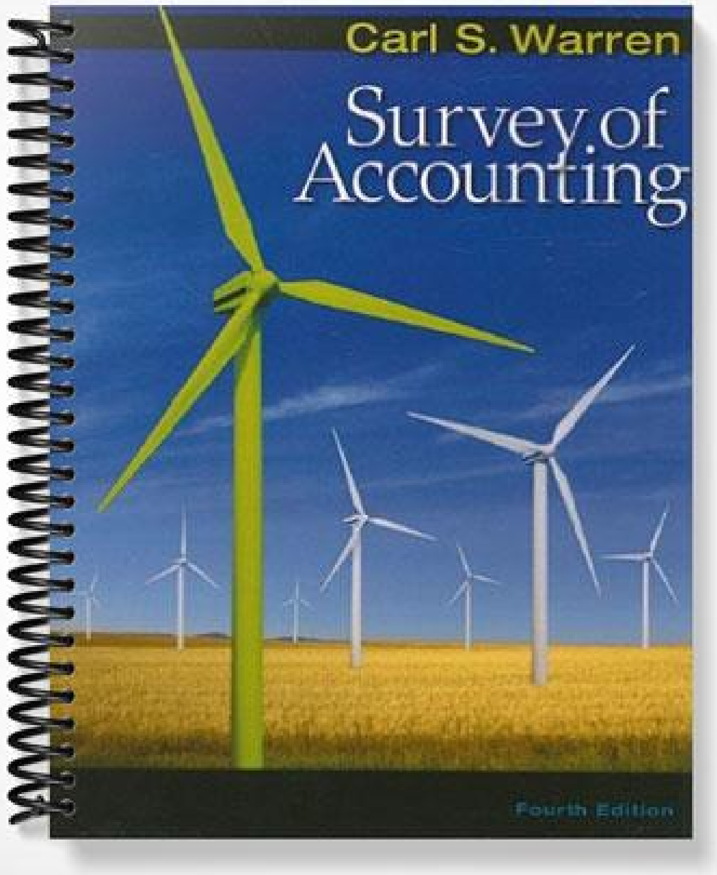
TEST BANK



Chapter 2—Basic Accounting Concepts

True/False

No.	Obj.	Difficulty	No.	Obj.	Difficulty
1	2-1	Easy	**11**	2-1	Easy
2	2-1	Easy	**12**	2-1/2-2	Moderate
3	2-1	Easy	**13**	2-1	Moderate
4	2-1	Moderate	**14**	2-1	Moderate
5	2-1	Moderate	**15**	2-2	Easy
6	2-1	Easy	**16**	2-2	Easy
7	2-1	Moderate	**17**	2-2	Easy
8	2-1	Easy	**18**	2-2	Easy
9	2-1	Easy	**19**	2-3	Easy
10	2-1/2-2	Moderate	**20**	2-3	Easy

Multiple Choice

No.	Obj.	Difficulty	No.	Obj.	Difficulty	No.	Obj.	Difficulty
1	2-1	Easy	**21**	2-2	Easy	**41**	2-3	Moderate
2	2-1	Easy	**22**	2-2	Easy	**42**	2-3	Easy
3	2-1	Difficult	**23**	2-2	Moderate	**43**	2-3	Easy
4	2-1	Moderate	**24**	2-2	Moderate	**44**	2-3	Easy
5	2-1	Difficult	**25**	2-2	Moderate	**45**	2-3	Easy
6	2-1	Easy	**26**	2-2	Moderate	**46**	2-3	Easy
7	2-1	Moderate	**27**	2-2	Easy	**47**	2-3	Easy
8	2-1	Difficult	**28**	2-2	Moderate	**48**	2-3	Easy
9	2-1	Moderate	**29**	2-2	Moderate	**49**	2-3	Easy
10	2-1	Difficult	**30**	2-2	Moderate	**50**	2-3	Easy
11	2-1	Easy	**31**	2-3	Easy	**51**	2-3	Easy
12	2-1	Moderate	**32**	2-3	Easy	**52**	2-3	Moderate
13	2-1	Moderate	**33**	2-3	Difficult	**53**	2-3	Moderate
14	2-2	Easy	**34**	2-3	Difficult	**54**	2-3	Easy
15	2-2	Easy	**35**	2-3	Difficult	**55**	2-3	Easy
16	2-2	Easy	**36**	2-3	Difficult	**56**	2-4	Easy
17	2-2	Easy	**37**	2-3	Difficult	**57**	2-4	Easy
18	2-2	Moderate	**38**	2-3	Moderate	**58**	2-5	Moderate
19	2-2	Moderate	**39**	2-3	Moderate	**59**	2-5	Moderate
20	2-2	Moderate	**40**	2-3	Moderate			

