000)					
3)	8,000					8,000	
4)	(4,400)		4,400				
5)	(10,500)			10,500			
6)				(7,250)			(7,250)
7)			(3,300)				(3,300)
	21,100	6,000	1,100	3,250		8,000	23,450

AACSB: Analytic
 AICPA BB: Critical Thinking
 AICPA FN: Reporting
 Bloom's: Application
 Difficulty: Medium
 Learning Objective: 1
 Learning Objective: 2
 Learning Objective: 3

Chapter 02 - Understanding the Accounting Cycle

145. For each of the following transactions, indicate the type by entering "AS" for asset source transaction, "AU" for asset use transaction, "AE" for asset exchange transaction, and "CE" for claims exchange transaction.

- 1) ___ The company paid \$10,000 for a plot of land.
- 2) ___ Recorded the accrual of \$1,000 in salaries to be paid later.
- 3) ___ The company issued common stock for \$20,000 in cash.
- 4) ___ The business incurred operating expense on account.
- 5) ___ The business paid off its accounts payable.
- 6) ___ The business earned revenue to be collected next year.
- 7) ___ The company paid \$2,000 in dividends to its stockholders.
- 8) ___ The business received cash from customers in #6 above.
- 9) ___ Paid the salaries accrued in #2 above.
- 10) ___ Borrowed money from a local bank.

1) AE 2) CE 3) AS 4) CE 5) AU 6) AS 7) AU 8) AE 9) AU 10) AS

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 6

146. Tell whether each of the following events are asset source (AS), asset use (AU), asset exchange (AE), or claims exchange (CE) transactions.

- _____ 1) Issued common stock to investors for \$8,000 cash
- _____ 2) Paid one year's rent in advance
- _____ 3) Provided services to customers and received \$35,000 cash
- _____ 4) Paid creditors \$10,000
- _____ 5) Received \$3,000 of revenue in advance
- _____ 6) Provided services to customers on account, \$12,000
- _____ 7) Collected \$2,000 from accounts receivable
- _____ 8) Recognized accrued salary expense of \$2,000
- _____ 9) Borrowed \$6,000 from creditors
- _____ 10) Adjusted the records for supplies used of \$800

1) AS 2) AE 3) AS 4) AU 5) AS 6) AS 7) AE 8) CE 9) AS 10) AU

AACSB: Analytic
AICPA BB: Critical Thinking
AICPA FN: Measurement
Bloom's: Comprehension
Difficulty: Medium
Learning Objective: 6