PRACTICE MULTIPLE-CHOICE QUESTIONS

**2-1.** (LO 1)

Which of the following statements about an account is **true**?

(a) The right side of an account is the debit or increase side.

(b) An account is an individual accounting record of increases and decreases in specific asset, liability, and equity items.

(c) There are separate accounts for specific assets and liabilities but only one account for equity items.

(d) The left side of an account is the credit or decrease side.

**Answer**

(b) An account is an individual accounting record of increases and decreases in specific asset, liability, and equity items.

**2-2.** (LO 2)

Debits:

(a) increase both assets and liabilities.

(b) decrease both assets and liabilities.

(c) increase assets and decrease liabilities.

(d) decrease assets and increase liabilities.

**Answer**

(c) increase assets and decrease liabilities.

**2-3.** (LO 2)

A revenue account:

(a) is increased by debits.

(b) is decreased by credits.

(c) has a normal balance of a debit.

(d) is increased by credits.

**Answer**

(d) is increased by credits.

**2-4.** (LO 2)

Accounts that normally have debit balances are:

(a) assets, expenses, and revenues.

(b) assets, expenses, and share capital—ordinary.

(c) assets, liabilities, and dividends.

(d) assets, dividends, and expenses.

**Answer**

(d) assets, dividends, and expenses.

**2-5.** (LO 2)

The expanded accounting equation is:

(a) Assets + Liabilities = Share Capital + Retained Earnings + Dividends + Revenues + Expenses.

(b) Assets = Liabilities + Share Capital + Retained Earnings + Dividends + Revenues − Expenses.

(c) Assets = Liabilities − Share Capital − Retained Earnings − Dividends − Revenues – Expenses.

(d) Assets = Liabilities + Share Capital + Retained Earnings + Revenues – Expenses – Dividends.

**Answer**

(d) Assets = Liabilities + Share Capital + Retained Earnings + Revenues – Expenses – Dividends.

**2-6.** (LO 3)

Which of the following is **not**part of the recording process?

(a) Analyzing transactions.

(b) Preparing a trial balance.

(c) Entering transactions in a journal.

(d) Posting transactions.

**Answer**

(b) Preparing a trial balance.

**2-7.** (LO 4)

Which of the following statements about a journal is **false**?

(a) It is not a book of original entry.

(b) It provides a chronological record of transactions.

(c) It helps to locate errors because the debit and credit amounts for each entry can be readily compared.

(d) It discloses in one place the complete effect of a transaction.

**Answer**

(a) It is not a book of original entry.

**2-8.** (LO 4)

The purchase of supplies on account should result in:

(a) a debit to Supplies Expense and a credit to Cash.

(b) a debit to Supplies Expense and a credit to Supplies.

(c) a debit to Supplies and a credit to Accounts Payable.

(d) a debit to Supplies and a credit to Accounts Receivable.

**Answer**

(c) a debit to Supplies and a credit to Accounts Payable.

**2-9.** (LO 5)

A ledger:

(a) contains only asset and liability accounts.

(b) should show accounts in alphabetical order.

(c) is a collection of the entire group of accounts maintained by a company.

(d) is a book of original entry.

**Answer**

(c) is a collection of the entire group of accounts maintained by a company.

**2-10.** (LO 6)

Posting:

(a) normally occurs before journalizing.

(b) transfers ledger transaction data to the journal.

(c) is an optional step in the recording process.

(d) transfers journal entries to ledger accounts.

**Answer**

(d) transfers journal entries to ledger accounts.

**2-11.** (LO 6)

Before posting a payment of €5,000, the Accounts Payable of Senator Company had a normal balance of €16,000. The balance after posting this transaction was:

(a) €21,000.

(b) €5,000.

(c) €11,000.

(d) Cannot be determined.

**Answer**

(c) €11,000.

**2-12.** (LO 7)

A trial balance:

(a) is a list of accounts with their balances at a given time.

(b) proves the mathematical accuracy of journalized transactions.

(c) will not balance if a correct journal entry is posted twice.

(d) proves that all transactions have been recorded.

**Answer**

(a) is a list of accounts with their balances at a given time.

**2-13.** (LO 7)

A trial balance will not balance if:

(a) a correct journal entry is posted twice.

(b) the purchase of supplies on account is debited to Supplies and credited to Cash.

(c) a £100 cash dividend is debited to Dividends for £1,000 and credited to Cash for £100.

(d) a £450 payment on account is debited to Accounts Payable for £45 and credited to Cash for £45.

**Answer**

(c) a £100 cash dividend is debited to Dividends for £1,000 and credited to Cash for £100.

**2-14.** (LO 7)

The trial balance of Clooney Ltd. had accounts with the following normal balances: Cash £5,000, Service Revenue £85,000, Salaries and Wages Payable £4,000, Salaries and Wages Expense £40,000, Rent Expense £10,000, Share Capital—Ordinary £42,000, Dividends £15,000, and Equipment £61,000. In preparing a trial balance, the total in the debit column is:

(a) £131,000.

(b) £216,000.

(c) £91,000.

(d) £116,000.

**Answer**

(a) £131,000.

QUESTIONS

**2-1.** Describe the parts of a T-account.

**2-2.** “The terms *debit* and *credit* mean increase and decrease, respectively.” Do you agree? Explain.

**2-3.** Jason Hilbert, a fellow student, contends that the double-entry system means each transaction must be recorded twice. Is Jason correct? Explain.

**2-4.** Sandra Browne, a beginning accounting student, believes debit balances are favorable and credit balances are unfavorable. Is Sandra correct? Discuss.

**2-5.** State the rules of debit and credit as applied to (a) asset accounts, (b) liability accounts, and (c) equity accounts (revenue, expenses, dividends, share capital—ordinary, and retained earnings).

**2-6.** What is the normal balance for each of the following accounts? (a) Accounts Receivable. (b) Cash. (c) Dividends. (d) Accounts Payable. (e) Service Revenue. (f) Salaries and Wages Expense. (g) Share Capital—Ordinary.

**2-7.** Indicate whether each of the following accounts is an asset, a liability, or an equity account and whether it has a normal debit or credit balance: (a) Accounts Receivable, (b) Accounts Payable, (c) Equipment, (d) Dividends, (e) Supplies.

**2-8.** For the following transactions, indicate the account debited and the account credited.

(a) Supplies are purchased on account.

(b) Cash is received on signing a note payable.

(c) Employees are paid salaries in cash.

**2-9.** Indicate whether the following accounts generally will have (a) debit entries only, (b) credit entries only, or (c) both debit and credit entries.

1. Cash.

2. Accounts Receivable.

3. Dividends.

4. Accounts Payable.

5. Salaries and Wages Expense.

6. Service Revenue.

**2-10.** What are the basic steps in the recording process?

**2-11.** What are the advantages of using a journal in the recording process?

**2-12.** (a) When entering a transaction in the journal, should the debit or credit be written first?

(b) Which should be indented, the debit or credit?

**2-13.** Describe a compound entry, and provide an example.

**2-14.** (a) Should business transaction debits and credits be recorded directly in the ledger accounts?

(b) What are the advantages of first recording transactions in the journal and then posting to the ledger?

**2-15.** The account number is entered as the last step in posting the amounts from the journal to the ledger. What is the advantage of this step?

**2-16.** Journalize the following business transactions.

(a) Alberto Rivera invests R$9,000 cash in the business in exchange for ordinary shares.

(b) Insurance of R$800 is paid for the year.

(c) Supplies of R$2,000 are purchased on account.

(d) Cash of R$7,500 is received for services rendered.

**2-17.** (a) What is a ledger?

(b) What is a chart of accounts and why is it important?