Problems

No.	Obj.	Difficulty	No.	Obj.	Difficulty
1	2-1	Moderate	**6**	2-3	Moderate
2	2-1	Difficult	**7**	2-3	Moderate
3	2-1	Moderate	**8**	2-5	Difficult
4	2-2	Moderate	**9**	2-5	Difficult
5	2-2/2-3	Difficult	**10**	2-5	Difficult

Other

No.	Obj.	Difficulty	No.	Obj.	Difficulty
1	2-2	Easy			

TRUE/FALSE

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

   ANS: T PTS: 1 DIF: Easy OBJ: 2-1
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

   ANS: F PTS: 1 DIF: Easy OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Reporting

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

   ANS: F PTS: 1 DIF: Easy OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Reporting

4. Dividends are an example of an expense.

   ANS: F PTS: 1 DIF: Moderate OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

5. Retained earnings will be reduced by the amount in the dividend account.

   ANS: T PTS: 1 DIF: Moderate OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

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

   ANS: T PTS: 1 DIF: Easy OBJ: 2-1
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

ANS: T PTS: 1 DIF: Moderate OBJ: 2-1
NAT: AACSB Analytic | AICPA FN-Reporting

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

ANS: T PTS: 1 DIF: Easy OBJ: 2-1
NAT: AACSB Analytic | AICPA FN-Reporting

9. The accounting equation can be expressed: Assets – Liabilities = Stockholders' Equity.

ANS: T PTS: 1 DIF: Easy OBJ: 2-1
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

10. When an accounts payable account is paid in cash, the stockholders' equity in the business decreases.

ANS: F PTS: 1 DIF: Moderate OBJ: 2-1 | 2-2
NAT: AACSB Analytic | AICPA FN-Measurement

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

ANS: F PTS: 1 DIF: Easy OBJ: 2-1
NAT: AACSB Analytic | AICPA FN-Reporting

12. When an account receivable is collected in cash, the total assets of the business increase.

ANS: F PTS: 1 DIF: Moderate OBJ: 2-1 | 2-2
NAT: AACSB Analytic | AICPA FN-Measurement

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

ANS: F PTS: 1 DIF: Moderate OBJ: 2-1
NAT: AACSB Analytic | AICPA FN-Reporting

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

ANS: T PTS: 1 DIF: Moderate OBJ: 2-1
NAT: AACSB Analytic | AICPA FN-Reporting

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

ANS: F PTS: 1 DIF: Easy OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

ANS: T PTS: 1 DIF: Easy OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

ANS: F PTS: 1 DIF: Easy OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

ANS: F PTS: 1 DIF: Easy OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

19. Revenues increase stockholders' equity.

ANS: T PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

ANS: F PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

MULTIPLE CHOICE

1. The basic financial statements do NOT include the
   a. income statement.
   b. tax return.
   c. balance sheet.
   d. statement of cash flows.

ANS: B PTS: 1 DIF: Easy OBJ: 2-1
NAT: AACSB Communication | AICPA FN-Reporting

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

ANS: C PTS: 1 DIF: Easy OBJ: 2-1
NAT: AACSB Communication | AICPA FN-Reporting

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

   ANS: D PTS: 1 DIF: Difficult OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Reporting

4. Which of the following is NOT considered to be a liability?
   a. Wages payable
   b. Accounts receivable
   c. Unearned revenues
   d. Accounts payable

   ANS: B PTS: 1 DIF: Moderate OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

5. Which of the following statements is NOT true about liabilities?
   a. Liabilities are debts owed to outsiders.
   b. Account titles of liabilities often include the term "payable."
   c. Cash received before services are performed is considered to be a liability.
   d. Liabilities do not include wages owed to employees of the company.

   ANS: D PTS: 1 DIF: Difficult OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

6. Which of the following accounts is a stockholders' equity account?
   a. Cash
   b. Accounts Payable
   c. Prepaid Insurance
   d. Retained Earnings

   ANS: D PTS: 1 DIF: Easy OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

7. Which of the following group of accounts are all assets?
   a. Cash, Accounts Payable, Buildings
   b. Accounts Receivable, Revenue, Cash
   c. Prepaid Expenses, Buildings, Patents
   d. Unearned Revenues, Prepaid Expenses, Cash

   ANS: C PTS: 1 DIF: Moderate OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

8. Which of the following situations increase stockholders' equity?
   a. Supplies are purchased on account.
   b. Services are provided on account.
   c. Cash is received from customers.
   d. Utility bill will be paid next month.

   ANS: B PTS: 1 DIF: Difficult OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

9. The stockholders' equity will be reduced by all of the following accounts EXCEPT:
   a. revenues.
   b. expenses.
   c. dividends.
   d. all of these.

   ANS: A PTS: 1 DIF: Moderate OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

10. Expenses can be defined as
    a. assets consumed.
    b. services used in the process of generating revenues.
    c. costs that have been incurred during the normal course of business.
    d. all of these.

