EMBA 7010 Financial and Managerial Accounting

Mid Term Exam

***MULTIPLE CHOICE: (4 POINTS EACH)—40 POINTS***

1. A company’s net cash flow will equal its net income …

A) Almost always

B) Rarely

C) Occasionally

D) Only when the company has no investing cash flow for the period

E) Only when the company has no investing or financing cash flow for the period

P1-17

2. The Goodyear Tire & Rubber Company’s December 31, 2016 financial statements reported the following (in millions):

|  |  |
| --- | --- |
| Total assets | $16,511 |
| Total liabilities | 11,786 |
| Total shareholders’ equity | 4,725 |
| Dividends | 82 |
| Net income (loss) | 1,264 |
| Retained earnings, December 31, 2015 | 4,570 |

What did Goodyear report for retained earnings at December 31, 2016?

A) $5,907 million

B) $5,752 million

C) $5,916 million

D) $5,834 million

E) There is not enough information to determine the answer.

**3.** As inventory and property plant and equipment on the balance sheet are consumed, they are reflected:

A) As a revenue on the income statement

B) As an expense on the income statement

C) As a use of cash on the statement of cash flows

D) On the balance sheet because assets are never consumed

E) Both B and C because the financial statements articulate

4. Pfizer Inc., a pharmaceutical company, reported net income for fiscal 2016 of $7,215 million, retained earnings at the start of the year of $71,993 million and dividends of $7,448 million, and other transactions with shareholders that increased retained earnings during the year by $14 million.

If there were no additional transactions during the year that affected retained earnings, what was the balance of retained earnings at the end of the year?

A) $ 71,774 million

B) $ 38,748 million

C) $ 124,926 million

D) $ 47,729 million

E) There is not enough information to calculate the amount.

**5.** During its first three months of operations, Cari’s Bakery, Inc. purchased supplies such as plates, napkins, bags, and cutlery for $9,000 and recorded this as supplies inventory. Supplies on hand at the end of the first quarter, amount to $5,600.

To prepare financial statement for the first quarter, the company must record which of the following accounting adjustments?

1. Increase Supplies expense by $5,600 and decrease Supplies inventory by $5,600
2. Increase Supplies expense by $3,400 and decrease Supplies inventory by $3,400
3. Increase Supplies inventory by $5,600 and decrease Supplies expense by $5,600
4. Increase Supplies inventory by $3,400 and decrease Supplies expense by $3,400
5. None of the above

**6.** During the month of March 2017, Weimar World, a tax-preparation service, had the following transactions.

* Billed $496,000 in revenues on credit
* Received $164,000 from customers’ accounts receivable
* Incurred expenses of $194,000 but only paid $87,700 cash for these expenses
* Prepaid $32,220 for computer services to be used next month

What was the company’s accrual basis net income for the month?

* 1. $ 302,000
  2. $ 264,080
  3. $ 41,860
  4. $408,300
  5. None of the above

7. The 2016 financial statements of The New York Times Company reveal average shareholders’ equity attributable to controlling interest of $837,283 thousand, net operating profit after tax of $48,032 thousand, net income attributable to The New York Times Company of $29,068 thousand, and average net operating assets of $354,414 thousand.

The company’s return on net operating assets (RNOA) for the year is:

A) 3.5%

B) 6.9%

C) 13.6%

D) 18.7%

E) There is not enough information to calculate the ratio.

8. The fiscal 2016 balance sheet for Whole Foods Market reports the following data (in millions). What is the company’s quick ratio?

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Cash and  cash equivalents | Marketable securities | Accounts receivable | Merchandise inventories | Current  assets | Current liabilities |
| $351 | $379 | $242 | $517 | $1,975 | $1,341 |

A) 0.69

B) 1.38

C) 0.72

D) 1.47

E) None of the above

9. Ticketmaster contracts with the producer of Blue Man Group to sell tickets online. Ticketmaster charges each customer a fee of $9 per ticket and receives $22 per ticket from the producer. Ticketmaster does not take control of the ticket inventory. Average ticket price for the event is $105.

How much revenue should Ticketmaster recognize for each Blue Man Group ticket sold?