**2-18.** What is a trial balance and what are its purposes?

**2-19.** Joe Kirby is confused about how accounting information flows through the accounting system. He believes the flow of information is as follows.

(a) Debits and credits posted to the ledger.

(b) Business transaction occurs.

(c) Information entered in the journal.

(d) Financial statements are prepared.

(e) Trial balance is prepared.

Is Joe correct? If not, indicate to Joe the proper flow of the information.

**2-20.** Two students are discussing the use of a trial balance. They wonder whether the following errors, each considered separately, would prevent the trial balance from balancing. What would you tell them?

(a) The bookkeeper debited Cash for €600 and credited Salaries and Wages Expense for €600 for payment of wages.

(b) Cash collected on account was debited to Cash for €900 and Service Revenue was credited for €90.

**2-21.** What are the normal balances for TSMC's Cash, Accounts Payable, and Interest Expense accounts?

BRIEF EXERCISES

**BE1-1.** *Use basic accounting equation*.

(LO 6)

Presented below is the basic accounting equation (in thousands). Determine the missing amounts.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Assets** | **=** | **Liabilities** | **+** | **Equity** |
|  |  |  |  |  |  |
| (a) | ¥88,000 |  | ¥50,000 |  | ? |
| (b) | ? |  | ¥45,000 |  | ¥70,000 |
| (c) | ¥94,000 |  | ? |  | ¥60,000 |

**BE2-1.** *Indicate debit and credit effects and normal balance*.

(LO 2)

For each of the following accounts, indicate the effects of (a) a debit and (b) a credit on the accounts and (c) the normal balance of the account.

1. Accounts Payable.

2. Advertising Expense.

3. Service Revenue.

4. Accounts Receivable.

5. Share Capital—Ordinary.

6. Dividends.

**BE2-2.** *Identify accounts to be debited and credited*.

(LO 2)

Transactions for the Kaustav Sen Company ASA, which provides welding services, for the month of June are presented below. Identify the accounts to be debited and credited for each transaction.

June 1 Kaustav Sen invests €4,000 cash in exchange for ordinary shares in a small welding business.

2 Purchases equipment on account for €900.

3 €800 cash is paid to landlord for June rent.

12 Sent an invoice to L. Nigh €300 for welding work done on account.

**BE2-3.** *Journalize transactions*.

(LO 4)

Using the data in BE2-2, journalize the transactions. (You may omit explanations.)

**BE2-4.** *Identify and explain steps in recording process*.

(LO 3)

Tim Weber, a fellow student, is unclear about the basic steps in the recording process. Identify and briefly explain the steps in the order in which they occur.

**BE2-5.** *Indicate basic and debit-credit analysis*.

(LO 2)

J.A. Motzek SA has the following transactions during August of the current year. Indicate (a) the effect on the accounting equation and (b) the debit-credit analysis illustrated on pages 65-70 of the textbook.

Aug. 1 Opens an office as a financial advisor, investing R$5,000 in cash in exchange for ordinary shares.

4 Pays insurance in advance for 6 months, R$1,800 cash.

16 Receives R$1,100 from clients for services provided.

27 Pays secretary R$1,000 salary.

**BE2-6.** *Journalize transactions*.

(LO 4)

Using the data in BE2-5, journalize the transactions. (You may omit explanations.)

**BE2-7.** *Post journal entries to T-accounts*.

(LO 6)

Selected transactions for the Gilles Ltd. are presented in journal form on the next page. Post the transactions to T-accounts. Make one T-account for each item and determine each account's ending balance.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  |  |  | **J1** |
| **Date** | **Account Titles and Explanation** | **Ref.** | **Debit** | **Credit** |
| May 5 | Accounts Receivable |  | 5,000 |  |
|  | Service Revenue |  |  | 5,000 |
|  | (Billed for services provided) |  |  |  |
| 12 | Cash |  | 2,100 |  |
|  | Accounts Receivable |  |  | 2,100 |
|  | (Received cash in payment of account) |  |  |  |
| 15 | Cash |  | 3,000 |  |
|  | Service Revenue |  |  | 3,000 |
|  | (Received cash for services provided) |  |  |  |

**BE2-8.** *Post journal entries to standard form of account*.

(LO 6)

Selected journal entries for the Gilles Company are presented in BE2-7. Post the transactions using the standard form of account.

**BE2-9.** *Prepare a trial balance*.

(LO 7)

From the ledger balances given below, prepare a trial balance for the Starr SE at June 30, 2017. List the accounts in the order shown on page 73 of the textbook. All account balances are normal.

Accounts Payable €8,600, Cash €6,800, Share Capital—Ordinary €20,000, Dividends €800, Equipment €17,000, Service Revenue €6,000, Accounts Receivable €3,000, Salaries and Wages Expense €6,000, and Rent Expense €1,000.

**BE2-10.** *Prepare a correct trial balance*.

(LO 7)

An inexperienced bookkeeper prepared the following trial balance. Prepare a correct trial balance, assuming all account balances are normal.

|  |  |  |  |
| --- | --- | --- | --- |
| **Cheng Company**  **Trial Balance**  **December 31, 2017** | | | |
|  | **Debit** |  | **Credit** |
| Cash | £16,800 |  |  |
| Prepaid Insurance |  |  | £3,500 |
| Accounts Payable |  |  | 3,000 |
| Unearned Service Revenue | 4,200 |  |  |
| Share Capital—Ordinary |  |  | 13,000 |
| Dividends |  |  | 4,500 |
| Service Revenue |  |  | 25,600 |
| Salaries and Wages Expense | 18,600 |  |  |
| Rent Expense |  |  | 2,400 |
|  | £39,600 |  | £52,000 |

**DO IT! REVIEW**

**DO IT! 2-1.** *Identify normal balances*.

(LO 2)

Graham Kahl has just rented space in a strip mall. In this space, he will open a photography studio, to be called “Picture This!” A friend has advised Graham to set up a double-entry set of accounting records in which to record all of his business transactions.

Identify the statement of financial position accounts that Graham will likely need to record the transactions needed to open his business (a corporation). Indicate whether the normal balance of each account is a debit or credit.

**DO IT! 2-2.** *Record business activities*.

(LO 4)

Graham Kahl engaged in the following activities in establishing his photography studio, Picture This!:

1. Opened a bank account in the name of Picture This! and deposited £8,000 of his own money into this account in exchange for ordinary shares.

2. Purchased photography supplies at a total cost of £1,600. The business paid £400 in cash and the balance is on account.

3. Obtained estimates on the cost of photography equipment from three different manufacturers.

In what form (type of record) should Graham record these three activities? Prepare the entries to record the transactions.

**DO IT! 2-3.** *Post transactions*.

(LO 6)

Graham Kahl recorded the following transactions during the month of April.

|  |  |  |  |
| --- | --- | --- | --- |
| April 3 | Cash | 3,100 |  |
|  | Service Revenue |  | 3,100 |
|  |  |  |  |
| 16 | Rent Expense | 600 |  |
|  | Cash |  | 600 |
|  |  |  |  |
| 20 | Salaries and Wages Expense | 500 |  |
|  | Cash |  | 500 |

Post these entries to the Cash T-account of the general ledger to determine the ending balance in cash. The beginning balance in cash on April 1 was £1,600.

