Chapter 3 (week 4 lecture)

Tutorial question (P3-4A, P3-8A)

P3–4A Buzzard Bicycle specializes in custom painting and design of bicycles. December 31 is the company's fiscal year-end. Information necessary to prepare the year-end adjusting entries appears below.

1. A three-year fire insurance policy was purchased on July 1, 2024, for $18,000. The company debited Prepaid Insurance for the entire amount on July 1.

2. Employee salaries of $25,000 for the month of December will be paid in early January.

3. On November 1, 2024, the company received $6,000 in cash from a customer requesting a custom design for six identical bikes ($1,000 each). Deferred Revenue was credited for the entire amount on November 1. By the end of the year, four of the bikes have been completed.

4. Supplies at the beginning of the year totaled $2,000. During 2024, additional supplies of $18,000 were purchased, and the entire amount was debited to Supplies at the time of purchase. Supplies remaining at the end of the year total $4,000.

5. Buzzard paid a local radio station $12,000 for four months of advertising on December 1, 2024. The advertising will appear evenly over the four-month period. The company debited Prepaid Advertising for the entire amount on December 1.

6. Buzzard borrowed $36,000 on March 1, 2024. The Principal is due to be paid in five years. Interest is payable each March 1 at an annual rate of 10%.

Required:

Record the necessary adjusting entries on December 31, 2024.

P3–8A The general ledger of Red Storm Cleaners at January 1, 2024, includes the following account balances:

Accounts	Debits	Credits
Cash	$20,000	
Accounts Receivable	8,000	
Supplies	4,000	
Equipment	15,000	
Accumulated Depreciation		$ 5,000
Salaries Payable		7,500
Common Stock		25,000
Retained Earnings		9,500
Totals	$47,000	$47,000

The following is a summary of the transactions for the year:

1. March	12	Provide services to customers, $60,000, of which $21,000 is on account.
2. May	2	Collect on accounts receivable, $18,000.
3. June	30	Issue shares of common stock in exchange for $6,000 cash.
4. August	1	Pay salaries, $7,500 from 2023 (prior year).
5. September	25	Pay repairs and maintenance expenses, $13,000.
6. October	19	Purchase equipment for $8,000 cash.
7. December	30	Pay $1,100 cash dividends to stockholders.

Required:

1. Set up the necessary T-accounts and enter the beginning balances from the trial balance. In addition to the accounts shown, the company also has accounts for Dividends, Service Revenue, Salaries Expense, Repairs and Maintenance Expense, Depreciation Expense, and Supplies Expense.
2. Record each of the summary transactions listed above.
3. Post the transactions to the accounts.
4. Prepare an unadjusted trial balance.
5. Record adjusting entries. Accrued salaries at year-end amounted to $19,600. Depreciation for the year on the equipment is $5,000. Office supplies remaining on hand at the end of the year equal $1,200.
6. Post adjusting entries.
7. Prepare an adjusted trial balance.
8. Prepare an income statement for 2024 and a classified balance sheet as of December 31, 2024.
9. Record closing entries.
10. Post closing entries.
11. Prepare a post-closing trial balance.

Take-home question (P3-3A, P3-7A, RWP3-6)

P3–3A The information necessary for preparing the 2024 year-end adjusting entries for Gamecock Advertising Agency appears below. Gamecock's fiscal year-end is December 31.

1. On July 1, 2024, Gamecock receives $6,000 from a customer for advertising services to be given evenly over the next 10 months. Gamecock credits Deferred Revenue on July 1.
2. At the end of the yera, income taxes owed are $7,000.
3. On May 1, 2024, the company paid $4,800 for a two-year fire and liability insurance policy. The company debited Prepaid Insurance on May 1.
4. On September 1, 2024, the company borrowed $20,000 from a local bank and signed a note. Principal and interest at 12% will be paid on August 31, 2025.
5. At year-end there is a $2,700 debit balance in the Supplies (asset) account. Only $1,000 of supplies remains on hand at the end of the year.

Required:

Record the necessary adjusting entries on December 31, 2024. No prior adjustments have been made during 2024.

P3–7A Crimson Tide Music Academy offers lessons in playing a wide range of musical instrucments. The unadjusted trial balance as of December 31, 2024, appears below. December 31 is the company's fisal year-end.

Accounts	Debit	Credit
Cash	$ 10,300	
Accounts Receivable	9,500	
Interest Receivable	-0-	
Supplies	2,000	
Prepaid Rent	7,200	
Land	78,000	
Notes Receivable	20,000	
Accounts Payable		$ 7,700
Salaries Payable		-0-
Deferred Revenue		5,300
Utilities Payable		-0-
Common Stock		79,000
Retained Earnings		19,700
Service Revenue		42,200
Interest Revenue		-0-
Salaries Expense	24,500	
Rent Expense	-0-	
Supplies Expense	-0-	
Utilities Expense	2,400	
Totals	$153,900	$153,900

In addition the company had the following year-end adjusting entries.

	Debit	Credit
a. Salaries Expense	2,100	
Salaries Payable		2,100
b. Interest Receivable	800	
Interest Revenue		800
c. Supplies Expense	1,300	
Supplies		1,300
d. Deferred Revenue	3,300	
Service Revenue		3,300
e. Rent Expense	5,400	
Prepaid Rent		5,400
f. Utilities Expense	200	
Utilities Payable		200

P3–7A (continued)

Required:

Complete the following steps:

1. Enter the unadjusted balances from the trial balance into T-accounts.

2. Post the adjusing entries to the accounts.

3. Prepare an adjusted trial balance.

4. Prepare an income statement and a statement of shareholders' equity for the year ended December 31, 2024, and a classified balance sheet as of December 31,2024. Assume that no common stock is issued during the year.

5. Record closing entries.

6. Post closing entries to the accounts.

7. Prepare a post-closing trial balance.

Ethics

RWP3–6 You have recently been hired as the assistant controller for Stanton Temperton Corporation, which rents building space in major metropolitan areas. Customers are required to pay six months of rent in advance. At the end of 2024, the company's president, Jim Temperton, notices that net income has fallen compared to last year. In 2023, the company reported pretax profit of $330,000, but in 2024 the pretax profit is only $280,000. This concerns Jim for two reasons. First, his year-end bonus is tied directly to pretax profits. Second, shareholders may see a decline in profitability as a weakness in the company and begin to sell their stock. With the sell-off of stock, Jim's personal investment in the company's stock, as well as his company-operated retirement plan, will be in jeopardy of severe losses.

After close inspection of the financial statements, Jim notices that the balance of the Deferred Revenue account is $120,000. This amount represents payments in advance from long-term customers ($80,000) and from relatively new customers ($40,000). Jim comes to you, the company's accountant, and suggests that the company should recognize as revenue in 2024 the $80,000 received in advance from long-term customers. He offers the following explanation: “First, we have received these customers' cash by the end of 2024, so there is no question about their ability to pay. Second, we have a long-term history of fulfilling our obligation to these customers. We have always stood by our commitments to our customers and we always will. We earned that money when we got them to sign the six-month contract.”

Required:

1. Understand the reporting effect: What are the effects on pretax profits of reporting the $80,000 as service revenue?
2. Specify the options: Instead of reporting the $80,000 as revenue, how else might you report this amount?
3. Identify the impact: Are investors and creditors potentially affected by Jim's suggestion?
4. Make a decision: As a staff employee, should you follow Jum's suggestion?