

Code of Conduct: By signing below you acknowledge that you are a member of a learning community at the Foster School of Business that is committed to the highest academic standards and that you adhered to these standards while completing this exam. Specific to this exam, by signing below you acknowledge that you did not receive or give help to others, nor did you witness others receiving or giving help to others, during the exam.

Date: 11/12/09

A215
Autumn 2009
Exam II

- 7
71
74

- You have one hour and twenty minutes to complete this exam.
- For problems that require calculations show your work.
- Provide your answers in the space provided (not on a separate answer sheet).
- Please check to see that you have 11 pages (they are numbered).

CONCEPTUAL QUESTIONS

*These questions help me assess whether you understand the concepts we have covered. [REDACTED] question from looking through the text, my slides, your quiz section instructor's materials, and the homework.

1. (3 pts) Internal control consists of five interrelated components. Name any three of the five components:

Risk Assessment

Controlling the environment

Controlling the activities

2. (2 pts) In what current asset account will you find a firm's short term investments that have a maturity date no longer than three months from the date of purchase?

Investment

3. (2 pts) Earnings quality is measured by comparing a company's net income to its

net assets

4. (2 pts) Firms refer to the small amount of cash that they keep on hand to pay for minor

purchases as petty cash

5. (2 pts) Does writing off a customer's accounts receivable balance change a firm's net accounts receivable? (circle one)

YES

NO

(X)

6. (2 pts) On ~~October 10~~, Bellatrix Corporation entered the following journal entry:

Bad debt expense.....400
 Accounts receivable.....400

Which one of the following is true? (check one)

- ☐ Bellatrix uses the allowance method to account for accounts receivable.
- ☒ Bellatrix uses the direct write-off method to account for accounts receivable.
- ☐ There is not enough information to determine which method Bellatrix uses to account for accounts receivable.

7. (2 pts) In fiscal 2008, Sirius Black Corporation wrote off Terry Boot's accounts receivable balance of \$140. Unexpectedly in fiscal 2009, Terry Boot magically appears and pays off his accounts receivable balance that was previously written off. Indicate how Sirius' cash flows will be affected in fiscal 2008 and fiscal 2009 as a result of these events.

Cash flows in fiscal 2008 will: (circle one)

- will increase
 will decrease
☒ will not change

Allowance
 A/R

Cash flows in fiscal 2009 will: (circle one)

- ☒ will increase
 will decrease
 will not change

A/R
 Allowance
 Cash
 A/R

8. (2 pts) Which account below is NOT a contra sales account? (circle one)

- Sales discounts
 Sales returns
☒ Trade discounts
 Sales allowances

9. (3 pts) Merchandising firms typically have one inventory account. In contrast, manufacturing firms typically classify inventory into three categories. What are the three categories?

Raw materials
Work in progress
Finished goods

10. (2 pts) The additional amount of inventory a firm would report if it used FIFO instead of LIFO is called the LIFO reserve.

11. (2 pts) Once a firm has determined both the cost and market value of inventory at the end of an accounting period it applies a rule to see if the inventory needs to be written down. What do we call this rule?

Lower of cost or market

12. (2 pts) Delacour Corporation uses a periodic inventory system. Delacour mistakenly overstates ending inventory at the end of period 1. Ending inventory is correctly stated at the end of period 2. Given this error, which of the following accounts will be understated at the end of period 2? (circle all accounts that will be understated)

Retained earnings
 Net income
 Inventory
 Cost of goods sold

13. (2 pts) We use the term capitalize to describe recording an expenditure as an asset rather than expensing it in the current period.

14. (3 pts) The systematic allocation of a **tangible** asset's cost to an expense over time is called depreciation. The systematic allocation of an **intangible** asset's cost to an expense over time is called amortization. The systematic allocation of a **natural resource** asset's cost to an expense over time is called depletion.

15. (2 pts) Does GAAP or MACRS allow firms greater flexibility in choosing a cost allocation method? (circle one)

GAAP allows more flexibility

MACRS allows more flexibility

16. (2 pts) At the beginning of fiscal 2009, Goyle Corporation sold a piece of equipment for \$56,000 cash. Goyle originally bought the equipment at the beginning of fiscal 2004 for \$100,000. At the time of purchase, Goyle estimated the equipment's service life to be 10 years and its residual value to be \$10,000. Which of the following is true? (circle one)

Goyle recorded a loss when it sold the equipment.

Goyle recorded a gain when it sold the equipment.

There is not enough information to determine if Goyle recorded a loss or a gain when it sold the equipment.