**DO IT! 2-4.** *Prepare a trial balance*.

(LO 7)

The following accounts are taken from the ledger of Chillin' Company SA at December 31, 2017.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| 200 | Notes Payable | R$20,000 |  | 101 | Cash | R$6,000 |
| 311 | Share Capital—Ordinary | 25,000 |  | 126 | Supplies | 5,000 |
| 157 | Equipment | 76,000 |  | 729 | Rent Expense | 2,000 |
| 332 | Dividends | 8,000 |  | 212 | Salaries and |  |
| 726 | Salaries and |  |  |  | Wages Payable | 3,000 |
|  | Wages Expense | 38,000 |  | 201 | Accounts Payable | 9,000 |
| 400 | Service Revenue | 86,000 |  | 112 | Accounts Receivable | 8,000 |

Prepare a trial balance in good form.

EXERCISES

**E2-1.** *Analyze statements about accounting and the recording process*.

(LO 1)

Larry Burns has prepared the following list of statements about accounts.

1. An account is an accounting record of either a specific asset or a specific liability.

2. An account shows only increases, not decreases, in the item it relates to.

3. Some items, such as cash and accounts receivable, are combined into one account.

4. An account has a left, or credit side, and a right, or debit side.

5. A simple form of an account, consisting of just the account title, the left side, and the right side, is called a T-account.

***Instructions***

Identify each statement as true or false. If false, indicate how to correct the statement.

**E2-2.** *Identify debits, credits, and normal balances*.

(LO 2)

Selected transactions for B. Madar, an interior decorating firm, in its first month of business, are shown below.

Jan. 2 Invested €15,000 cash in the business in exchange for ordinary shares.

3 Purchased used car for €7,000 cash for use in the business.

9 Purchased supplies on account for €500.

11 Billed customers €1,800 for services performed.

16 Paid €200 cash for advertising.

20 Received €700 cash from customers billed on January 11.

23 Paid creditor €300 cash on balance owed.

28 Declared and paid a €1,000 cash dividend.

***Instructions***

For each transaction indicate the following.

(a) The basic type of account debited and credited (asset, liability, equity).

(b) The specific account debited and credited (cash, rent expense, service revenue, etc.).

(c) Whether the specific account is increased or decreased.

(d) The normal balance of the specific account.

Use the following format, in which the January 2 transaction is given as an example.

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  | **Account Debited** | | | | | | |  | **Account Credited** | | | | | | |
|  |  | **(a)** |  | **(b)** |  | **(c)** |  | **(d)** |  | **(a)** |  | **(b)** |  | **(c)** |  | **(d)** |
| **Date** |  | **Basic Type** |  | **Specific Account** |  | **Effect** |  | **Normal Balance** |  | **Basic Type** |  | **Specific Account** |  | **Effect** |  | **Normal Balance** |
| Jan. 2 |  | Asset |  | Cash |  | Increase |  | Debit |  | Equity |  | Share Capital |  | Increase |  | Credit |

**E2-3.** *Journalize transactions*.

(LO 4)

Data for B. Madar SE, interior decorating, are presented in E2-2.

***Instructions***

Journalize the transactions using journal page J1. (You may omit explanations.)

**E2-4.** *Analyze transactions and determine their effect on accounts*.

(LO 2)

Presented below is information related to Beijing Real Estate Agency Ltd.

Oct. 1 Lynn Robbins begins business as a real estate agent with a cash investment of ¥200,000 in exchange for ordinary shares.

2 Hires an administrative assistant.

3 Purchases office furniture for ¥19,000, on account.

6 Sells a house and lot for N. Fennig; bills N. Fennig ¥32,000 for realty services provided.

27 Pays ¥8,500 on the balance related to the transaction of October 3.

30 Pays the administrative assistant ¥25,000 in salary for October.

***Instructions***

Prepare the debit-credit analysis for each transaction as illustrated on pages 63-68.

**E2-5.** *Journalize transactions*.

(LO 4)

Transaction data for Beijing Real Estate Agency Ltd. are presented in E2-4.

***Instructions***

Journalize the transactions. (You may omit explanations.)

**E2-6.** *Analyze transactions and journalize*.

(LO 2, 3, 4)

Minsk Industries OAO had the following transactions.

1. Borrowed pyб50,000 from the bank by signing a note.

2. Paid pyб25,000 cash for a computer.

3. Purchased pyб4,500 of supplies on account.

***Instructions***

(a) Indicate what accounts are increased and decreased by each transaction.

(b) Journalize each transaction. (Omit explanations.)

**E2-7.** *Analyze transactions and journalize*.

(LO 2, 3, 4)

Rockford Enterprises had the following selected transactions.

1. Kris Rockford invested £5,000 cash in the business in exchange for ordinary shares.

2. Paid office rent of £1,100.

3. Performed consulting services worth £4,700 on account.

4. Declared and paid a £400 cash dividend.

***Instructions***

(a) Indicate the effect each transaction has on the accounting equation (Assets = Liabilities + Equity), using plus and minus signs.

(b) Journalize each transaction. (Omit explanations.)

**E2-8.** *Analyze statements about the ledger*.

(LO 5)

Rachel Manny has prepared the following list of statements about the general ledger.

1. The general ledger contains all the asset and liability accounts, but no equity accounts.

2. The general ledger is sometimes referred to as simply the ledger.

3. The accounts in the general ledger are arranged in alphabetical order.

4. Each account in the general ledger is numbered for easier identification.

5. The general ledger is a book of original entry.

***Instructions***

Identify each statement as true or false. If false, indicate how to correct the statement.

**E2-9.** *Post journal entries and prepare a trial balance*.

(LO 6, 7)

Selected transactions from the journal of Roberta Mendez SLU, investment broker, are presented below.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Date** | **Account Titles and Explanation** | **Ref.** | **Debit** | **Credit** |
| Aug. 1 | Cash |  | 5,000 |  |
|  | Share Capital—Ordinary |  |  | 5,000 |
|  | (Investment of cash for shares) |  | 2,700 |  |
| 10 | Cash |  |  |  |
|  | Service Revenue |  |  | 2,700 |
|  | (Received cash for services provided) |  |  |  |
| 12 | Equipment |  | 5,000 |  |
|  | Cash |  |  | 1,500 |
|  | Notes Payable |  |  | 3,500 |
|  | (Purchased office equipment for cash and notes payable) |  |  |  |
| 25 | Accounts Receivable |  | 1,900 |  |
|  | Service Revenue |  |  | 1,900 |
|  | (Billed clients for services provided) |  |  |  |
| 31 | Cash |  | 850 |  |
|  | Accounts Receivable |  |  | 850 |
|  | (Receipt of cash on account) |  |  |  |

***Instructions***

(a) Post the transactions to T-accounts.

(b) Prepare a trial balance at August 31, 2017.

**E2-10.** *Journalize transactions from account data and prepare a trial balance*.

(LO 4, 7)

The T-accounts below summarize the ledger of Pierre Landscaping Company SA at the end of the first month of operations.

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Cash No. 101** | | | |  | **Unearned** | | | |
| 4/1 | 10,000 | 4/15 | 720 |  | **Service Revenue No. 209** | | | |
| 4/12 | 900 | 4/25 | 1,500 |  |  |  | 4/30 | 1,000 |
| 4/29 | 400 |  |  |  |  | | | |
| 4/30 | 1,000 |  |  |  | **Share Capital—Ordinary No. 311** | | | |
|  | | | |  |  |  | 4/1 | 10,000 |
| **Accounts Receivable No. 112** | | | |  |  | | | |
| 4/7 | 3,200 | 4/29 | 400 |  | **Service Revenue No. 400** | | | |
|  | | | |  |  |  | 4/7 | 3,200 |
| **Supplies No. 126** | | | |  |  |  | 4/12 | 900 |
| 4/4 | 1,800 |  |  |  |  | | | |
|  | | | |  | **Salaries and** | | | |
| **Accounts Payable No. 201** | | | |  | **Wages Expense No. 726** | | | |
| 4/25 | 1,500 | 4/4 | 1,800 |  | 4/15 | 720 |  |  |

***Instructions***

(a) Prepare the complete general journal (including explanations) from which the postings to Cash were made.

