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COURSE: Accounting 215D  
INSTRUCTOR: Bill Wells  
QUARTER: Autumn 2009

TEST: Second Examination  
DATE: November 16, 2009  
Version: ① 2

At what time does your quiz section meet? (Circle one time)      10:30      ① 11:30      12:30

By signing below, you acknowledge that you are a part of a learning community at the Foster School of Business that is committed to the academic standards of honesty, respect, and integrity, and that you adhered to these standards while completing this examination.

- You will need access to a hand-held calculator and pencil(s)/pen only to complete this examination; all other materials should be out of sight. Scratch work should be done on the examination.
- If you need clarification (e.g. definition of words, an unclear problem) during the test, raise your hand. We will help you as best we can; we will not, however, reteach any point.
- Do not make any unnecessary or unsupported assumptions. Select the best answer from the choices provided. You may omit explanations which otherwise should accompany journal entries. Unless indicated otherwise, multiple choice questions are worth 4 points.
- Unless indicated otherwise, all situations are subject to U.S. rules and procedures. Partial credit may be given on certain questions marked "PC" if all mathematical work is shown immediately below the problem or the narrative is close to the best answer. All answers recorded by you must be the result of only your own efforts.
- You have approximately 80 minutes to complete the test. When the end of the test is announced, you should **immediately stop your work**. Work after the exam has ended is not fair to other students who complete the test within the allotted time. If such work continues after the bell, it will be subject to point reduction at my discretion.
- BUDGET YOUR TIME WISELY. WE WISH YOU SUCCESS.

**FINANCIAL ACCOUNTING II (26)**

1. (22 – 1 POINT EACH) For each of the accounts listed below, indicate whether they would 1) not be closed at year-end, or 2) closed by debiting the account, or 3) closed by crediting the account. Enter only one check mark for each listed account/total/category (one check per line).

| ACCOUNT, TOTAL, CATEGORY   | Not Closed | Closed by crediting the account | Closed by debiting the account |
|--|------------|---------------------------------|--------------------------------|
| Accumulated depreciation   | ✓          |                                 |                                |
| Retained earnings at the end of fiscal year 2009                     |            |                                 | ✓                              |
| Dividends declared   |            |                                 | ✓                              |
| Supplies inventory   | ✓          |                                 |                                |
| Merchandise inventory  | ✓          |                                 |                                |
| Realized gain on selling a building                                  |            |                                 | ✓                              |
| Unearned revenue   | ✓          |                                 |                                |
| Prepaid advertising  | ✓          |                                 |                                |
| Depreciation expense   |            | ✓                               |                                |
| Long-term liabilities  | ✓          |                                 |                                |
| Buildings  | ✓          |                                 |                                |
| Cost of goods sold   |            | ✓                               |                                |
| Accounts receivable  | ✓          |                                 |                                |
| Paid in capital  | ✓          |                                 |                                |
| Dividends payable  | ✓          |                                 |                                |
| Supply expense   |            | ✓                               |                                |
| Accounts payable   | ✓          |                                 |                                |
| Sales Revenue  |            |                                 | ✓                              |
| Loss on sale of equipment  |            | ✓                               |                                |
| Extraordinary gain on insurance settlement                           |            |                                 | ✓                              |
| Unrealized price increase/decrease on available-for-sale investments | _____      | _____                           | _____                          |
| Unrealized gain on Trading securities                                |            |                                 | ✓                              |

2. Suppose, during the closing process using an Income Summary account (as you did in Team Assignment 2), you determined that the Income Summary account had a debit balance. What does that mean?
- a. A mistake was made
- ☒ b. Net income will be reported as a positive number
- c. A net loss will be reported
- d. After the closing process is complete, retained earnings should increase by that amount

ADJUSTMENTS (18)

3. (6PC) As a matter of policy, Nicole Inc. capitalizes all rent prepayments it receives, making any adjusting entries at the end of the fiscal year which occurs on December 31. On November 1, 2009, \$4,500 - three months rent - was received in advance of it being earned. What adjusting journal entry is needed on December 31, 2009?

