

# CHAPTER 11

## Current Liabilities and Payroll Accounting

### ASSIGNMENT CLASSIFICATION TABLE

<u>Study Objectives</u>	<u>Questions</u>	<u>Brief Exercises</u>	<u>Exercises</u>	<u>A Problems</u>	<u>B Problems</u>
1. Explain a current liability, and identify the major types of current liabilities.	1	1	7	1A	1B
2. Describe the accounting for notes payable.	2	2	1, 2, 7	1A, 2A	1B, 2B
3. Explain the accounting for other current liabilities.	3, 4	3, 4	3, 4, 7	1A	1B
4. Explain the financial statement presentation and analysis of current liabilities.	5	5	7, 8, 9	1A	1B
5. Describe the accounting and disclosure requirements for contingent liabilities.	6, 7	6	5, 6, 7	1A	1B
6. Compute and record the payroll for a pay period.	8, 9, 10, 12 13, 14, 15	7, 8	10, 11, 12 13	3A, 4A, 5A	3B, 4B, 5B
7. Describe and record employer payroll taxes.	9, 10, 11, 15	9	12, 14	3A, 4A, 5A	3B, 4B, 5B
8. Discuss the objectives of internal control for payroll.	16, 17	10			
*9. Identify additional fringe benefits associated with employee compensation.	18, 19, 20, 21, 22	11	15, 16	4A	4B

**\*Note:** All **asterisked** Questions, Exercises, and Problems relate to material contained in the appendix to the chapter.

## ASSIGNMENT CHARACTERISTICS TABLE

<b>Problem Number</b>	<b>Description</b>	<b>Difficulty Level</b>	<b>Time Allotted (min.)</b>
1A	Prepare current liability entries, adjusting entries, and current liabilities section.	Moderate	30–40
2A	Journalize and post note transactions and show balance sheet presentation.	Moderate	30–40
3A	Prepare payroll register and payroll entries.	Simple	30–40
4A	Journalize payroll transactions and adjusting entries.	Moderate	30–40
5A	Prepare entries for payroll and payroll taxes; prepare W-2 data.	Moderate	30–40
1B	Prepare current liability entries, adjusting entries, and current liabilities section.	Moderate	30–40
2B	Journalize and post note transactions and show balance sheet presentation.	Moderate	30–40
3B	Prepare payroll register and payroll entries.	Simple	30–40
4B	Journalize payroll transactions and adjusting entries.	Moderate	30–40
5B	Prepare entries for payroll and payroll taxes; prepare W-2 data.	Moderate	30–40

# BLOOM'S TAXONOMY TABLE

Correlation Chart between Bloom's Taxonomy, Study Objectives and End-of-Chapter Exercises and Problems

Study Objective	Knowledge	Comprehension	Application	Analysis	Synthesis	Evaluation
1. Explain a current liability, and identify the major types of current liabilities.		Q11-1 BE11-1	E11-7	P11-1A P11-1B		
2. Describe the accounting for notes payable.		Q11-2	E11-7	BE11-2 E11-1 E11-2 P11-1A P11-2A P11-1B P11-2B		
3. Explain the accounting for other current liabilities.			BE11-4 Q11-3 Q11-4 E11-3 E11-7 E11-4	BE11-3 E11-7 E11-4 P11-1A P11-1B		
4. Explain the financial statement presentation and analysis of current liabilities.		Q11-5 BE11-5	E11-7 E11-8 E11-9	P11-1A P11-1B		
5. Describe the accounting and disclosure requirements for contingent liabilities.		Q11-6 Q11-7 E11-6	E11-5 E11-6 E11-7	BE11-6 E11-5 P11-1A P11-1B		
6. Compute and record the payroll for a pay period.	Q11-9 Q11-12 Q11-14	Q11-8 Q11-10 Q11-13	BE11-7 BE11-8 E11-10 E11-11 E11-12 E11-13	P11-3A P11-4A P11-5A P11-3B P11-4B P11-5B		
7. Describe and record employer payroll taxes.	Q11-11	Q11-9 Q11-10 Q11-15	BE11-9 E11-12 E11-14	P11-3A P11-4A P11-5A P11-3B P11-4B P11-5B		
8. Discuss the objectives of internal control for payroll.	Q11-17	Q11-16 BE11-10				
*9. Identify additional fringe benefits associated with employee compensation.	Q11-18	Q11-19 Q11-20 Q11-21	BE11-11 E11-16	E11-15 P11-4A P11-4B		
Broadening Your Perspective		Financial Reporting Communication Exploring the Web		Comparative Analysis		Decision Making Across the Organization Ethics Case All About You