(b) Prepare a trial balance at April 30, 2017.

**E2-11.** *Journalize transactions from account data and prepare a trial balance*.

(LO 4, 7)

Presented below is the ledger for Sparks Co. Ltd.

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Cash No. 101** | | | |  | **Share Capital—Ordinary No. 311** | | | |
| 10/1 | 5,000 | 10/4 | 400 |  |  |  | 10/1 | 5,000 |
| 10/10 | 650 | 10/12 | 1,500 |  |  |  | 10/25 | 2,000 |
| 10/10 | 3,000 | 10/15 | 280 |  |  | | | |
| 10/20 | 500 | 10/30 | 300 |  | **Dividends No. 332** | | | |
| 10/25 | 2,000 | 10/31 | 600 |  | 10/30 | 300 |  |  |
|  | | | |  |  | | | |
| **Accounts Receivable No. 112** | | | |  | **Service Revenue No. 400** | | | |
| 10/6 | 800 | 10/20 | 500 |  |  |  | 10/6 | 800 |
| 10/20 | 940 |  |  |  |  |  | 10/10 | 650 |
|  | | | |  |  |  | 10/20 | 940 |
| **Supplies No. 126** | | | |  |  | | | |
| 10/4 | 400 |  |  |  | **Salaries and** | | | |
|  | | | |  | **Wages Expense No. 726** | | | |
| **Equipment No. 157** | | | |  | 10/31 | 500 |  |  |
| 10/3 | 2,000 |  |  |  |  | | | |
|  | | | |  | **Rent Expense No. 729** | | | |
| **Notes Payable No. 200** | | | |  | 10/15 | 280 |  |  |
|  |  | 10/10 | 3,000 |  |  | | | |
|  | | | |  |
| **Accounts Payable No. 201** | | | |  |
| 10/12 | 1,500 | 10/3 | 2,000 |  |

***Instructions***

(a) Reproduce the journal entries for the transactions that occurred on October 1, 10, and 20, and provide explanations for each.

(b) Determine the October 31 balance for each of the accounts above, and prepare a trial balance at October 31, 2017.

**E2-12.** *Prepare journal entries and post using standard account form*.

(LO 4, 6)

Selected transactions for Isabelle Rossini Company SpA during its first month in business are presented below.

Sept. 1 Invested €10,000 cash in the business in exchange for ordinary shares.

5 Purchased equipment for €12,000 paying €4,000 in cash and the balance on account.

25 Paid €2,400 cash on balance owed for equipment.

30 Declared and paid a €500 cash dividend.

Rossini's chart of accounts shows No. 101 Cash, No. 157 Equipment, No. 201 Accounts Payable, No. 311 Share Capital—Ordinary, No. 332 Dividends.

***Instructions***

(a) Journalize the transactions on page J1 of the journal. (Omit explanations.)

(b) Post the transactions using the standard account form.

**E2-13.** *Analyze errors and their effects on trial balance*.

(LO 7)

The bookkeeper for Arno Equipment Repair NV made a number of errors in journalizing and posting, as described below.

1. A credit posting of €400 to Accounts Receivable was omitted.

2. A debit posting of €750 for Prepaid Insurance was debited to Insurance Expense.

3. A collection from a customer of €100 in payment of its account owed was journalized and posted as a debit to Cash €100 and a credit to Service Revenue €100.

4. A credit posting of €300 to Property Taxes Payable was made twice.

5. A cash purchase of supplies for €250 was journalized and posted as a debit to Supplies €230 and a credit to Cash €230.

6. A debit of €495 to Advertising Expense was posted as €459.

***Instructions***

For each error:

(a) Indicate whether the trial balance will balance.

(b) If the trial balance will not balance, indicate the amount of the difference.

(c) Indicate the trial balance column that will have the larger total.

Consider each error separately. Use the following form, in which error (1) is given as an example.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  |  | **(a)** |  | **(b)** |  | **(c)** |
| **Error** |  | **In Balance** |  | **Difference** |  | **Larger Column** |
| (1) |  | No |  | $400 |  | debit |

**E2-14.** *Prepare a trial balance*.

(LO 2, 7)

The accounts in the ledger of Tempus Fugit Delivery Service Ltd. contain the following balances on July 31, 2017.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Accounts Receivable | £10,642 |  | Prepaid Insurance | £ 1,968 |
| Accounts Payable | 8,396 |  | Maintenance and Repairs Expense | 961 |
| Cash | ? |  | Service Revenue | 10,610 |
| Equipment | 49,360 |  | Dividends | 700 |
| Gasoline Expense | 758 |  | Share Capital—Ordinary | 40,000 |
| Utilities Expense | 523 |  | Salaries and Wages Expense | 4,428 |
| Notes Payable | 26,450 |  | Salaries and Wages Payable | 815 |
|  |  |  | Retained Earnings | 4,636 |

***Instructions***

Prepare a trial balance with the accounts arranged as illustrated in the chapter and fill in the missing amount for Cash.

**E2-15.** *Identify cash flow activities*.

(LO 7)

The statement of cash flows classifies each transaction as an operating activity, an investing activity, or a financing activity. Operating activities are the types of activities the company performs to generate profits. Investing activities include the purchase of long-lived assets such as equipment or the purchase of investment securities. Financing activities are borrowing money, issuing shares, and paying dividends.

Presented below are the following transactions.

1. Issued shares for €20,000 cash.

2. Issued note payable for €10,000 cash.

3. Purchased equipment for €11,000 cash.

4. Received €15,000 cash for services provided.

5. Paid €1,000 cash for rent.

6. Paid €600 cash dividend to shareholders.

7. Paid €6,500 cash for salaries.

***Instructions***

Classify each of these transactions as operating, investing, or financing activities.

PROBLEMS: SET A AND PROBLEMS: SET B

**Problems: Set A**

**P2-1A** *Journalize a series of transactions*.

(LO 2, 4)

Prairie Park ASA was started on April 1 by F. L. Wright and associates. The following selected events and transactions occurred during April.

Apr. 1 Shareholders invested €50,000 cash in the business in exchange for ordinary shares.

4 Purchased land costing €34,000 for cash.

8 Incurred advertising expense of €1,800 on account.

11 Paid salaries to employees €1,500.

12 Hired park manager at a salary of €4,000 per month, effective May 1.

13 Paid €1,500 cash for a one-year insurance policy.

17 Declared and paid a €1,400 cash dividend.

20 Received €6,400 in cash for admission fees.

25 Sold 100 coupon books for €30 each. Each book contains 10 coupons that entitle the holder to one admission to the park.

30 Received €8,500 in cash admission fees.

30 Paid €900 on balance owed for advertising incurred on April 8.

Prairie Park uses the following accounts: Cash, Prepaid Insurance, Land, Accounts Payable, Unearned Service Revenue, Share Capital—Ordinary, Dividends, Service Revenue, Advertising Expense, and Salaries and Wages Expense.

***Instructions***

Journalize the April transactions.

**P2-2A** *Journalize transactions, post, and prepare a trial balance*.

(LO 2, 4, 6, 7)

Lena Fohn is a licensed accountant. During the first month of operations of her business, Lena Fohn, AG, the following events and transactions occurred.

May 1 Shareholders invested €20,000 cash in exchange for ordinary shares.

