

## HW9 Solution

### E9-1 Identifying Current Liabilities, Computing Working Capital, and Explaining Working Capital

#### *Required:*

1. Identify current liabilities and compute working capital. Why is working capital important to management?
2. Would your computation be different if the company reported \$250,000 worth of contingent liabilities in the notes to its financial statements? Explain

#### Req. 1

(a) Current assets (\$530,000 - \$362,000)		\$168,000
Current liabilities:		
Accounts payable	\$56,000	
Income taxes payable	14,000	
Liability for withholding taxes	3,000	
Rent revenue collected in advance	7,000	
Wages payable	7,000	
Property taxes payable	3,000	
Note payable, 10% (due in 6 months)	12,000	
Interest payable	400	(102,400 )
Working capital (current assets – current liabilities)		<u><u>\$ 65,600</u></u>

Working capital is critical for the efficient operation of a business. The working capital accounts are actively managed to achieve a balance between a company's short-term obligations and the resources needed to satisfy those obligations. If a business has too little working capital, it runs the risk of not being able to meet its obligations. If it has too much working capital, it runs the risk of tying up resources in unproductive assets.

#### Req. 2

No. If the contingent liabilities are reported in the notes, then they would not affect working capital.

### E9-3 Computing Payroll Costs; Discussion of Labor Costs

**Required:**

1. What was the total labor cost to the company? What was the amount of the employees' take-home pay?
2. List the liabilities and their amounts reported on the company's January 31 balance sheet, assuming the employees have been paid but that no transfers have been made to government agencies.
3. A junior accountant at Oaks stated in a meeting that giving all employees a 5 percent raise would have cost Oaks \$4,300 ( $\$86,000 \times 0.05$ ) in the month of January. Do you agree?

Req. 1

The total labor cost to the company was  $\$86,000 + \$6,000 = \$92,000$ . The \$6,000 is the employer's portion of the FICA payroll tax. The employees' take-home pay was \$70,000; that is, the total of salaries and wages less the deductions paid by the employees (i.e.,  $\$86,000 - \$10,000 - \$6,000$ ).

Req. 2

Balance sheet liabilities:

Liability for employee income taxes withheld	\$ 10,000
FICA taxes payable ( $\$6,000 + \$6,000$ )	12,000
Total	<u>\$ 22,000</u>

Req. 3

The junior accountant is only seeing a piece of the total compensation puzzle. Since employers pay some taxes, like FICA taxes, as a percent of employees' salaries, the five percent raise will actually cost the company more than five percent of the salaries and wages earned.

## E9-8 Reporting Notes Payable and Calculating Interest Expense

### **Required:**

1. Prepare the journal entry North Face will record when it signs the note and receives the cash.
2. Prepare the journal entry that North Face will record when it pays off the note and any accrued interest after nine months.

#### Req. 1

At signing:

Cash (+A)	2,000,000	
Note payable (+L)		2,000,000

Signed a nine-month note with an interest rate of 8%.

#### Req. 2

At maturity:

Interest expense (+E, -SE)	120,000*	
Note payable (-L)	2,000,000	
Cash (-A)		2,120,000

Paid off note plus nine months of accrued interest.

$$*\$2,000,000 \times 0.08 \times 9/12 = \$120,000$$

## E9-17 Computing a Present Value Involving an Annuity and a Single Payment

Present value of option (a):

Single amount: $\$12,000 \times 0.67297$	\$ 8,075.64
Annuity: $\$500 \times 16.35143$	8,175.72
Present value	<u>\$16,251.36</u>

Present value of option (b): \$14,906

In present value terms, option (b) is the better option as it has the lowest present value.