~~Unearned Rev 4500~~  
~~UE Rev 4500~~

UE Rev 3000  
 Rev 3000

4. (6PC) Using the same facts as in question 3 above, what journal entry should have been made on December 31, 2009 assuming the receipt was originally "expensed" (put on the income statement.)

4 Rev ~~1500~~  
 Unearned Rev ~~1500~~

5. (2) True or False (circle one). Since the starting point and adjustments required in the two previous questions (3 and 4) are different, the ending balances at year-end in the affected accounts must therefore also be different.

0

6. (4) Adjustments (other than those made to revalue something such as cash) are made because the preparer of the statements is trying to apply certain principles correctly. Circle the letters that correspond to those two principles.

- a. Matching  
 b. Conservatism  
 c. Revenue Recognition  
 d. Going concern

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**INVESTMENTS (8)**

11. Use the information below to answer the questions which follow:

|               |  |
|---------------|--|
| 2007          | Purchased 1000 shares of stock in Andre Inc. for \$50 each     |
| 2007 year end | The market price per share of Andre Inc. had declined to \$40  |
| 2008 year end | The market price per share of Andre Inc. had increased to \$46 |
| 2009          | All shares in Andre Inc. were sold for \$48 per share          |

(1 EACH) What amount related to Andre investment would be included in ~~net~~ net income if the investment was considered to be trading (Col. 2) or available for sale (Col. 3) when purchased? (If the effect is negative, be sure to place a minus sign or parenthesis around the amount entered.) If the effect is zero, be sure to put a "0" in the cell; blank cells will be graded as incorrect.

| Column 1   | TRADING                      | AVAILABLE FOR SALE         |
|--|------------------------------|----------------------------|
| 2007 Net Income                                  | <del>(50,000)</del> (10,000) | <del>(50,000)</del> 0      |
| 2008 Net Income                                  | 6,000                        | 0                          |
| 2009 Net Income                                  | 2,000                        | <del>(2,000)</del> (2,000) |
| 2009 Ending total of all Owners' Equity accounts | (2,000) <del>46,000</del>    | <del>46,000</del> (2,000)  |

**CASH (6)**

12. Senait Inc. was in the middle of some big deal that had required it to place \$50,000 of its funds in an "escrow" account some months ago. The funds are still your funds but you cannot access them until the deal is done or abandoned (which is expected to occur about 10 months from the beginning of next fiscal year). Should the \$50,000 be:

- 4
- a. Excluded from the balance sheet altogether
  - b. Included on the balance sheet and shown as a long-term assets
  - c. Included on the balance sheet and shown on the "cash and equivalent"
  - ☒ d. Included on the balance sheet and shown as a current assets other than on the "cash and equivalent" line

13. (2) Using the definition provided by me in my overheads and COSTCO re: "cash equivalents", would an investment in 60-day Treasury Bills (debt issued by the US Government) be included as a cash equivalent and thus be included on the first line of a balance sheet? Yes or No (circle one)

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**RECEIVABLES (28)**

14. (6PC) Credit sales are recorded at the gross selling price. On July 10, a \$100 credit sale occurred that offered the customer payment terms of 3/15/n45. On July 23, your firm received payment from this customer, bringing its balance owing to zero. Record the journal entry needed on July 23rd?

Cash 97  
Less CDT (3)  
A/R 100      6

15. The information below is available to you just before making an adjusting entry relative to receivables:

|  |                        |
|--|------------------------|
| Total credit sales   | 10,000,000             |
| Accounts Receivable (end of year balance)                        | 2,300,000              |
| Allowance for Doubtful Accounts ( <u>before</u> adjusting entry) | 13,000 (debit balance) |

- a. (4PC) Assuming 1% of credit sales were estimated to result in bad debts, at what net realizable value will receivables be reported on the balance sheet?

| Allow BD | BD Exp  |
|----------|---------|
| 13,000   | 100,000 |
| 100,000  |         |
| 87,000   |         |

  

$$10,000,000 \times .01 = 100,000$$
  

|            |  |
|------------|--|
| 10,000,000 |  |
| - 100,000  |  |
|            |  |

  

|            |                  |
|------------|------------------|
| A/R        | 2,300,000        |
| (Allow BD) | (87,000)         |
| <u>NRV</u> | <u>2,213,000</u> |

- b. (6PC) Assuming an aging schedule estimated that \$57,000 of the outstanding receivables would not be collected, record the necessary adjusting entry.

|          |        |  |
|----------|--------|--|
| Allow BD | BD Exp | Bad Debt expense <del>70,000</del>       |
| 13,000   | 70,000 | Allowance for Bad Debt <del>70,000</del> |
| 70,000   |        |  |
| 57,000   |        |  |

- c. (2PC) In the prior question, a debit balance existed in the Allowance for Doubtful Accounts account before the end-of-period adjustment was recorded. What would cause this?