2 Hired a secretary-receptionist at a salary of €2,000 per month.

3 Purchased €1,500 of supplies on account from Hartig Supply Company.

7 Paid office rent of €900 cash for the month.

11 Completed a tax assignment and billed client €2,800 for services provided.

12 Received €3,500 advance on a management consulting engagement.

17 Received cash of €1,200 for services completed for Lucille Co.

31 Paid secretary-receptionist €2,000 salary for the month.

31 Paid 40% of balance due Hartig Supply Company.

Lena uses the following chart of accounts: No. 101 Cash, No. 112 Accounts Receivable, No. 126 Supplies, No. 201 Accounts Payable, No. 209 Unearned Service Revenue, No. 311 Share Capital—Ordinary, No. 400 Service Revenue, No. 726 Salaries and Wages Expense, and No. 729 Rent Expense.

***Instructions***

(a) Journalize the transactions.

(b) Post to the ledger accounts.

(c) Prepare a trial balance on May 31, 2017.

Trial balance totals €28,400

**P2-3A** *Journalize and post transactions and prepare a trial balance*.

(LO 2, 4, 6, 7)

Sean Browne owns and manages a computer repair service, which had the following trial balance on December 31, 2016 (the end of its fiscal year).

|  |  |  |  |
| --- | --- | --- | --- |
| **BYTE REPAIR SERVICE, LTD.**  **Trial Balance**  **December 31, 2016** | | | |
| Cash | £8,000 |  |  |
| Accounts Receivable | 16,000 |  |  |
| Supplies | 13,000 |  |  |
| Prepaid Rent | 3,000 |  |  |
| Equipment | 24,000 |  |  |
| Accounts Payable |  |  | £19,000 |
| Share Capital—Ordinary |  |  | 33,000 |
| Retained Earnings |  |  | 12,000 |
|  | £64,000 |  | £64,000 |

Summarized transactions for January 2017 were as follows.

1. Advertising costs, paid in cash, £1,000.

2. Additional supplies acquired on account £4,000.

3. Miscellaneous expenses, paid in cash, £1,100.

4. Cash collected from customers in payment of accounts receivable £13,000.

5. Cash paid to creditors for accounts payable due £15,000.

6. Repair services performed during January: for cash £5,000; on account £9,000.

7. Wages for January, paid in cash, £3,000.

8. Dividends during January were £2,000.

***Instructions***

(a) Open T-accounts for each of the accounts listed in the trial balance, and enter the opening balances for 2017.

(b) Prepare journal entries to record each of the January transactions. (Omit explanations.)

(c) Post the journal entries to the accounts in the ledger. (Add accounts as needed.)

(d) Prepare a trial balance as of January 31, 2017.

Trial balance totals $63,000

**P2-4A** *Prepare a correct trial balance*

(LO 7)

The trial balance of the Jason Company Ltd. shown below does not balance.

|  |  |  |  |
| --- | --- | --- | --- |
| **JASON COMPANY LTD.**  **Trial Balance**  **May 31, 2017** | | | |
|  | **Debit** |  | **Credit** |
| Cash | £3,850 |  |  |
| Accounts Receivable |  |  | £ 2,750 |
| Prepaid Insurance | 700 |  |  |
| Equipment | 12,000 |  |  |
| Accounts Payable |  |  | 4,500 |
| Unearned Service Revenue | 560 |  |  |
| Share Capital—Ordinary |  |  | 11,700 |
| Service Revenue | 8,690 |  |  |
| Salaries and Wages Expense | 4,200 |  |  |
| Advertising Expense |  |  | 1,100 |
| Utilities Expense | 800 |  |  |
|  | £30,800 |  | £20,050 |

Your review of the ledger reveals that each account has a normal balance. You also discover the following errors.

1. The totals of the debit sides of Prepaid Insurance, Accounts Payable, and Utilities Expense were each understated £100.

2. Transposition errors were made in Accounts Receivable and Service Revenue. Based on postings made, the correct balances were £2,570 and £8,960, respectively.

3. A debit posting to Salaries and Wages Expense of £200 was omitted.

4. A £1,000 cash dividend was debited to Share Capital—Ordinary for £1,000 and credited to Cash for £1,000.

5. A £520 purchase of supplies on account was debited to Equipment for £520 and credited to Cash for £520.

6. A cash payment of £450 for advertising was debited to Advertising Expense for £45 and credited to Cash for £45.

7. A collection from a customer for £420 was debited to Cash for £420 and credited to Accounts Payable for £420.

***Instructions***

Prepare a correct trial balance. Note that the chart of accounts includes the following: Dividends and Supplies. (*Hint*: It helps to prepare the correct journal entry for the transaction described and compare it to the mistake made.)

Trial balance totals £26,720

**P2-5A** *Journalize transactions, post, and prepare a trial balance*.

(LO 2, 4, 6, 7)

The Classic Theater opened on April 1. All facilities were completed on March 31. At this time, the ledger showed No. 101 Cash €6,000, No. 140 Land €10,000, No. 145 Buildings (concession stand, projection room, ticket booth, and screen) €8,000, No. 157 Equipment €6,000, No. 201 Accounts Payable €2,000, No. 275 Mortgage Payable €8,000, and No. 311 Share Capital—Ordinary €20,000. During April, the following events and transactions occurred.

Apr. 2 Paid film rental of €800 on first movie.

3 Ordered two additional films at €1,000 each.

9 Received €1,800 cash from admissions.

10 Made €2,000 payment on mortgage and €1,000 for accounts payable due.

11 Classic Theater contracted with D. Zarle Company to operate the concession stand. Zarle is to pay 18% of gross concession receipts (payable monthly) for the rental of the concession stand.

12 Paid advertising expenses €300.

20 Received one of the films ordered on April 3 and was billed €1,000. The film will be shown in April.

25 Received €5,500 cash from admissions.

29 Paid salaries €1,600.

30 Received statement from D. Zarle showing gross concession receipts of €1,200 and the balance due to The Classic Theater of €216 (€1,200 × 18%) for April. Zarle paid one-half of the balance due and will remit the remainder on May 5.

30 Prepaid €1,300 rental on special film to be run in May.

In addition to the accounts identified above, the chart of accounts shows No. 112 Accounts Receivable, No. 136 Prepaid Rent, No. 400 Service Revenue, No. 429 Rent Revenue, No. 610 Advertising Expense, No. 726 Salaries and Wages Expense, and No. 729 Rent Expense.

***Instructions***

(a) Enter the beginning balances in the ledger as of April 1. Insert a check mark (✓) in the reference column of the ledger for the beginning balance.

(b) Journalize the April transactions.

(c) Post the April journal entries to the ledger. Assume that all entries are posted from page 1 of the journal.

(d) Prepare a trial balance on April 30, 2017.

Trial balance totals €35,516

**Problems: Set B**

**P2-1B** *Journalize a series of transactions*.

(LO 2, 4)

Surepar Disc Golf Course was opened on March 1 by Bill Arnsdorf. The following selected events and transactions occurred during March:

Mar. 1 Invested €60,000 cash in the business in exchange for ordinary shares.

3 Purchased Lee's Golf Land for €38,000 cash. The price consists of land €23,000, shed €9,000, and equipment €6,000. (Make one compound entry.)

5 Advertised the opening of the driving range and miniature golf course, paying advertising expenses of €1,300.

6 Paid cash €3,000 for a one-year insurance policy.

10 Purchased golf discs and other equipment for €1,050 from Parton Company payable in 30 days.

18 Received €440 in cash for golf fees earned.

19 Sold 100 coupon books for €18 each. Each book contains 4 coupons that enable the holder to play one round of disc golf.