A) $9 because the $22 from the producer is similar to a negative cost of goods sold

B) $105 because the $83 is cost of goods sold paid to the Blue Man Group producer

C) $31 because both the fee from the customer and the Blue Man Group producer are earned

D) $114 because the $83 is cost of goods sold paid to the Blue Man Group producer

E) None of the above

10. On its 2016 income statement, Abbott Laboratories reported research and development expense of $1,422,000,000.

Which of the following statements must be *true*?

A) Abbott Laboratories spent $1,422,000,000 in cash to develop new products and improve old products.

B) Research and development expense reduced Abbott Laboratories 2016 net income by $1,422,000,000.

C) Abbott Laboratories capitalized at least $1,422,000,000 of research and development costs in 2016.

D) The $1,422,000,000 included amortized research and development costs from prior years that were not previously expensed, because Abbott Laboratories incurs such expenses each year.

E) None of the above

***PROBLEMS/ESSAYS: (10 POINTS EACH)-60 POINTS***

**1.** In its October 2, 2016 annual report, Starbucks Corporation reports the following items.

|  |  |
| --- | --- |
| *($ millions)* | 2016 |
| Cash flows from operations | $4,575.1 |
| Total revenues | 21,315.9 |
| Shareholders’ equity | 5,890.7 |
| Cash flows from financing | (1,753.5) |
| Total liabilities | 8,438.8 |
| Cash, ending year | 2,128.8 |
| Expenses | 18,497.0 |
| Noncash assets | 12,200.7 |
| Cash flows from investing | (2,222.9) |
| Net earnings | 2,818.9 |
| Cash, beginning year | 1,530.1 |

a. Prepare the balance sheet for Starbucks for October 2, 2016.

b. Prepare the income statement for Starbucks for the year ended October 2, 2016.

c. Prepare the statement of cash flows for Starbucks for the year ended October 2, 2016.

**2.** Book value of stockholders’ equity usually differs from company market value. Explain some reasons why a company’s book value of stockholders’ equity can differ from a company’s market value.

3. Craft Corner began operations in March with cash and common stock of $36,000. The company made $582,000 in net income its first month. It performed print jobs for customers and billed these customers $900,000. The company collected half of its receivables by the end of the month. The company had cost of goods sold of $162,000 paid for in cash and $6,000 inventory left over at the end of the month. Craft Corner employees earned wages but those are not paid until the first of April. This was the company’s only liability.

Complete the following statements for the end of March.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Income Statement | | |  | Balance Sheet | | |
| Sales |  | $ |  | Cash |  | $ |
| Cost of sales |  |  |  | Accounts receivable |  |  |
| Wages expense |  |  |  | Inventory |  |  |
| Net income |  | $ |  | Total assets |  | $ |
|  |  |  |  |  |  |  |
|  |  |  |  | Wages payable |  | $ |
|  |  |  |  | Common Stock |  |  |
|  |  |  |  | Retained earnings |  |  |
|  |  |  |  | Total liabilities and equity |  | $ |

**4.** Use the following selected balance sheet and income statement data for Mattel Inc. (in $ thousands) to compute a) return on equity, b) profit margin (PM), c) asset turnover (AT), and d) financial leverage (FL) for fiscal 2016. Show that ROE = PM × AT × FL.

|  |  |  |
| --- | --- | --- |
| *(in thousands)* | 2016 | 2015 |
| Net sales | $5,456,650 | $5,702,613 |
| Operating income | 519,233 | 540,922 |
| Interest expense | 95,118 | 85,270 |
| Net income | 318,022 | 369,416 |
| Total assets | 6,493,794 | 6,535,143 |
| Total liabilities | 4,086,012 | 3,901,889 |

5. The asset side of the 2017 balance sheet for Oracle Corporation is below. The company reported total revenues of $37,728 million in 2017 and $37,047 million in 2016. Use this information to answer the required.