# ANSWERS TO QUESTIONS

1. Jill is not correct. A current liability is a debt that can reasonably be expected to be paid: (a) from existing current assets or through the creation of other current liabilities and (2) within one year or the operating cycle, whichever is longer.
2. In the balance sheet, Notes Payable of \$40,000 and Interest Payable of \$900 ( $\$40,000 \times .09 \times 3/12$ ) should be reported as current liabilities. In the income statement, Interest Expense of \$900 should be reported under other expenses and losses.
3. (a) Disagree. The company only serves as a collection agent for the taxing authority. It does not report sales taxes as an expense; it merely forwards the amount paid by the customer to the government.  
 (b) The entry to record the proceeds is:
 

Cash .....	7,400	
Sales .....		7,000
Sales Taxes Payable .....		400
4. (a) The entry when the tickets are sold is:
 

Cash .....	800,000	
Unearned Football Ticket Revenue .....		800,000

  
 (b) The entry after each game is:
 

Unearned Football Ticket Revenue.....	160,000	
Football Ticket Revenue.....		160,000
5. Liquidity refers to the ability of a company to pay its maturing obligations and meet unexpected needs for cash. Two measures of liquidity are working capital (current assets – current liabilities) and the current ratio (current assets ÷ current liabilities).
6. A contingent liability is an existing situation involving uncertainty as to a possible obligation which will be resolved when one or more future events occur or fail to occur. Contingent liabilities are only recorded in the accounts if they are probable and the amount is reasonably estimable. Warranty costs are a contingent liability usually recorded in the accounts since they are both probable in incurrence and subject to estimation.
7. If an event is only reasonably possible, then only note disclosure is required. If the possibility of a contingent liability occurring is only remote, then neither recording in the accounts nor note disclosure is required.
8. Gross pay is the amount an employee actually earns. Net pay, the amount an employee is paid, is gross pay reduced by both mandatory and voluntary deductions, such as FICA taxes, union dues, federal income taxes, etc. Gross pay should be recorded as wages or salaries expense.
9. Both employees and employers are required to pay FICA taxes.
10. No. When an employer withholds federal or state income taxes from employee paychecks, the employer is merely acting as a collection agent for the taxing body. Since the employer holds employees' funds, these withholdings are a liability for the employer until they are remitted to the government.

## Questions Chapter 11 (Continued)

11. FICA stands for Federal Insurance Contribution Act; FUTA stands for Federal Unemployment Tax Act; and SUTA stands for State Unemployment Tax Act.
12. A W-2 statement contains the employee's name, address, social security number, wages, tips, other compensation, social security taxes withheld, wages subject to social security taxes, and federal, state and local income taxes withheld.
13. Payroll deductions can be classified as either mandatory (required by the government) or voluntary (not required by the government). Mandatory deductions include FICA taxes and income taxes. Examples of voluntary deductions are health and life insurance premiums, pension contributions, union dues, and charitable contributions.
14. The employee earnings record is used in: (1) determining when an employee has earned the maximum earnings subject to FICA taxes, (2) filing state and federal tax returns, and (3) providing each employee with a statement of gross earnings and tax withholdings for the year.
15. (a) The three types of taxes are: (1) FICA, (2) federal unemployment, and (3) state unemployment.  
(b) The tax liability accounts are classified as current liabilities in the balance sheet. Payroll tax expense is classified under operating expenses in the income statement.
16. The main internal control objectives associated with payrolls are: (1) to safeguard company assets from unauthorized payments of payrolls and (2) to assure the accuracy and reliability of the accounting records pertaining to payrolls.
17. The four functions associated with payroll are: (1) hiring employees, (2) timekeeping, (3) preparing the payroll, and (4) paying the payroll.
- \*18. Two additional types of fringe benefits are:
  - (1) Paid absences—vacation pay, sick pay, and paid holidays.
  - (2) Post-retirement benefits—pensions and health care and life insurance.
- \*19. Paid absences refer to compensation paid by employers to employees for vacations, sickness, and holidays. When the payment of such compensation is probable and the amount can be reasonably estimated, a liability should be accrued for paid future absences which employees have earned. When this amount cannot be reasonably estimated, the potential liability should be disclosed.
- \*20. Post-retirement benefits consist of payments by employers to retired employees for: (1) pensions and (2) health care and life insurance.
- \*21. A 401(K) works as follows: an employee can contribute up to a certain percentage of pay into a 401(K) plan and employers will match a percentage of the employee's contribution.
- \*22. A defined contribution plan defines the contribution that an employer can make but not the benefit that the employee will receive. In a defined benefit plan, the employer agrees to pay a defined amount to retirees based on employees meeting certain eligibility standards.