25 Declared and paid an €800 cash dividend.

30 Paid salaries of €250.

30 Paid Parton Company in full.

31 Received €200 cash for fees earned.

Surepar uses the following accounts: Cash, Prepaid Insurance, Land, Buildings, Equipment, Accounts Payable, Unearned Service Revenue, Share Capital—Ordinary, Dividends, Service Revenue, Advertising Expense, and Salaries and Wages Expense.

***Instructions***

Journalize the March transactions.

**P2-2B** *Journalize transactions, post, and prepare a trial balance*.

(LO 2, 4, 6, 7)

Judi Dench is a licensed dentist. During the first month of the operation of her business, the following events and transactions occurred.

April 1 Shareholders invested £40,000 cash in exchange for ordinary shares.

1 Hired a secretary-receptionist at a salary of £600 per week payable monthly.

2 Paid office rent for the month £1,400.

3 Purchased dental supplies on account from Halo Company £5,200.

10 Provided dental services and billed insurance companies £6,600.

11 Received £1,000 cash advance from Rich Welk for an implant.

20 Received £2,100 cash for services completed and delivered to Phil Stueben.

30 Paid secretary-receptionist for the month £2,400.

30 Paid £1,900 to Halo Company for accounts payable due.

Judi uses the following chart of accounts: No. 101 Cash, No. 112 Accounts Receivable, No. 126 Supplies, No. 201 Accounts Payable, No. 209 Unearned Service Revenue, No. 311 Share Capital—Ordinary, No. 400 Service Revenue, No. 726 Salaries and Wages Expense, and No. 729 Rent Expense.

***Instructions***

(a) Journalize the transactions.

(b) Post to the ledger accounts.

(c) Prepare a trial balance on April 30, 2017.

Trial balance totals £53,000

**P2-3B** *Journalize transactions, post, and prepare a trial balance*.

(LO 2, 4, 6, 7)

Richardson Services Ltd. was formed on May 1, 2017. The following transactions took place during the first month.

Transactions on May 1:

1. Shareholders invested £50,000 cash in exchange for ordinary shares.

2. Hired two employees to work in the warehouse. They will each be paid a salary of £2,800 per month.

3. Signed a 2-year rental agreement on a warehouse; paid £24,000 cash in advance for the first year.

4. Purchased furniture and equipment costing £30,000. A cash payment of £8,000 was made immediately; the remainder will be paid in 6 months.

5. Paid £1,800 cash for a one-year insurance policy on the furniture and equipment.

Transactions during the remainder of the month:

6. Purchased basic office supplies for £750 cash.

7. Purchased more office supplies for £1,300 on account.

8. Total revenues earned were £20,000—£8,000 cash and £12,000 on account.

9. Paid £400 to suppliers for accounts payable due.

10. Received £3,000 from customers in payment of accounts receivable.

11. Received utility bills in the amount of £260, to be paid next month.

12. Paid the monthly salaries of the two employees, totalling £5,600.

***Instructions***

(a) Prepare journal entries to record each of the events listed. (Omit explanations.)

(b) Post the journal entries to T-accounts.

(c) Prepare a trial balance as of May 31, 2017.

Trial balance totals £93,160

**P2-4B** *Prepare a correct trial balance*.

(LO 7)

The trial balance of Mueller SE shown below does not balance.

|  |  |  |  |
| --- | --- | --- | --- |
| **MUELLER SE**  **Trial Balance**  **June 30, 2017** | | | |
|  | **Debit** |  | **Credit** |
| Cash |  |  | €3,840 |
| Accounts Receivable | € 2,898 |  |  |
| Supplies | 800 |  |  |
| Equipment | 3,000 |  |  |
| Accounts Payable |  |  | 2,666 |
| Unearned Service Revenue | 2,200 |  |  |
| Share Capital—Ordinary |  |  | 9,000 |
| Dividends | 800 |  |  |
| Service Revenue |  |  | 2,380 |
| Salaries and Wages Expense | 3,400 |  |  |
| Utilities Expense | 910 |  |  |
|  | €14,008 |  | €17,886 |

Each of the listed accounts has a normal balance per the general ledger. An examination of the ledger and journal reveals the following errors.

1. Cash received from a customer in payment of its account was debited for €570, and Accounts Receivable was credited for the same amount. The actual collection was for €750.

2. The purchase of a computer on account for €620 was recorded as a debit to Supplies for €620 and a credit to Accounts Payable for €620.

3. Services were performed on account for a client for €890. Accounts Receivable was debited for €890, and Service Revenue was credited for €89.

4. A debit posting to Salaries and Wages Expense of €700 was omitted.

5. A payment of a balance due for €309 was credited to Cash for €309 and credited to Accounts Payable for €390.

6. The payment of a €600 cash dividend was debited to Salaries and Wages Expense for €600 and credited to Cash for €600.

***Instructions***

Prepare a correct trial balance. (*Hint*: It helps to prepare the correct journal entry for the transaction described and compare it to the mistake made.)

Trial balance totals €16,348

**P2-5B** *Journalize transactions, post, and prepare a trial balance*.

(LO 2, 4, 6, 7)

The Wilson Theater Ltd., owned by Tegan Wilson, will begin operations in March. The Wilson will be unique in that it will show only triple features of sequential theme movies. As of March 1, the ledger of Wilson showed No. 101 Cash £7,000, No. 140 Land £22,000, No. 145 Buildings (concession stand, projection room, ticket booth, and screen) £10,000, No. 157 Equipment £8,000, No. 201 Accounts Payable £7,000, and No. 311 Share Capital—Ordinary £40,000. During the month of March, the following events and transactions occurred.

Mar. 2 Rented the three *Indiana Jones* movies to be shown for the first 3 weeks of March. The film rental was £3,500; £1,000 was paid in cash and £2,500 will be paid on March 10.

3 Ordered the *Lord of the Rings* movies to be shown the last 10 days of March. It will cost £240 per night.

9 Received £4,000 cash from admissions.

10 Paid balance due on *Indiana Jones* movies rental and £1,600 on March 1 accounts payable.

11 Wilson Theater contracted with M. Brewer to operate the concession stand. Brewer is to pay 15% of gross concession receipts (payable monthly) for the right to operate the concession stand.

12 Paid advertising expenses £450.

20 Received £4,400 cash from customers for admissions.

20 Received the *Lord of Rings* movies and paid the rental fee of £2,400.

31 Paid salaries of £2,500.

31 Received statement from M. Brewer showing gross receipts from concessions of £3,000 and the balance due to Wilson Theater of £450 (£3,000 × 15%) for March. Brewer paid one-half the balance due and will remit the remainder on April 5.

31 Received £9,000 cash from customers for admissions.

In addition to the accounts identified above, the chart of accounts includes No. 112 Accounts Receivable, No. 400 Service Revenue, No. 429 Rent Revenue, No. 610 Advertising Expense, No. 729 Rent Expense, and No. 726 Salaries and Wages Expense.

***Instructions***

(a) Enter the beginning balances in the ledger. Insert a check mark (✓) in the reference column of the ledger for the beginning balance.

(b) Journalize the March transactions.

(c) Post the March journal entries to the ledger. Assume that all entries are posted from page 1 of the journal.

(d) Prepare a trial balance on March 31, 2017.

Trial balance totals £63,250

MATCHA CREATIONS

(*Note*: This is a continuation of the Matcha Creations problem from Chapter 1.)

**MC2**After researching the different forms of business organization, Mei-ling Lee decides to operate “Matcha Creations” as a corporation. She then starts the process of getting the business running. In November 2017, the following activities take place.

Nov. 8 Mei-ling sells her investments for NT$520, which she deposits in her personal bank account.