More than \$57,000 was written off to begin with.      2

16. (6PC) Using letters corresponding to the accounts below, indicate in the appropriate columns the accounts that should be debited or credited when correctly recording each given circumstance. Each block may contain more than one letter and each letter may be used more than once.

- A. Accounts Receivable  
B. Sales Revenue  
C. Cash

- D. Allowance for Bad Debts  
E. Bad Debts Expense

| CIRCUMSTANCE  | DEBIT  | CREDIT |
|---|--------|--------|
| a. Owing to some very bad decisions, one of your customers notified you that he was unable to pay what he owes your firm. While you thought he was more unwilling than unable, you wrote him and his account off. | D      | A      |
| b. Sometime after his account was written off, he made a partial payment. You believe the prospect of future payments looks good so you want to keep his remaining balance on your books.                         | A<br>C | D<br>A |

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17. (4PC) In the spaces below, construct the accounts receivable turnover ratio by describing what information should be used in the numerator and denominator of that ratio.

a. Numerator

~~Accounts Receivable~~

0 Sales Rev

b. Denominator

Average A/R

### INVENTORY (26)

18. (3) In periods of falling inventory wholesale prices, which inventory method should minimize cash outflow for taxes?

- a. LIFO  
b. FIFO  
c. Weighted Average

3

19. Circle the inventory method used by Costco in its national and international markets

a. (2) US operations LIFO FIFO

b. (2) Foreign Operations LIFO FIFO

4

20. (2) True or False (circle one) Assuming wholesale inventory unit costs are rising, when less inventory is bought than sold and LIFO is used, then net income will be higher than it otherwise would have been had purchases equaled sales.

2

21. (10PC) Use the following information to answer the lettered questions which follow:

|         |                       | <u>Units</u> | <u>Cost per unit</u> |         |    |
|---------|-----------------------|--------------|----------------------|---------|----|
| 1/1/09  | Beginning Inventory   | 100          | \$3                  | 100 @ 3 |    |
| 3/14/09 | Sales                 | 70           |                      |         | 70 |
| 4/12/09 | Sales                 | 20           |                      |         | 20 |
| 4/21/09 | Purchases (additions) | 50           | \$4                  | 50 @ 4  |    |
| 5/16/09 | Sales                 | 40           |                      |         | 40 |

- a. (4PC) If the firm assumes a LIFO flow and accounts for inventory periodically, what dollar amount of inventory was **sold** during the period?

$$\begin{array}{r}
 40 @ 4 \\
 10 @ 4 \\
 10 @ 3 \\
 + 70 @ 3 \\
 \hline
 = 440
 \end{array}$$

$$4 \quad \underline{440}$$

- b. (2PC) If the firm assumes a FIFO flow and perpetually accounts for inventory sales, what dollar amount of goods were **still on hand** at the end of the period?

$$\begin{array}{r}
 10 @ 3 \\
 10 @ 4
 \end{array}$$

$$0 \quad \underline{20}$$

- c. (4PC) If the nature of the inventory permitted use of the specific identification method and your goal was to maximize net income, what would you report as the cost of goods sold, assuming you determined cost of goods sold periodically?

$$\begin{array}{r}
 300 \\
 120 \\
 \hline
 420
 \end{array}
 \quad
 \begin{array}{r}
 70 + 20 + 40 = 130
 \end{array}$$

$$4 \quad \underline{420}$$

22. (4) Which statement best states the relationship between inventory flow assumptions used for financial reporting purposes versus that used for tax purposes?