|  |  |  |
| --- | --- | --- |
| Oracle Corporation  CONSOLIDATED BALANCE SHEETS (excerpts) | | |
| in millions | May 31, 2017 | May 31, 2016 |
| [Current assets:](javascript:void(0);) |  |  |
| [Cash and cash equivalents](javascript:void(0);) | $ 21,784 | $ 20,152 |
| [Marketable securities](javascript:void(0);) | 44,294 | 35,973 |
| [Trade receivables, net of allowances for doubtful accounts of $319 and $327 as of May 31, 2017 and May 31, 2016, respectively](javascript:void(0);) | 5,300 | 5,385 |
| [Inventories](javascript:void(0);) | 300 | 212 |
| [Prepaid expenses and other current assets](javascript:void(0);) | 2,837 | 2,591 |
| [Total current assets](javascript:void(0);) | 74,515 | 64,313 |
| [Non-current assets:](javascript:void(0);) |  |  |
| [Property, plant and equipment, net](javascript:void(0);) | 5,315 | 4,000 |
| [Intangible assets, net](javascript:void(0);) | 7,679 | 4,943 |
| [Goodwill, net](javascript:void(0);) | 43,045 | 34,590 |
| [Deferred tax assets](javascript:void(0);) | 1,143 | 1,291 |
| [Other assets](javascript:void(0);) | 3,294 | 3,043 |
| [Total non-current assets](javascript:void(0);) | 60,476 | 47,867 |
| [Total assets](javascript:void(0);) | $134,991 | $112,180 |

*Required:*

a. What is the company’s gross amount of receivables at the end of 2017 and 2016?

b. Compute the common-size amount for gross accounts receivable, for both years. Interpret the year-over-year change in this ratio.

c. Compute the allowance for doubtful accounts to gross accounts receivable, for both years. Interpret the year-over-year change in this ratio.

d. Based on the ratios you calculated, form an opinion about the quality of the company’s accounts receivable.

6. Income statements and balance sheets follow for The New York Times Company. Refer to these financial statements to answer the requirements.

|  |  |  |
| --- | --- | --- |
| The New York Times Company  Consolidated Statements of Income | | |
|  | Fiscal year ended | |
| *(in thousands)* | Dec. 29, 2016 | Dec. 30, 2015 |
| Revenues |  |  |
| Circulation | $ 880,543 | $ 851,790 |
| Advertising | 580,732 | 638,709 |
| Other | 94,067 | 88,716 |
| Total revenues | 1,555,342 | 1,579,215 |
| Production costs |  |  |
| Wages and benefits | 363,051 | 354,516 |
| Raw materials | 72,325 | 77,176 |
| Other | 192,728 | 186,120 |
| Total production costs | 628,104 | 617,812 |
| Selling, general and administrative costs | 721,083 | 713,837 |
| Depreciation and amortization | 61,723 | 61,597 |
| Total operating costs | 1,410,910 | 1,393,246 |
| Restructuring charge | 14,804 | 0 |
| Multiemployer pension plan withdrawal expense | 6,730 | 9,055 |
| Pension settlement charges | 21,294 | 40,329 |
| Early termination charge | 0 | 0 |
| Operating profit | 101,604 | 136,585 |
| Loss from joint ventures | (36,273) | (783) |
| Interest expense, net | 34,805 | 39,050 |
| Income from continuing operations before income taxes | 30,526 | 96,752 |
| Income tax expense/(benefit) | 4,421 | 33,910 |
| Income from continuing operations | 26,105 | 62,842 |
| Loss from discontinued operations, net of income taxes | (2,273) | 0 |
| Net income | 23,832 | 62,842 |
| Net loss attributable to the noncontrolling interest | 5,236 | 404 |
| Net income attributable to The New York Times Company common stockholders | $29,068 | $63,246 |