    ANS: D PTS: 1 DIF: Difficult OBJ: 2-1
    NAT: AACSB Analytic | AICPA FN-Measurement

11. The gross increases in stockholders' equity attributable to business activities are called
    a. assets.
    b. liabilities.
    c. revenues.
    d. net income.

    ANS: C PTS: 1 DIF: Easy OBJ: 2-1
    NAT: AACSB Analytic | AICPA FN-Measurement

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

    ANS: A PTS: 1 DIF: Moderate OBJ: 2-1
    NAT: AACSB Analytic | AICPA FN-Reporting

13. Which of the following will increase stockholders' equity?
    a. Expenses > revenues
    b. Dividends
    c. Revenues > expenses
    d. Cash is received from customers on account.

    ANS: C PTS: 1 DIF: Moderate OBJ: 2-1
    NAT: AACSB Analytic | AICPA FN-Measurement

14. A __________ is an economic event that under generally accepted accounting principles affects an element of the financial statements and must be recorded.
    a. framework
    b. control
    c. set of rules
    d. transaction

    ANS: D PTS: 1 DIF: Easy OBJ: 2-2
    NAT: AACSB Communication | AICPA FN-Reporting

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

    ANS: A PTS: 1 DIF: Easy OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

16. Better Belly, Inc. had the following assets and liabilities as of September 30, 2009:

Assets	$54,433
Liabilities	$28,416

    What is the stockholders' equity of Better Belly as of September 30, 2009?
    a. $0
    b. $26,017
    c. $82,849
    d. Cannot be determined with this information

    ANS: B PTS: 1 DIF: Easy OBJ: 2-2
    NAT: AACSB Analytic | AICPA FN-Reporting

17. Better Belly, Inc. had the following assets and liabilities as of September 30, 2009:

Assets	$54,433
Liabilities	$28,416

If assets increased by $3,914 and equity increased by $2,290, what is the increase or decrease in liabilities of Better Belly as of September 30, 2009?

a. ($1,624)
b. $1,624
c. $6,204
d. ($6,204)

ANS: B PTS: 1 DIF: Easy OBJ: 2-2
NAT: AACSB Analytic | AICPA FN-Reporting

18. RST borrowed $25,000 from the bank. Which of the following accurately shows the effects of the transaction?

a. Increase cash $25,000 and decrease notes payable $25,000
b. Increase cash $25,000 and increase notes payable $25,000
c. Decrease cash $25,000 and decrease notes payable $25,000
d. Decrease cash $25,000 and increase notes payable $25,000

ANS: B PTS: 1 DIF: Moderate OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

19. Arnold, Inc. received cash from fees earned. How does this transaction affect the Statement of Cash Flows?

a. Increase cash from Operating Activities
b. Increase cash from Investing Activities
c. Increase cash from Financing Activities
d. No effect on the Statement of Cash Flows

ANS: A PTS: 1 DIF: Moderate OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

20. Badger Corporation purchased equipment for cash. What is the effect of this transaction?

a. Cash will decrease and equipment will increase.
b. Total assets will remain unchanged.
c. Cash flow from Investing Activities will decrease.
d. All of these.

ANS: D PTS: 1 DIF: Moderate OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

21. Anderson, Inc. paid rent expense of $4,000 for the month of October. How are the accounts affected due to this transaction?

a. Increase in cash $4,000 and increase in retained earnings $4,000
b. Increase in cash $4,000 and decrease in retained earnings $4,000
c. Decrease in cash $4,000 and decrease in retained earnings $4,000
d. Decrease in cash $4,000 and increase in retained earnings $4,000

ANS: C PTS: 1 DIF: Easy OBJ: 2-2
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

22. Anderson, Inc. purchased land for cash. What effect does this transaction have on the following accounts:
    a. Increase in Cash and decrease in Land
    b. Decrease in Cash and decrease in Land
    c. Increase in Cash and increase in Land
    d. Decrease in Cash and increase in Land

    ANS: D PTS: 1 DIF: Easy OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

23. Anderson, Inc. issued $15,000 in capital stock in exchange for cash. What is the effect of this transaction?
    a. Total assets remain unchanged.
    b. Cash flow from Financing Activities will increase.
    c. Net Income will increase.
    d. Total Retained Earnings will increase.

    ANS: B PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

24. Anderson, Inc. receives $5,000 cash for fees earned. What is the effect of this transaction?
    a. Total assets remain unchanged.
    b. Cash flow from Financing Activities will increase.
    c. Net income will increase.
    d. Retained earnings will remain unchanged.

    ANS: C PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

25. The stockholders' equity will be reduced by all of the following accounts EXCEPT:
    a. revenues.
    b. expenses.
    c. dividends.
    d. all of these.