8 She opens a bank account under the name “Matcha Creations” and transfers NT$500 from her personal account to the new account in exchange for ordinary shares.

11 Mei-ling pays NT$65 to have advertising brochures and posters printed. She plans to distribute these as opportunities arise. (*Hint*: Use Advertising Expense.)

13 She buys baking supplies, such as flour, sugar, butter, and chocolate chips, for NT$125 cash.

14 Mei-ling starts to gather some baking equipment to take with her when teaching the cookie classes. She has an excellent top-of-the-line food processor and mixer that originally cost her NT$750. Mei-ling decides to start using it only in her new business. She estimates that the equipment is currently worth NT$300. She invests the equipment in the business in exchange for ordinary shares.

16 Mei-ling realizes that her initial cash investment is not enough. Her grandmother lends her NT$2,000 cash, for which Mei-ling signs a note payable in the name of the business. Mei-ling deposits the money in the business bank account. (*Hint*: The note does not have to be repaid for 24 months. As a result, the notes payable should be reported in the accounts as the last liability and also on the statement of financial position as the last liability.)

17 She buys more baking equipment for NT$900 cash.

20 She teaches her first class and collects NT$125 cash.

25 Mei-ling books a second class for December 4 for NT$150. She receives NT$30 cash in advance as a down payment.

30 Mei-ling pays NT$1,320 for a one-year insurance policy that will expire on December 1, 2018.

***Instructions***

(a) Prepare journal entries to record the November transactions.

(b) Post the journal entries to general ledger accounts.

(c) Prepare a trial balance at November 30.

**Broadening Your Perspective**

Financial Reporting and Analysis

**BYP2-1. Financial Reporting Problem: TSMC, Ltd. (TWN)**

The financial statements of TSMC are presented in Appendix A. The notes accompanying the statements contain the following selected accounts. The complete annual report, including the notes to the financial statements, is available in the Investor Relations section of the company's website, *www.tsmc.com*.

|  |  |
| --- | --- |
| Accounts (Trade) Payable | Tax Payable |
| Accounts (Trade) Receivable | Interest Expense (finance cost) |
| Property, Plant, and Equipment | Inventories |

***Instructions***

(a) Answer the following questions.

(1) What is the increase and decrease side for each account?

(2) What is the normal balance for each account?

(b) Identify the probable other account in the transaction and the effect on that account when:

(1) Accounts (Trade) Receivable is decreased.

(2) Accounts (Trade) Payable is decreased.

(3) Inventories are increased.

(c) Identify the other account(s) that ordinarily would be involved when:

(1) Interest Expense is increased.

(2) Property, Plant, and Equipment is increased.

**BYP2-2. Comparative Analysis Problem: Nestlé SA (CHE) vs. Petra Foods Ltd. (SGP)**

Nestlé's financial statements are presented in Appendix B. Financial statements of Petra Foods are presented in Appendix C.

***Instructions***

(a) Based on the information contained in the financial statements, determine the normal balance of the listed accounts for each company.

|  |  |  |
| --- | --- | --- |
| **Nestlé** |  | **Petra Foods** |
| 1. Inventory |  | 1. Accounts (Trade) Receivable |
| 2. Property, Plant, and Equipment |  | 2. Cash and Cash Equivalents |
| 3. Accounts (Trade) Payable |  | 3. Cost of Goods Sold (expense) |
| 4. Interest Expense (finance cost) |  | 4. Sales (revenue) |

(b) Identify the other account ordinarily involved when:

1. Accounts (Trade) Receivable is increased.

2. Salaries and Wages Payable is decreased.

3. Property, Plant, and Equipment is increased.

4. Interest Expense is increased.

**BYP2-3. Real-World Focus**

Much information about specific companies is available on the Internet. Such information includes basic descriptions of the company's location, activities, industry, financial health, and financial performance.

***Address:* finance.yahoo.com/**, or go to **www.wiley.com/college/weygandt**

***Steps***

1. Type in a company name, or use index to find company name.

2. Choose **Profile**. Perform instructions (a)-(c) below.

3. Click on the company's specific industry to identify competitors. Perform instructions (d)-(g) below.

***Instructions***

Answer the following questions.

(a) What is the company's industry?

(b) What was the company's total sales?

(c) What was the company's net income?

(d) What are the names of four of the company's competitors?

(e) Choose one of these competitors.

(f) What is this competitor's name? What were its sales? What was its net income?

(g) Which of these two companies is larger by size of sales? Which one reported higher net income?

Critical Thinking

**BYP1-4. Decision-Making Across the Organization**

Amy Torbert operates Hollins Riding Academy. The academy's primary sources of revenue are riding fees and lesson fees, which are paid on a cash basis. Amy also boards horses for owners, who are billed monthly for boarding fees. In a few cases, boarders pay in advance of expected use. For its revenue transactions, the academy maintains the following accounts: No. 1 Cash, No. 5 Boarding Accounts Receivable, No. 27 Unearned Boarding Revenue, No. 51 Riding Revenue, No. 52 Lesson Revenue, and No. 53 Boarding Revenue.

The academy owns 10 horses, a stable, a riding corral, riding equipment, and office equipment. These assets are accounted for in accounts No. 11 Horses, No. 12 Building, No. 13 Riding Corral, No. 14 Riding Equipment, and No. 15 Office Equipment.

For its expenses, the academy maintains the following accounts: No. 6 Hay and Feed Supplies, No. 7 Prepaid Insurance, No. 21 Accounts Payable, No. 60 Salaries Expense, No. 61 Advertising Expense, No. 62 Utilities Expense, No. 63 Veterinary Expense, No. 64 Hay and Feed Expense, and No. 65 Insurance Expense.

Amy makes periodic payments of cash dividends to shareholders. To record equity in the business and dividends, Torbert maintains three accounts: No. 50 Share Capital—Ordinary, No. 51 Retained Earnings, and No. 52 Dividends.

During the first month of operations, an inexperienced bookkeeper was employed. Amy Torbert asks you to review the following eight entries of the 50 entries made during the month. In each case, the explanation for the entry is correct.

|  |  |  |  |
| --- | --- | --- | --- |
| May 1 | Cash | 18,000 |  |
|  | Share Capital—Ordinary |  | 18000 |
|  | (Invested £18,000 cash in exchange for shares) |  |  |
| 5 | Cash | 250 |  |
|  | Riding Revenue |  | 250 |
|  | (Received £250 cash for lessons provided) |  |  |
| 7 | Cash | 500 |  |
|  | Boarding Revenue |  | 500 |
|  | (Received £500 for boarding of horses |  |  |
|  | beginning June 1) |  |  |
| 14 | Riding Equipment | 80 |  |
|  | Cash |  | 800 |
|  | (Purchased desk and other office |  |  |
|  | equipment for £800 cash) |  |  |
| 15 | Salaries Expense | 440 |  |
|  | Cash |  | 440 |
|  | (Issued dividend checks to shareholders) |  |  |
| 20 | Cash | 148 |  |
|  | Riding Revenue |  | 184 |
|  | (Received £184 cash for riding fees) |  |  |
| 30 | Veterinary Expense | 75 |  |
|  | Accounts Payable |  | 75 |
|  | (Received bill of £75 from veterinarian for |  |  |
|  | services rendered) |  |  |
| 31 | Hay and Feed Expense | 1,500 |  |
|  | Cash |  | 1,500 |
|  | (Purchased an estimated 2 months' supply |  |  |
|  | of feed and hay for £1,500) |  |  |

***Instructions***

With the class divided into groups, answer the following.