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|  |  |  |
| --- | --- | --- |
| The New York Times Company  Consolidated Balance Sheets | | |
|  | As of | |
| *(in thousands)* | Dec. 29, 2016 | Dec. 30, 2015 |
|  |  |  |
| Cash and cash equivalents | $ 100,692 | $ 105,776 |
| Short-term investments | 449,535 | 507,639 |
| Accounts receivable, net | 197,355 | 207,180 |
| Prepaid assets | 15,948 | 19,430 |
| Other current assets | 32,648 | 22,507 |
| Total current assets | 796,178 | 862,532 |
| Long-term marketable securities | 187,299 | 291,136 |
| Investments in joint ventures | 15,614 | 22,815 |
| Property plant and equipment, net | 596,743 | 632,439 |
| Goodwill | 134,517 | 109,085 |
| Deferred income taxes | 301,342 | 309,142 |
| Miscellaneous assets | 153,702 | 190,541 |
| Total assets | $2,185,395 | $2,417,690 |
|  |  | |
| Accounts payable | $ 104,463 | $ 96,082 |
| Accrued payroll and other related liabilities | 96,463 | 98,256 |
| Unexpired subscriptions | 66,686 | 60,184 |
| Current portion of long-term debt | 0 | 188,377 |
| Accrued expenses and other | 131,125 | 120,686 |
| Total current liabilities | 398,737 | 563,585 |
|  |  |  |
| Long-term debt and capital lease obligations | 246,978 | 242,851 |
| Pension benefits obligation | 558,790 | 627,697 |
| Postretirement benefits obligation | 57,999 | 62,879 |
| Other | 78,647 | 92,223 |
| Total other liabilities | 942,414 | 1,025,650 |
|  |  |  |
| Stockholders’ equity |  |  |
| Common stock of $0.10 par value |  |  |
| Class A common stock | 16,921 | 16,826 |
| Class B convertible stock | 82 | 82 |
| Additional paid-in capital | 149,928 | 146,348 |
| Retained earnings | 1,331,911 | 1,328,744 |
| Common stock held in treasury, at cost | (171,211) | (156,155) |
| Accumulated other comprehensive loss, net of tax | (479,816) | (509,094) |
| Total New York Times Company stockholders’ equity | 847,815 | 826,751 |
| Noncontrolling interest | (3,571) | 1,704 |
| Total stockholders’ equity | 844,244 | 828,455 |
| Total liabilities and stockholders’ equity | $2,185,395 | $2,417,690 |

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*Required:*

a. Compute net operating profit after tax (NOPAT) for 2016 and 2015. Assume that combined federal and state statutory tax rates are 37% for both years.

b. Compute net operating assets (NOA) for 2016 and 2015.

c. Compute return on net operating assets (RNOA) for 2016 and 2015. Net operating assets are $397,299 thousand in 2014.

d. Compute return on common shareholders equity (ROE) for 2016 and 2015. Stockholders’ equity attributable to New York Times Company in 2014 is $726,328 thousand.

e. What is nonoperating return component of ROE for 2016 and 2015?

f. Comment on the difference between ROE and RNOA. What inference do you draw from this comparison?

BONUS: 5 POINTS

Income statements and balance sheets follow for Microsoft Corporation and Apple Inc. Refer to these financial statements to answer the requirements.

|  |  |  |
| --- | --- | --- |
| MICROSOFT CORPORATION  Income Statements  For the years ended June 30, | | |
| *(in millions)* | 2016 | 2015 |
| Revenue |  |  |
| Product | $61,502 | $75,956 |
| Service | 23,818 | 17,624 |
| Total revenue | 85,320 | 93,580 |
| Cost of revenue |  |  |
| Product | 17,880 | 21,410 |
| Service and other | 14,900 | 11,628 |
| Total cost of revenue | 32,780 | 33,038 |
| Gross margin | 52,540 | 60,542 |
| Research and development | 11,988 | 12,046 |
| Sales and marketing | 14,697 | 15,713 |
| General and administrative | 4,563 | 4,611 |
| Impairment, integration, and restructuring | 1,110 | 10,011 |
| Operating income | 20,182 | 18,161 |
| Dividends and interest income | 903 | 766 |
| Interest expense | (1,243) | (781) |
| Other income (expense), net | (91) | 361 |
| Income before taxes | 19,751 | 18,507 |
| Provision for income taxes | 2,953 | 6,314 |
| Net income | $16,798 | $ 12,193 |

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|  |  |  |
| --- | --- | --- |
| MICROSOFT CORPORATION  Balance Sheet  As of June 30, | | |
| *(in millions)* | 2016 | 2015 |
| Current assets: |  |  |
| Cash and cash equivalents | $ 6,510 | $ 5,595 |
| Short-term investments | 106,730 | 90,931 |
| Accounts receivable, net | 18,277 | 17,908 |
| Inventories | 2,251 | 2,902 |
| Other current assets | 5,892 | 5,461 |
| Total current assets | 139,660 | 122,797 |
| Property and equipment, net | 18,356 | 14,731 |
| Equity and other investments | 10,431 | 12,053 |
| Goodwill | 17,872 | 16,939 |
| Intangible assets, net | 3,733 | 4,835 |
| Other long-term assets | 3,642 | 3,117 |
| Total assets | $193,694 | $174,472 |
| Current liabilities: |  |  |
| Accounts payable | $ 6,898 | $ 6,591 |
| Short-term debt | 12,904 | 4,985 |
| Current portion of long-term debt | 0 | 2,499 |
| Accrued compensation | 5,264 | 5,096 |
| Income taxes | 580 | 606 |
| Short-term unearned revenue | 27,468 | 23,223 |
| Other current liabilities | 6,243 | 6,647 |
| Total current liabilities | 59,357 | 49,647 |
| Long-term debt | 40,783 | 27,808 |
| Long-term unearned revenue | 6,441 | 2,095 |
| Deferred income taxes | 1,476 | 1,295 |
| Other long-term liabilities | 13,640 | 13,544 |
| Total liabilities | 121,697 | 94,389 |
| Stockholders' equity: |  |  |
| Common stock and paid-in capital | 68,178 | 68,465 |
| Retained earnings | 2,282 | 9,096 |
| Accumulated other comprehensive income | 1,537 | 2,522 |
| Total stockholders' equity | 71,997 | 80,083 |
| Total liabilities and stockholders' equity | $193,694 | $ 174,472 |