    ANS: A PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Analytic | AICPA FN-Measurement

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

    ANS: A PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

    ANS: D PTS: 1 DIF: Easy OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

    ANS: A PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: C PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

    ANS: A PTS: 1 DIF: Moderate OBJ: 2-2
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: D PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: A PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

Exhibit 2-1

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

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

    ANS: A PTS: 1 DIF: Difficult OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: C PTS: 1 DIF: Difficult OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: B PTS: 1 DIF: Difficult OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: A PTS: 1 DIF: Difficult OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: D PTS: 1 DIF: Difficult OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: C PTS: 1 DIF: Moderate OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: B PTS: 1 DIF: Moderate OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

    ANS: C PTS: 1 DIF: Moderate OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

41. An increase in Stockholders’ Equity from revenues earned will also result in an increase in
a. liabilities.
b. assets.
c. expenses.
d. no financial statement element.

ANS: B PTS: 1 DIF: Moderate OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

42. For EFG Co., the transaction “Payment to creditors” would
a. increase total assets.
b. decrease total assets.
c. have no effect on total assets.

ANS: B PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

43. For EFG Co., the transaction “Cash sales to customers” would
a. increase total assets.
b. decrease total assets.
c. have no effect on total assets.

ANS: A PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

44. For EFG Co., the transaction “Payment of interest expense” would
a. increase total assets.
b. decrease total assets.
c. have no effect on total assets.

ANS: B PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

45. For EFG Co., the transaction “Purchase of store equipment with cash” would
a. increase total assets.
b. decrease total assets.
c. have no effect on total assets.

ANS: C PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

46. For EFG Co., the transaction “Payment of dividends” would
a. increase total assets.
b. decrease total assets.
c. have no effect on total assets.

ANS: B PTS: 1 DIF: Easy OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

47. For EFG Co., the transaction “Purchase of store equipment with a note payable” would
    a. increase total assets.
    b. decrease total assets.
    c. have no effect on total assets.

    ANS: A PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

48. For EFG Co., the transaction “Payment of quarterly taxes” would
    a. increase total assets.
    b. decrease total assets.
    c. have no effect on total assets.

    ANS: B PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

49. For EFG Co., the transaction “Receipt of interest income” would
    a. increase total assets.
    b. decrease total assets.
    c. have no effect on total assets.

    ANS: A PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

50. For EFG Co., the transaction “Receipt of a utility bill” would
    a. increase total assets.
    b. decrease total assets.
    c. have no effect on total assets.

    ANS: C PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

51. For EFG Co., the transaction “Billed a customer for fees earned (cash basis)” would
    a. increase total assets.
    b. decrease total assets.
    c. have no effect on total assets.

    ANS: C PTS: 1 DIF: Easy OBJ: 2-3
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

    ANS: A PTS: 1 DIF: Moderate OBJ: 2-3
    NAT: AACSB Analytic | AICPA FN-Reporting

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

   ANS: B PTS: 1 DIF: Moderate OBJ: 2-3
   NAT: AACSB Analytic | AICPA FN-Reporting

54. Declaring and paying cash dividends affects which accounts?
   a. Cash only
   b. Capital stock only
   c. Cash and retained earnings
   d. Cash and capital stock

   ANS: C PTS: 1 DIF: Easy OBJ: 2-3
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

55. Buying equipment for cash affects which accounts?
   a. Cash only
   b. Retained earnings only
   c. Equipment and retained earnings
   d. Cash and equipment

   ANS: D PTS: 1 DIF: Easy OBJ: 2-3
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

56. Receiving cash for fees earned affects which financial statement elements?
   a. Assets only
   b. Stockholders' equity only
   c. Assets and stockholders' equity
   d. Assets and liabilities

   ANS: C PTS: 1 DIF: Easy OBJ: 2-4
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

57. Paying expenses affects which financial statement elements?
   a. Assets only
   b. Stockholders' equity only
   c. Assets and stockholders' equity
   d. Assets and liabilities

   ANS: C PTS: 1 DIF: Easy OBJ: 2-4
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

58. The payment of a liability
   a. decreases assets and stockholders' equity.
   b. increases assets and decreases liabilities.
   c. decreases assets and increase liabilities.
   d. decreases assets and decreases liabilities.

   ANS: D PTS: 1 DIF: Moderate OBJ: 2-5
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

59. The first month of operation showed the net cash from operating activities to be $3,760, the net cash from investing activities to be ($5,415), and the ending cash balance to be $2,425. The net cash from financing activities must be
    a. $770.
    b. $4,080.
    c. ($11,600).
    d. $11,600.

    ANS: B   PTS: 1   DIF: Moderate   OBJ: 2-5
    NAT: AACSB Analytic | AICPA FN-Reporting

PROBLEM

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

   ANS:
   A financial accounting system is designed to produce financial statements. The basic elements of a financial accounting system include:
   (1) A set of rules for determining what, when, and how much should be recorded for economic events
   (2) A framework for preparing financial statements
   (3) One or more controls to determine whether errors may have arisen in the recording process.

