**E2.6** The following items are taken from the financial statements of Carmen Co. at December 31, 2022.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Land | $195,600 | Notes receivable (due in 2023) | 5,300 | Accum. Dep. - equipment | 18,720 |
| Accounts receivable | 21,700 | Accum. Dep. - land improvements | 12,600 | Interest payable | 3,600 |
| Supplies | 9,200 | Common stock | 75,000 | Income taxes payable | 14,700 |
| Cash | 11,840 | Retained earnings (12/31/22) | 495,000 | Patents | 46,700 |
| Equipment | 82,400 | Accum. Dep. - buildings | 32,600 | Investments in stock (long-term) | 71,500 |
| Buildings | 261,200 | Accounts payable | 9,500 | Debt investments (short-term) | 4,100 |
| Land improvements | 45,780 | Mortgage payable | 93,600 |  |  |

**Instructions**

Prepare a classified balance sheet. Assume that $9,100 of the mortgage payable will be paid in 2023.

|  |  |  |
| --- | --- | --- |
|  | | |
| Assets | | |
| Current Assets |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
| Total Current Assets |  |  |
| Long Term Investments |  |  |
|  |  |  |
| Property, Plant, and Equipment |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
| Total Property, Plant, and Equipment |  |  |
| Intangibles |  |  |
|  |  |  |
| **Total Assets** |  |  |
| Liabilities and Stockholders’ Equity | | |
| Current Liabilities |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
| Total Current Liabilities |  |  |
| Long-term Liabilities |  |  |
|  |  |  |
| Total Liabilities |  |  |
| Stockholders’ Equity |  |  |
|  |  |  |
|  |  |  |
| Total Stockholders’ Equity |  |  |
| **Total Liabilities and Stockholders’ Equity** |  |  |

**E2.9** The chief financial officer (CFO) of Myeneke Corporation requested that the accounting department prepare a preliminary balance sheet on December 30, 2022, so that the CFO could get an idea of how the company stood. He knows that certain debt agreements with its creditors require the company to maintain a current ratio of at least 2:1. The preliminary balance sheet is as follows.

| **Myeneke Corp. Balance Sheet December 30, 2022** | | | | | |
| --- | --- | --- | --- | --- | --- |
| Current assets |  |  | Current liabilities |  |  |
| Cash | $25,000 |  | Accounts payable | $ 20,000 |  |
| Accounts receivable | 30,000 |  | Salaries and wages payable | 10,000 | $   30,000 |
| Prepaid insurance | 5,000 | $   60,000 | Long-term liabilities |  |  |
| Equipment (net) |  | 200,000 | Notes payable |  | 80,000 |
| Total assets |  | $260,000 | Total liabilities |  | 110,000 |
|  |  |  | Stockholders’ equity |  |  |
|  |  |  | Common stock | 100,000 |  |
|  |  |  | Retained earnings | 50,000 | 150,000 |
|  |  |  | Total liabilities and stockholders’ equity |  | $260,000 |

**Instructions**

1. Calculate the current ratio and working capital based on the preliminary balance sheet.
2. Based on the results in (a), the CFO requested that $20,000 of cash be used to pay off the balance of the Accounts Payable account on December 31, 2022. Calculate the new current ratio and working capital after the company takes these actions.
3. Discuss the pros and cons of the current ratio and working capital as measures of liquidity.
4. Was it unethical for the CFO to take these steps?

**P2.2**  These items are taken from the financial statements of Martin Corporation for 2022.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Retained earnings (beginning of year) | $31,000 | Common stock | 12,000 | Accounts receivable | 11,700 |
| Utilities expense | 2,000 | Dividends | 12,000 | Insurance expense | 2,200 |
| Equipment | 66,000 | Service revenue | 68,000 | Salaries and wages expense | 37,000 |
| Accounts payable | 18,300 | Prepaid insurance | 3,500 | Accumulated depreciation—equipment | 17,600 |
| Cash | 10,100 | Maintenance and repairs expense | 1,800 |  |  |
| Salaries and wages payable | 3,000 | Depreciation expense | 3,600 |  |  |

**Instructions**: Prepare an income statement, a retained earnings statement, and a classified balance sheet as of December 31, 2022.