Need to know how the equipment was depreciated

Cash
Accum depreciation
loss or gain
Equipment

56,000
??

100,000

$$\frac{100,000 - 10,000}{10} = 9,000$$

SHORT PROBLEMS

*These questions help me assess whether can use the concepts we have covered to solve problems. I created each question from looking through the text, my slides, your quiz section instructor's materials, and the homework.

17. (4 pts: Homework E4-7) On July 31, 2010, Arkie Company's general ledger shows a checking account balance of \$22,870. The July cash receipts of \$1,785 included in the general ledger balance are placed in the night depository at the bank on July 31 and processed by the bank on August 1. The bank statement dated July 31 shows bank service charges of \$45. The bank statement reflects all checks written by the company on or before July 31, except for one check totaling \$1,360. The bank statement shows a balance of \$22,400 on July 31.

Prepare a bank reconciliation to calculate the correct ending balance of cash on July 31, 2010.

Bank's Cash Balance		Company's Cash Balance	
BB	\$ 22,400	BB	\$ 22,870
Deposits Outstanding	1,785	Service Charge	(45)
Outstanding Checks	(1,360)		
EB	<u>\$ 22,825</u>	EB	<u>\$ 22,825</u>

18. (3 pts) After completing its bank reconciliation and conducting a thorough investigation, Katie Bell Company cannot explain why its October 31 cash balance reported in the general ledger is \$45 less than the cash balance reported on its October 31 bank statement. What is the journal entry that Katie Bell will record to reconcile its cash balance with the bank's cash balance?

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
10/31	1	Cash over and short Cash	45	45

2

19. Borgan and Burkes Corporation reported the following information for fiscal 2006-2009:

	2006	2007	2008	2009
Net sales	\$120,000	\$100,000	\$90,000	\$80,000
Cost of goods sold	70,000	50,000	45,000	40,000
Depreciation expense	24,000	20,000	18,000	16,000
Other operating expenses	6,000	5,000	4,500	4,000
Tax expense	18,000	15,000	13,500	12,000
Net income	2,000	10,000	<u>9,000</u>	8,000
Accounts receivable	8,000	12,000	8,000	11,000
Inventory	12,000	14,000	16,000	15,000
Total assets	120,000	118,000	122,000	128,000
Total liabilities	50,000	60,000	60,000	68,000
Total owners' equity	70,000	58,000	62,000	60,000

Round all ratios to the nearest tenth.

a. (2 pts) What is Borgan & Burkes' average collection period for 2008?

$$\text{Receivables Turnover Ratio} = \frac{\text{net credit sales}}{\text{average accts rec}} = \frac{90,000}{10,600} = 9$$

$$\text{Average collection period} = \frac{365 \text{ days}}{\text{Receivables turnover ratio}} = \frac{365 \text{ days}}{9} = 40.6 \text{ days}$$

b. (2 pts) What is Borgan & Burkes' inventory turnover ratio for 2008?

$$\text{Inventory Turnover} = \frac{\text{COGS}}{\text{average inventory}} = \frac{45,000}{15,000} = 3$$

c. (2 pts) What is Borgan & Burkes' return on assets ratio for 2008?

$$\text{ROA} = \frac{\text{net income}}{\text{net sales}} \cdot \frac{\text{net sales}}{\text{average total assets}} = \frac{9,000}{90,000} \cdot \frac{90,000}{120,000} = 0.08$$

0.1

20. (3 pts) On October 2, Barty Crouch Company sells a bike to a customer for \$2,000. The customer pays with a credit card. The credit card company charges 2% of the sale price of an item as a processing fee. Provide the journal entry that Barty will record when it sells the bike on October 2.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
10/2		Cash	1960	
		Credit Card Processing Fee	40	
		Sales		2000

-0

21. (3 pts: Homework E5-3) On October 10, Sir Nicholas Corporation provides services on account to Fleur Company for \$10,000 with terms 3/10, n/30. Fleur pays cash for those services on October 18. Record the collection of cash for Sir Nicholas on October 18.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
10/18	1	Cash Sales Discount Accounts Receivable	9700 300	10,000

22. (3 pts) On March 1, Gideon Company provides consulting services to Diggory Corporation totaling \$140,000. In payment for the services, Diggory signs a note requiring payment of the principle and interest on October 1. The annual interest rate on the note is 12%. Record the collection of cash for Gideon on October 1. $140,000 \cdot 0.12 = \frac{16,800}{12} = 1400 \cdot 7 = 9,800$ interest

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
10/1	1	Cash Notes Receivable Interest Revenue	149,800	140,000 9,800