   PTS: 1   DIF: Moderate   OBJ: 2-1
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

2. Calculate the following:
   (a) Determine the cash receipts for June based on the following data:

Cash payments during May	$42,500
Cash account balance, May 1	3,750
Cash account balance, May 30	7,000

   (b) Determine the cash received from customers on account during June based on the following data:

Accounts receivable account balance, May 1	$11,500
Accounts receivable account balance, May 30	8,250
Fees billed to customers during May	27,000

   ANS:
   (a) $45,750 ($7,000 + $42,500 – $3,750)
   (b) $30,250 ($11,500 + $27,000 – $8,250)

   PTS: 1   DIF: Difficult   OBJ: 2-1
   NAT: AACSB Analytic | AICPA FN-Measurement

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

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

PTS: 1 DIF: Moderate OBJ: 2-1
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

4. Lou’s Laundry and Dry Cleaning incorporated and started business on January 1, 2006.
   1 Lou’s Laundry and Dry Cleaning began business by depositing $30,000 in a checking account in the name of Lou’s Laundry and Dry Cleaning, Inc. Capital stock is issued.
   2 Borrowed $6,000 from City Bank.
   3 Purchased equipment from Washers Wholesale, $16,200.
   4 Purchased supplies costing $3,000 from Suds ‘n Stuff with cash.
   5 Paid one month’s rent for business space in Pine Plaza, $1,000.
   6 Services provided to customers during January totaled $13,400. All services were paid for in cash.
   7 Paid employees for January, $2,240.
   8 Received and paid the utility bill, $500.
   9 Received and paid the telephone bill, $250.
   10 Paid dividends to the stockholders, $2,140.

Indicate the effect of each transaction on the accounting equation by listing the numbers identifying the transactions, (1) through (10) in a vertical column, and inserting at the right of each number the appropriate letter from the following list:

a.	Increase in an asset, decrease in another asset.
b.	Increase in an asset, increase in a liability.
c.	Increase in an asset, increase in stockholders’ equity.
d.	Decrease in an asset, decrease in a liability.
e.	Decrease in an asset, decrease in stockholders’ equity

ANS:
1. c
2. b
3. a
4. a
5. e
6. c
7. e
8. e
9. e
10. e

PTS: 1 DIF: Moderate OBJ: 2-2
NAT: AACSB Analytic | AICPA FN-Reporting

5. **Part A**

Indicate the effect of each transaction during the month of October 2009 and the balances for the accounting equation after all transactions have been recorded. No beginning balances exist in the accounts. An accounting equation has been provided.

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

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

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

Ole, Inc. **Income Statement**		

Ole, Inc. **Retained Earnings Statement**		

Ole, Inc.
Balance Sheet

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

ANS:

Part A

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

Part B

Ole, Inc. Income Statement For the Month Ended October 31, 2009		
Revenues:		
Fees Earned		$13,000
Expenses:		
Rent Expense	$2,000	
Salaries Expense	1,000	
Interest Expense	100	
Total Expenses		3,100
Net Income		$ 9,900

Ole, Inc. Retained Earnings Statement For the Month Ended October 31, 2009		
Retained Earnings, October 1, 2009 Add: Net Income		0 $9,900
Less Dividends		(3,000)
Retained Earnings, October 31, 2009		$6,900

Ole, Inc. Balance Sheet October 31, 2009		
Assets		
Cash	$59,900	
Equipment	7,000	
Total Assets		$66,900
Liabilities		
Liabilities		
Notes Payable		$20,000
Stockholders' Equity		
Capital Stock	$40,000	
Retained Earnings	6,900	46,900
Total Liabilities and Stockholders' Equity		$66,900

Ole, Inc. **Statement of Cash Flows** **For the Month Ended October 31, 2009**		
Cash flows from operating activities:		
Cash receipts from operating activities	$13,000	0
Cash payments for operating activities	(3,100)	
Net cash flows from operating activities		$ 9,900
Cash flows from investing activities:		
Cash payments for equipment		(7,000)
Cash flows from financing activities:		
Cash receipts from issuing capital stock	$40,000	
Cash receipts from note payable	20,000	
Cash payments for dividends	(3,000)	
Net cash flows from financing activities		57,000
Cash as of October 31, 2009		$ 59,900

PTS: 1 DIF: Difficult OBJ: 2-2|2-3
NAT: AACSB Analytic | AICPA FN-Reporting

6. Explain how the four financial statements are linked.

ANS:
A financial accounting system is designed to produce four financial statements. The income statement, statement of retained earnings, and statement of cash flows are linked to an element of the balance sheet.