|  |  |  |
| --- | --- | --- |
| Martin Corporation  Income Statement  For EOY December 31st 2022 | | |
| Revenues |  |  |
| Service Revenue | 68000 | 68000 |
| Expenses |  |  |
| Utilities Expense | 2000 |  |
| Maintenance & Repairs Expense | 1800 |  |
| Depreciation Expense | 3600 |  |
| Insurance Expense | 2200 |  |
| Salaries & Wages Expense | 37000 |  |
| Total Expenses |  | 44600 |
| **Net Income** |  | 21400 |

|  |  |  |
| --- | --- | --- |
| Martin Corporation  Retained Earnings Statement  For EOY December 31st, 2022 | | |
| Retained Earnings (Beginning of Year) | 31000 |  |
| Add: Net Income | 21400 |  |
|  | 52400 |  |
| Less: Dividends | 12000 |  |
| Retained Earnings – December 31st, 2022 | 40400 |  |

|  |  |  |
| --- | --- | --- |
| Martin Corporation  Balance Sheet  as of December 31st, 2022 | | |
| Assets | | |
| Current Assets |  |  |
| Cash | 10100 |  |
| Prepaid Insurance | 3500 |  |
| Accounts Receivable | 11700 |  |
| Total Current Assets |  | 25300 |
| Property, Plant, and Equipment |  |  |
| Equipment | 66000 |  |
| Less: Accumulated Depreciation | 17600 |  |
| Total Property, Plant, and Equipment |  | 48400 |
| **Total Assets** |  | 73700 |
| Liabilities and Stockholders’ Equity | | |
| Current Liabilities |  |  |
| Accounts Payable | 18300 |  |
| Salaries & Wages Payable | 3000 |  |
| Total Current Liabilities |  | 21300 |
| Stockholders’ Equity |  |  |
| Common Stock | 12000 |  |
| Retained Earnings, December 31, 2022 | 40400 |  |
| Total Stockholders’ Equity |  | 52400 |
| **Total Liabilities and Stockholders’ Equity** |  | 73700 |

**E2.10** Suppose the following data were taken from the 2022 and 2021 financial statements of **American Eagle Outfitters**. (All numbers, including share data, are in thousands.)

|  | **2022** | **2021** |
| --- | --- | --- |
| Current assets | $ 925,359 | $1,020,834 |
| Total assets | 1,963,676 | 1,867,680 |
| Current liabilities | 401,763 | 376,178 |
| Total liabilities | 554,645 | 527,216 |
| Net income | 179,061 | 400,019 |

**Instructions:** Perform each of the following.

1. Calculate the current ratio for each year.

Annual Current Ratio = current assets / current liabilities

2022 = 2.713699

2021 = 2.303246

1. Calculate the debt to assets ratio for each year.

Annual Debt-To-Assets ratio = Total Liabilities / Total Assets

2022 = 0.282452 (28.24%)

2021 = 0.282284 (28.23%)

1. Discuss American Eagle’s solvency in 2022 versus 2021.

American Eagle’s solvency remained relatively the same from 2021 to 2022. Its ratio of 28.24% mean that every dollar of assets was financed by 28.24 cents of debt. For a retailer, this is pretty pretty poor. This low solvency suggests that American Eagle’s ability to meet its debt payments was questionable.

**P2.4** Comparative financial statement data for Loeb Corporation and Bowsh Corporation, two competitors, appear below. All balance sheet data are as of December 31, 2022.

|  | **Loeb Corporation** | **Bowsh Corporation** |
| --- | --- | --- |
|  | **2022** | **2022** |
| Net sales | $1,800,000 | $620,000 |
| Cost of goods sold | 1,175,000 | 340,000 |
| Operating expenses | 283,000 | 98,000 |
| Interest expense | 9,000 | 3,800 |
| Income tax expense | 85,000 | 36,000 |
| Current assets | 407,200 | 190,336 |
| Plant assets (net) | 532,000 | 139,728 |
| Current liabilities | 66,325 | 33,716 |
| Long-term liabilities | 108,500 | 40,684 |

**Instructions**

1. Comment on the relative liquidity of the companies by computing working capital and the current ratio for each company for 2022.

Annual Current Ratio = current assets / current liabilities

Loeb Corp. Annual Current Ratio = 6.139

Bowsh Corp. Annual Current Ratio = 5.645

A ratio above 1 means current assets exceed liabilities, and, generally, the higher the ratio, the better.

1. Comment on the relative solvency of the companies by computing the debt to assets ratio for each company for 2022.

Annual Debt-To-Assets ratio = Total Liabilities / Total Assets

Loeb Corp : (Current Liabilities + Long-Term Liabilities) / (Current Assets / Plant Assets) = 0.186

Bowsh Corp : (Current Liabilities + Long-Term Liabilities) / (Current Assets / Plant Assets) = 0.225