- ☐ a. LIFO must be used for tax purposes if it is used for reporting purposes  
☒ b. If LIFO is used for tax purposes, it must also be used for reporting purposes  
☐ c. Any flow assumption can be used for reporting purposes but FIFO can not be used for tax purposes  
☒ d. If FIFO is used for reporting purposes, it must also be used for tax purposes



23. (3) Given the following values of ending inventory, at what value should ending inventory be shown on the balance sheet?

|                      | \$  |
|----------------------|-----|
| Historical cost      | 101 |
| Replacement cost     | 90  |
| Net realizable value | 118 |
| Normal profit margin | 20  |

$$(NIRV - DM) = 98$$

HC (101) →

101 ✓

0

### LONG-TERM ASSETS (23)

24. If the \$200,000 paving expenditures are amortized over a 10 year period with no salvage value envisioned, what will:

20,000 per year

- a. (3PC) The book value of the parking surface be after four full years of usage using straight-line depreciation?

$$20,000 \times 4 = 80,000$$

80,000

$$200,000 - 80,000 = 120,000$$

- b. (4PC) Depreciation expense for the parking surface be at the end of the second full year of usage using the double declining balance method?

|        | 1       | 2                                   |
|--------|---------|-------------------------------------|
| Histor | 200,000 | 200,000                             |
| A/D    | (0)     | (40,000)                            |
| Book   | 200,000 | 160,000                             |
| 20%    | 40,000  | <u>32,000</u> ← Real correct answer |
| Net    | 160,000 | 128,000                             |

$$10\% \times 2 = 20\%$$

32,000

4

- c. (4PC) Suppose after using the lot for 5 years (five financial statements have been prepared), it was determined that used asphalt has alternative uses so the estimated salvage value of the lot changed from zero to \$20,000. What amount of depreciation expense should be recorded in the sixth year, assuming straight-line depreciation was and continues to be used?

$$\frac{\$100,000 - 20,000}{5} = 16,000$$

16,000

4

- d. (2) Suppose a new asphalt coating was invented that, when applied, extends the asphalt's life for several years. If \$30,000 (a material amount) is invested in this new coating, should that amount be expensed or capitalized? (circle one)

2

25. (2) A developer bought some land for \$100,000; she intended to convert it to a parking lot. In addition to the purchase price, \$20,000 of clearing and leveling costs are incurred. With the land now ready, \$200,000 was spent on paving the area and \$200,000 on lighting and fencing the area. What amount should be charged to the land account?

2      120,000

26. (2) Your firm normally spends \$500,000 per year on research and development. Due to a severe drop in business, it is forced to cut this year's R&D efforts and thus costs by half. What effect, if any, will the curtailment of R&D have on this year's expenses?

Retard      No effect      will be cut in half

27. (4PC) Suppose a firm is considering the purchase of another firm. After all discovery has been completed, the deal breaks down to the following:

|                     | <u>Book Value</u> | <u>Market Value</u> |
|---------------------|-------------------|---------------------|
| Assets to be gained | 100,000           | 123,000             |
| Liabilities assumed | 30,000            | 30,000              |

What amount of goodwill should be recorded if the other firm is purchased for \$110,000?

$$\begin{array}{r} 123,000 \\ - 30,000 \\ \hline 93,000 \end{array}$$

$$\begin{array}{r} 110,000 \\ - 93,000 \\ \hline 17,000 \end{array}$$

4      \$ 17,000

28. (2) Suppose an existing patent may be purchased for \$100,000. Alternatively, a new patent, developed by your firm would cost \$100,000. In either case, the patent you eventually own is expected to provide exclusive benefit to you for 10 years, after which you believe another product will have been invented and patented. If the purchase or development could occur in one fiscal year, which method, development or purchase (circle one) will have the largest adverse impact on this year's income statement?

All development costs are expensed

**EXTRA CREDIT (8)**

29. In the article "Big Oil's Accounting Methods Fuel Criticism..."

- a. What inventory flow method were large oil companies reportedly using?

~~FIFO~~

- b. Briefly describe (one sentence) why, according to the article, the oil companies believed the method they were using was justified?

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- c. Briefly describe (one sentence) the argument put forth by critics of the policy being used by oil companies.

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