23. (3 pts) Below is a portion of Dumbledore Company's fiscal 2009 trial balance (before any adjusting entries have been recorded):

	Debits	Credits
Net sales		\$100,000
Cost of goods sold	70,000	
Operating expenses	24,000	
Accounts receivable	<u>28,000</u>	
Allowance for bad debt		400
Inventory	20,000	
Accounts payable		4,000
Long-term debt		58,000
Retained earnings		18,000

$28,000 \cdot 0.15 = 4,200$
 $\frac{400}{4200} = 0.095$
 Dumbledore estimates uncollectible accounts to be 15% of accounts receivable. Record the adjusting entry to record bad debt expense at the end of fiscal 2009.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
12/31/09	1	Bad Debt Expense Allowance for Bad Debt	3800	3800

24. During 2009, Hufflepuff Company had the following inventory transactions:

Date	Transaction	Units	Unit cost	Total cost
Jan 1	Beginning inventory	1,000	\$11	\$11,000
Feb 1	Sale	200		
Mar 1	Sale	600		
Jun 1	Purchase	400	\$10	\$4,000
Sep 1	Sale	500		
Nov 1	Purchase	100	\$15	\$1,500

The sale price of each unit sold in 2009 was \$20. ¹⁵⁰⁰

- a. (3 pts) If Hufflepuff uses LIFO and a perpetual inventory system, what is the dollar amount of cost of goods sold and ending inventory at the end of 2009?

$$\begin{array}{r}
 800 \cdot 11 = 8800 \\
 400 \cdot 10 = 4000 \\
 100 \cdot 11 = 1100 \\
 \hline
 13,900
 \end{array}$$

$$\begin{array}{r}
 11,000 \\
 4,000 \\
 1,500 \\
 \hline
 16,500
 \end{array}
 - 13,900 = 2,600$$

COGS = \$13,900

Ending Inventory = \$2,600

- b. (3 pts) If Hufflepuff uses average cost and a periodic inventory system, what is the dollar amount of cost of goods sold and ending inventory at the end of 2009?

$$\frac{16,500}{1500} = \$11$$

$$\text{Sale Total} = 1300 \cdot \$11 = \$14,300$$

$$16,500 - 14,300 = \$2,200$$

COGS = \$14,300

Ending Inventory = \$2,200



$$\frac{4000 - 700}{3} = 1100$$

25. On January 1, 2007, Luna Company purchases a moped for \$4,000. Luna estimates that at the end of its three-year service life the moped can be sold for \$700. During the three-year period Luna expects to drive the moped 3,000 miles.

- a. (3 pts) Provide the journal entry to record depreciation expense for **year 2** assuming Luna uses the straight-line method of depreciation.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
12/31/08	1	Depreciation Expense Accumulated Depreciation	1100	1100

- b. (3 pts) Provide the journal entry to record depreciation expense for **year 2** assuming Luna uses the 150% declining balance method of depreciation.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
12/31/08	1	Depreciation Expense Accumulated Depreciation	1000	1000

- c. (3 pts) Provide the journal entry to record depreciation expense for **year 2** assuming Luna uses the activity-based method of depreciation. Luna drove the moped 1,100 miles in year 1, 1,200 miles in year 2, and 1,000 miles in year 3.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
12/31/08	1	Depreciation Expense Accumulated Depreciation	1320	1320

$$\frac{4000 - 700}{3000} = 1.1$$

$$1.1 \cdot 1100 = 1210$$

$$4000 - 1210 = 2790$$

$$1200 \cdot 1.1 = 1320$$

$$2790 - 1320 = 1470$$

(3)

- d. (3 pts) Assume that Luna uses the straight-line method of depreciation and has determined at the end of year 2 (after recording depreciation expense) that the moped is impaired with a fair value of only \$1,000. Provide the journal entry to record the impairment loss at the end of year 2.

DATE	REF #	ACCOUNTS	DEBIT	CREDIT
12/31/08	1	Loss on Impairment Moped/Equipment	800	800

$$\frac{4000 - 200}{3} = 1100$$

$$4000 - 1100 - 1100 = 1800$$

Feedback (no points, but I appreciate your feedback & will share the results with you in our next class)

Was the exam fair (i.e., did it cover topics addressed in the text, my slides, your quiz section instructor's materials, and/or the homework problems)?

<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
1	2	3	4	5	6	7	8	9	10	11
No, the exam was not fair										Yes, the exam was fair

Was the exam difficult?

<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
1	2	3	4	5	6	7	8	9	10	11
No, it was quite easy										Yes, it was very difficult

Approximately how many hours did you spend studying for the exam? 20 hours

0