(a) Identify each journal entry that is correct. For each journal entry that is incorrect, prepare the entry that should have been made by the bookkeeper.

(b) Which of the incorrect entries would prevent the trial balance from balancing?

(c) What was the correct net income for May, assuming the bookkeeper reported net income of £4,600 after posting all 50 entries?

(d) What was the correct cash balance at May 31, assuming the bookkeeper reported a balance of £12,475 after posting all 50 entries (and the only errors occurred in the items listed above)?

**BYP2-5. Communication Activity**

Shandler's Maid Company offers home-cleaning service. Two recurring transactions for the company are billing customers for services rendered and paying employee salaries. For example, on March 15, bills totaling €6,000 were sent to customers and €2,000 was paid in salaries to employees.

***Instructions***

Write a memo to your instructor that explains and illustrates the steps in the recording process for each of the March 15 transactions. Use the format illustrated in the textbook under the heading, “The Recording Process Illustrated” (page 65).

**BYP2-6.** **Ethics Case**

Sara Rankin is the assistant chief accountant at Hokey Company Ltd., a manufacturer of computer chips and cellular phones. The company presently has total sales of €20 million. It is the end of the first quarter. Sara is hurriedly trying to prepare a general ledger trial balance so that quarterly financial statements can be prepared and released to management and the regulatory agencies. The total credits on the trial balance exceed the debits by €1,000. In order to meet the 4 p.m. deadline, Sara decides to force the debits and credits into balance by adding the amount of the difference to the Equipment account. She chose Equipment because it is one of the larger account balances; percentage-wise, it will be the least misstated. Sara “plugs” the difference! She believes that the difference will not affect anyone's decisions. She wishes that she had another few days to find the

error but realizes that the financial statements are already late.

***Instructions***

(a) Who are the stakeholders in this situation?

(b) What are the ethical issues involved in this case?

(c) What are Sara's alternatives?

A LOOK at U.S. GAAP

Companies that use GAAP follow the same set of procedures and records to keep track of transaction data as do IFRS companies. Thus, the material in Chapter 2 dealing with the account, general rules of debit and credit, and steps in the recording process—the journal, ledger, and chart of accounts—is the same under both GAAP and IFRS.

**Key Points**

* Both the IASB and FASB go beyond the basic definitions provided in this textbook for the key elements of financial statements, that is, assets, liabilities, equity, revenues, and expenses. The more substantive definitions, using the FASB definitional structure, are provided in the Chapter 1 *A Look at U.S. GAAP* section on page 50.
* In deciding whether the United States should adopt IFRS, some of the issues the SEC said should be considered are:
* Whether IFRS is sufficiently developed and consistent in application.
* Whether the IASB is sufficiently independent.
* Whether IFRS is established for the benefit of investors.
* The issues involved in educating investors about IFRS.
* The impact of a switch to IFRS on U.S. laws and regulations.
* The impact on companies including changes to their accounting systems, contractual arrangements, corporate governance, and litigation.
* The issues involved in educating accountants, so they can prepare statements under IFRS.

**Similarities**

* + A trial balance under GAAP follows the same format as shown in the textbook.
  + As shown in the textbook, currency signs are typically used only in the trial balance and the financial statements. The same practice is followed under GAAP, using the U.S. dollar. For example, the income statement shown below for Apple Inc. (USA) is denominated in its own currency—the U.S. dollar.

|  |  |
| --- | --- |
| **APPLE INC.**  Consolidated Statement of Operations  (in millions except per share data)  For the Year Ended September 28, 2013 | |
| Net sales | $170,910 |
| Cost of sales | 106,606 |
| Gross margin | 64,304 |
| Operating expenses: |  |
| Research and development | 4,475 |
| Selling, general and administrative | 10,830 |
| Total operating expenses | 15,305 |
| Operating income | 48,999 |
| Other income/(expense), net | 1,156 |
| Income before provision for income taxes | 50,155 |
| Provision for income taxes | 13,118 |
| Net income | $ 37,037 |

**Differences**

* + In the United States, equity is often referred to as either shareholders' equity or stockholders' equity, and Share Capital—Ordinary is referred to as Common Stock. The statement of financial position is often called the balance sheet in the United States.
  + Rules for accounting for specific events sometimes differ across countries. For example, IFRS companies rely less on historical cost and more on fair value than U.S. companies. Despite the differences, the double-entry accounting system is the basis of accounting systems worldwide.

**Looking to the Future**

The basic recording process shown in this textbook is followed by companies across the globe. It is unlikely to change in the future. The definitional structure of assets, liabilities, equity, revenues, and expenses may change over time as the IASB and FASB evaluate their overall conceptual framework for establishing accounting standards.

**GAAP Practice**

**GAAP Self-Test Questions**

**1.** Which statement is **correct**regarding GAAP?

(a) GAAP reverses the rules of debits and credits, that is, debits are on the right and credits are on the left.

(b) GAAP uses the same process for recording transactions as IFRS.

(c) The chart of accounts under GAAP is different because revenues follow assets.

(d) None of the above statements are correct.

**Answer**

(b) GAAP uses the same process for recording transactions as IFRS.

**2.** The expanded accounting equation under GAAP is as follows:

(a) Assets = Liabilities + Common Stock – Retained Earnings – Dividends + Revenues – Expenses.

(b) Assets + Liabilities = Common Stock + Retained Earnings – Dividends + Revenues – Expenses.

(c) Assets = Liabilities + Common Stock + Retained Earnings – Dividends + Revenues – Expenses.

(d) Assets = Liabilities + Common Stock – Retained Earnings – Dividends – Revenues – Expenses.

**Answer**

(c) Assets = Liabilities + Common Stock + Retained Earnings – Dividends + Revenues – Expenses.

**3.** A trial balance:

(a) is the same under GAAP and IFRS.

(b) proves that transactions are recorded correctly.

(c) proves that all transactions have been recorded.

(d) will not balance if a correct journal entry is posted twice.

**Answer**

(a) is the same under GAAP and IFRS.

**4.** One difference between GAAP and IFRS is that:

(a) IFRS uses accrual-accounting concepts, and GAAP uses primarily the cash basis of accounting.

(b) GAAP uses a different posting process than IFRS.

(c) IFRS uses more fair value measurements than GAAP.

(d) the limitations of a trial balance are different between GAAP and IFRS.

**Answer**

(c) IFRS uses more fair value measurements than GAAP.

**5.** The general policy for using proper currency signs (dollar, yen, pound, etc.) is the same for both GAAP and this textbook. This policy is as follows:

(a) Currency signs only appear in ledgers and journal entries.

(b) Currency signs are only shown in the trial balance.

(c) Currency signs are shown for all compound journal entries.

(d) Currency signs are shown in trial balances and financial statements.

**Answer**

(d) Currency signs are shown in trial balances and financial statements.

**GAAP Exercises**

**GAAP2-1.** Describe some of the issues the SEC must consider in deciding whether the United States should adopt IFRS.

**GAAP Financial Reporting Problem: Apple Inc. (USA)**

**GAAP2-2.** The financial statements of Apple Inc. are presented in Appendix D. The company's complete annual report, including the notes to its financial statements, is available at *http://investor.apple.com*.

***Instructions***

(a) Apple has the following selected accounts:

|  |  |
| --- | --- |
| Accounts Payable | Inventories |
| Accounts Receivable | Rent Revenue |
| Buildings | Rent Expense |

1. What is the increase and decrease side of each account?

2. What is the normal balance for each account?

(b) Identify the probable other account in the transaction and the effect on that account when:

1. Accounts Receivable is decreased.

2. Accounts Payable is decreased.

3. Inventories is increased.