(1) The income statement shows the net effects of revenues and expenses, which affects the retained earnings on the balance sheet.
(2) The statement of retained earnings reflects the net income and dividends paid and shows how retained earnings in the balance sheet moves from the beginning balance to the ending balance.
(3) The statement of cash flows explains how the cash balance in the balance sheet moves from the beginning balance to the ending balance by looking at the cash effects of operating, investing, and financing activities.

PTS: 1 DIF: Moderate OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

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

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

PTS: 1 DIF: Moderate OBJ: 2-3
NAT: AACSB Reflective Thinking | AICPA FN-Reporting

8. The following are included in Ace Auto Parts, Inc.'s December 31, 2009 balance sheet:

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

Below are the balances for December 31, 2010:

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

Analyze the changes in these balances and determine net income for 2010, assuming that the only change to stockholders' equity is from net income.

ANS:

	Assets	**=**	**Liabilities**	**+**	**Stockholder's Equity**
	50,000		40,000		
	100,000				
	60,000				
	130,000		70,000		
Bal. 12/31/2009	340,000		110,000		230,000

	Assets	**=**	**Liabilities**	**+**	**Stockholder's Equity**
	75,000				
	100,000				
	150,000		60,000		
	130,000		50,000		
Bal. 12/31/2010	455,000		110,000		345,000

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

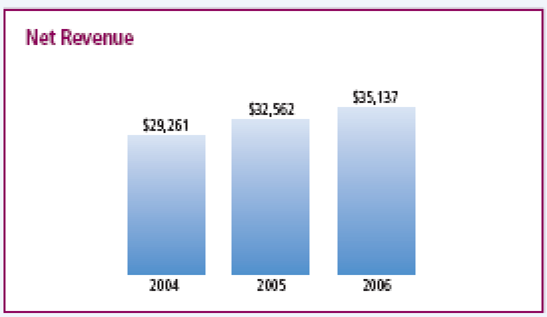
PTS: 1 DIF: Difficult OBJ: 2-5
NAT: AACSB Analytic | AICPA FN-Reporting

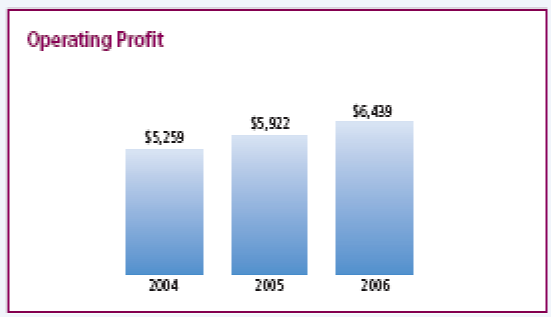
Consolidated Statement of Income

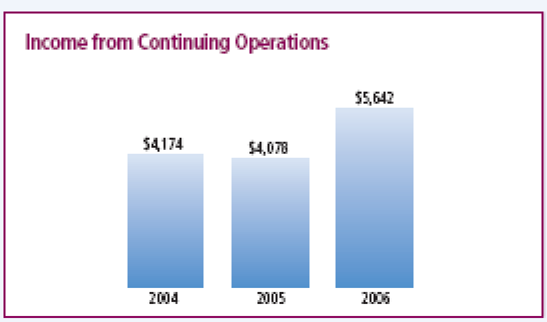
PepsiCo, Inc. and Subsidiaries
Fiscal years ended December 30, 2006, December 31, 2005 and December 25, 2004

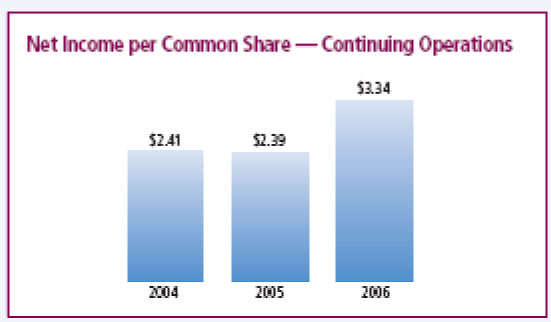
(in millions except per share amounts)	2006	2005	2004
Net Revenue	**$35,137**	**$32,562**	**$29,261**
Cost of sales	15,762	14,176	12,674
Selling, general and administrative expenses	12,774	12,314	11,031
Amortization of intangible assets	162	150	147
Restructuring and impairment charges	–	–	150
Operating Profit	6,439	5,922	5,259
Bottling equity income	616	557	380
Interest expense	(239)	(256)	(167)
Interest income	173	159	74
Income from Continuing Operations before Income Taxes	6,989	6,382	5,546
Provision for Income Taxes	1,347	2,304	1,372
Income from Continuing Operations	5,642	4,078	4,174
Tax Benefit from Discontinued Operations	–	–	38
Net Income	$ 5,642	$ 4,078	$ 4,212
Net Income per Common Share — Basic			
Continuing operations	$3.42	$2.43	$2.45
Discontinued operations	–	–	0.02
Total	$3.42	$2.43	$2.47
Net Income per Common Share — Diluted			
Continuing operations	$3.34	$2.39	$2.41
Discontinued operations	–	–	0.02
Total	$3.34	$2.39	$2.44*

* Based on unrounded amounts.
See accompanying notes to consolidated financial statements.