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|  |  |  |
| --- | --- | --- |
| Apple Inc.  Consolidated Statement of Operations | | |
|  | Fiscal year ended | |
| *(in millions)* | Sept. 24, 2016 | Sept. 26, 2015 |
| Net sales | $ 215,639 | $ 233,715 |
| Cost of sales | 131,376 | 140,089 |
| Gross margin | 84,263 | 93,626 |
| Operating expenses |  |  |
| Research and development | 10,045 | 8,067 |
| Selling, general and administrative | 14,194 | 14,329 |
| Total operating expenses | 24,239 | 22,396 |
| Operating income | 60,024 | 71,230 |
| Interest and dividend income | 3,999 | 2,921 |
| Interest expense | (1,456) | (733) |
| Other expense, net | (1,195) | (903) |
| Income before provision for income taxes | 61,372 | 72,515 |
| Provision for income taxes | 15,685 | 19,121 |
| Net income | $ 45,687 | $ 53,394 |

|  |  |  |
| --- | --- | --- |
| Apple Inc.  Consolidated Balance Sheets | | |
|  | As of | |
| *(in thousands)* | Sept. 24, 2016 | Sept. 26, 2015 |
|  |  |  |
| Cash and cash equivalents | $ 20,484 | $ 21,120 |
| Short-term investments | 46,671 | 20,481 |
| Accounts receivable, net | 15,754 | 16,849 |
| Inventories | 2,132 | 2,349 |
| Other current assets | 21,828 | 28,579 |
| Total current assets | 106,869 | 89,378 |
| Long-term marketable securities | 170,430 | 164,065 |
| Property plant and equipment, net | 27,010 | 22,471 |
| Goodwill | 5,414 | 5,116 |
| Acquired intangible assets, net | 3,206 | 3,893 |
| Other assets | 8,757 | 5,422 |
| Total assets | 321,686 | 290,345 |
|  |  | |

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|  |  |  |
| --- | --- | --- |
| Apple Inc.  Consolidated Balance Sheets—continued | | |
|  | As of | |
| *(in thousands)* | Sept. 24, 2016 | Sept. 26, 2015 |
|  |  |  |
| Accounts payable | 37,294 | 35,490 |
| Accrued expenses | 22,027 | 25,181 |
| Deferred revenue | 8,080 | 8,940 |
| Current portion of LT debt and short-term debt | 11,605 | 10,999 |
| Total current liabilities | 79,006 | 80,610 |
|  |  |  |
| Deferred revenue – non-current | 2,930 | 3,624 |
| Long-term debt | 75,427 | 53,329 |
| Other non-current liabilities | 36,074 | 33,427 |
| Total liabilities | 193,437 | 170,990 |
|  |  |  |
| Stockholders’ equity |  |  |
| Common stock no par value | 31,251 | 27,416 |
| Retained earnings | 96,364 | 92,284 |
| Accumulated other comprehensive income (loss) | 634 | (345) |
| Total stockholders’ equity | 128,249 | 119,355 |
| Total liabilities and stockholders’ equity | $ 321,686 | $ 290,345 |

*Required:*

a. Compute the current ratio and quick ratio for both firms for fiscal 2016. Compare the ratios and determine which company is more liquid.

b. Compute the times interest earned and liabilities-to-equity ratios for both firms for fiscal 2016. Which company is more solvent?

c. Do you have any concerns about either company’s ability to meet its debt obligations? Explain.