Consolidated Statement of Cash Flows

PepsiCo, Inc. and Subsidiaries
Fiscal years ended December 30, 2006, December 31, 2005 and December 25, 2004

(in millions)	2006	2005	2004
Operating Activities			
Net income	$ 5,642	$ 4,078	$ 4,212
Depreciation and amortization	1,406	1,308	1,264
Stock-based compensation expense	270	311	368
Excess tax benefits from share-based payment arrangements	(134)	–	–
Restructuring and impairment charges	–	–	150
Cash payments for merger-related costs and restructuring charges	–	(22)	(92)
Tax benefit from discontinued operations	–	–	(38)
Pension and retiree medical plan contributions	(131)	(877)	(534)
Pension and retiree medical plan expenses	544	464	395
Bottling equity income, net of dividends	(479)	(411)	(297)
Deferred income taxes and other tax charges and credits	(510)	440	(203)
Other non-cash charges and credits, net	32	145	166
Change in accounts and notes receivable	(330)	(272)	(130)
Change in inventories	(186)	(132)	(100)
Change in prepaid expenses and other current assets	(37)	(56)	(31)
Change in accounts payable and other current liabilities	223	188	216
Change in income taxes payable	(295)	609	(268)
Other, net	69	79	(24)
Net Cash Provided by Operating Activities	6,084	5,852	5,054
Investing Activities			
Snack Ventures Europe (SVE) minority interest acquisition	–	(750)	–
Capital spending	(2,068)	(1,736)	(1,387)
Sales of property, plant and equipment	49	88	38
Investment in finance assets	(25)	–	–
Other acquisitions and investments in noncontrolled affiliates	(522)	(345)	(64)
Cash proceeds from sale of PBG stock	318	214	–
Divestitures	37	3	52
Short-term investments, by original maturity			
More than three months — purchases	(29)	(83)	(44)
More than three months — maturities	25	84	38
Three months or less, net	2,021	(992)	(963)
Net Cash Used for Investing Activities	(194)	(3,517)	(2,330)
Financing Activities			
Proceeds from issuances of long-term debt	51	25	504
Payments of long-term debt	(157)	(177)	(512)
Short-term borrowings, by original maturity			
More than three months — proceeds	185	332	153
More than three months — payments	(358)	(85)	(160)
Three months or less, net	(2,168)	1,601	1,119
Cash dividends paid	(1,854)	(1,642)	(1,329)
Share repurchases — common	(3,000)	(3,012)	(3,028)
Share repurchases — preferred	(10)	(19)	(27)
Proceeds from exercises of stock options	1,194	1,099	965
Excess tax benefits from share-based payment arrangements	134	–	–
Net Cash Used for Financing Activities	(5,983)	(1,878)	(2,315)
Effect of exchange rate changes on cash and cash equivalents	28	(21)	51
Net (Decrease)/Increase in Cash and Cash Equivalents	(65)	436	460
Cash and Cash Equivalents, Beginning of Year	1,716	1,280	820
Cash and Cash Equivalents, End of Year	$ 1,651	$ 1,716	$ 1,280

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet

PepsiCo, Inc. and Subsidiaries
December 30, 2006 and December 31, 2005

(in millions except per share amounts)	2006	2005
ASSETS		
Current Assets		
Cash and cash equivalents	$ 1,651	$ 1,716
Short-term investments	1,171	3,166
Accounts and notes receivable, net	3,725	3,261
Inventories	1,926	1,693
Prepaid expenses and other current assets	657	618
Total Current Assets	9,130	10,454
Property, Plant and Equipment, net	9,687	8,681
Amortizable Intangible Assets, net	637	530
Goodwill	4,594	4,088
Other nonamortizable intangible assets	1,212	1,086
Nonamortizable Intangible Assets	5,806	5,174
Investments in Noncontrolled Affiliates	3,690	3,485
Other Assets	980	3,403
Total Assets	$29,930	$31,727
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Short-term obligations	$ 274	$ 2,889
Accounts payable and other current liabilities	6,496	5,971
Income taxes payable	90	546
Total Current Liabilities	6,860	9,406
Long-Term Debt Obligations	2,550	2,313
Other Liabilities	4,624	4,323
Deferred Income Taxes	528	1,434
Total Liabilities	14,562	17,476
Commitments and Contingencies		
Preferred Stock, no par value	41	41
Repurchased Preferred Stock	(120)	(110)
Common Shareholders' Equity		
Common stock, par value 1 2/3¢ per share (issued 1,782 shares)	30	30
Capital in excess of par value	584	614
Retained earnings	24,837	21,116
Accumulated other comprehensive loss	(2,246)	(1,053)
	23,205	20,707
Less: repurchased common stock, at cost (144 and 126 shares, respectively)	(7,758)	(6,387)
Total Common Shareholders' Equity	15,447	14,320
Total Liabilities and Shareholders' Equity	$29,930	$31,727

See accompanying notes to consolidated financial statements.

Consolidated Statement of Common Shareholders' Equity

PepsiCo, Inc. and Subsidiaries
Fiscal years ended December 30, 2006, December 31, 2005 and December 25, 2004

	2006		2005		2004	
(in millions)	Shares	Amount	Shares	Amount	Shares	Amount
Common Stock	1,782	$ 30	1,782	$ 30	1,782	$ 30
Capital in Excess of Par Value						
Balance, beginning of year		614		618		548
Stock-based compensation expense		270		311		368
Stock option exercises[a]		(300)		(315)		(298)
Balance, end of year		584		614		618
Retained Earnings						
Balance, beginning of year		21,116		18,730		15,961
Net income		5,642		4,078		4,212
Cash dividends declared — common		(1,912)		(1,684)		(1,438)
Cash dividends declared — preferred		(1)		(3)		(3)
Cash dividends declared — RSUs		(8)		(5)		(2)
Balance, end of year		24,837		21,116		18,730
Accumulated Other Comprehensive Loss						
Balance, beginning of year		(1,053)		(886)		(1,267)
Currency translation adjustment		465		(251)		401
Cash flow hedges, net of tax:						
Net derivative (losses)/gains		(18)		54		(16)
Reclassification of (gains)/losses to net income		(5)		(8)		9
Unamortized pension and retiree medical, net of tax		(1,782)		–		–
Minimum pension liability adjustment, net of tax		138		16		(19)
Unrealized gain on securities, net of tax		9		24		6
Other		–		(2)		–
Balance, end of year		(2,246)		(1,053)		(886)
Repurchased Common Stock						
Balance, beginning of year	(126)	(6,387)	(103)	(4,920)	(77)	(3,376)
Share repurchases	(49)	(3,000)	(54)	(2,995)	(58)	(2,994)
Stock option exercises	31	1,619	31	1,523	32	1,434
Other	–	10	–	5	–	16
Balance, end of year	(144)	(7,758)	(126)	(6,387)	(103)	(4,920)
Total Common Shareholders' Equity		$15,447		$14,320		$13,572

	2006	2005	2004
Comprehensive Income			
Net income	$5,642	$4,078	$4,212
Currency translation adjustment	465	(251)	401
Cash flow hedges, net of tax	(23)	46	(7)
Minimum pension liability adjustment, net of tax	5	16	(19)
Unrealized gain on securities, net of tax	9	24	6
Other	–	(2)	–
Total Comprehensive Income	$6,098	$3,911	$4,593

(a) Includes total tax benefits of $130 million in 2006, $125 million in 2005 and $183 million in 2004.
See accompanying notes to consolidated financial statements.

9. Refer to PepsiCo's financial statements and answer the following questions:
   (a) Did PepsiCo issue any stock in 2006? If so, how much and where might this information be found?
   (b) Did PepsiCo repurchase any preferred stock in 2006? If so, how much and where might this information be found?

   ANS:
   (a) Yes, PepsiCo issued 1,782,000 shares of common stock. The information is in the Stockholders' Equity section of the Balance Sheet.
   (b) Yes, PepsiCo repurchased $120,000,000 of preferred stock. The information is in the Stockholders' Equity section of the Balance Sheet.

   PTS: 1 DIF: Difficult OBJ: 2-5
   NAT: AACSB Reflective Thinking | AICPA FN-Reporting

10. Refer to PepsiCo's financial statements. PepsiCo's cash balance decreased from 2005 to 2006. By looking at just the balance sheet, do you think this is a positive or negative financial indicator? What other short-term asset accounts might you consider in answering this question?

    ANS:
    Cash declined, but the largest decline in Current Assets was in short-term investments. Accounts and notes receivable actually increased from 2005 to 2006.

    PTS: 1 DIF: Difficult OBJ: 2-5
    NAT: AACSB Reflective Thinking | AICPA FN-Reporting

OTHER

1. On April 1, the cash account balance was $67,880. During April, cash receipts totaled $345,600 and the April 30 balance was $95,230. Determine the cash payments made during April.

   ANS:
   95,230 = 67,880 + 345,600 – ?
   Cash payments = $318,250

   PTS: 1 DIF: Easy OBJ: 2-2
   NAT: AACSB Analytic | AICPA FN-Measurement