# SOLUTIONS TO BRIEF EXERCISES

## BRIEF EXERCISE 11-1

- (a) A note payable due in two years is a long-term liability, not a current liability.
- (b) \$30,000 of the mortgage payable is a current maturity of long-term debt. This amount should be reported as a current liability.
- (c) Interest payable is a current liability because it will be paid out of current assets in the near future.
- (d) Accounts payable is a current liability because it will be paid out of current assets in the near future.

## BRIEF EXERCISE 11-2

July 1	Cash .....	80,000	
	Notes Payable .....		80,000
Dec. 31	Interest Expense .....	4,000	
	Interest Payable .....		4,000
	(\$80,000 X 10% X 1/2)		

## BRIEF EXERCISE 11-3

### Sales tax payable

- (1) Sales = \$14,800 = (\$15,540 ÷ 1.05)
- (2) Sales taxes payable = \$740 = (\$14,800 X 5%)

Mar. 16	Cash .....	15,540	
	Sales .....		14,800
	Sales Taxes Payable .....		740

#### BRIEF EXERCISE 11-4

Cash .....	720,000	
Unearned Basketball Ticket Revenue .....		720,000
(To record sale of 4,000 season tickets)		
Unearned Basketball Ticket Revenue .....	60,000	
Basketball Ticket Revenue .....		60,000
(To record basketball ticket revenues earned)		

#### BRIEF EXERCISE 11-5

- (a) Working capital = \$4,090,475 – \$1,180,707 = \$2,909,768 (thousand)  
(b) Current ratio = \$4,090,475 ÷ \$1,180,707 = 3.46:1

#### BRIEF EXERCISE 11-6

Dec. 31	Warranty Expense .....	4,000	
	Estimated Warranty Liability .....		4,000
	[(1,000 X 5%) X \$80]		

#### BRIEF EXERCISE 11-7

Gross earnings:			
Regular pay (40 X \$16) .....	\$640.00		
Overtime pay (7 X \$24) .....	<u>168.00</u>		<u>\$808.00</u>
Gross earnings .....			\$808.00
Less: FICA taxes payable (\$808 X 8%) .....	\$ 64.64		
Federal income taxes payable .....	<u>95.00</u>		<u>159.64</u>
Net pay .....			<u>\$648.36</u>

### BRIEF EXERCISE 11-8

Jan. 15	Wages Expense .....	808.00	
	FICA Taxes Payable (\$808 X 8%) .....		64.64
	Federal Income Taxes Payable .....		95.00
	Wages Payable .....		648.36
Jan. 15	Wages Payable .....	648.36	
	Cash .....		648.36

### BRIEF EXERCISE 11-9

Jan. 31	Payroll Tax Expense .....	9,940	
	FICA Taxes Payable (\$70,000 X 8%) .....		5,600
	Federal Unemployment Taxes Payable (\$70,000 X .8%) .....		560
	State Unemployment Taxes Payable .....		3,780
	(\$70,000 X 5.4%)		

### BRIEF EXERCISE 11-10

- |                      |                           |
|----------------------|---------------------------|
| (a) Timekeeping      | (c) Preparing the payroll |
| (b) Hiring employees | (d) Paying the payroll    |

### \*BRIEF EXERCISE 11-11

Jan. 31	Vacation Benefits Expense (80 X \$120) .....	9,600	
	Vacation Benefits Payable .....		9,600



# SOLUTIONS TO EXERCISES

## EXERCISE 11-1

July 1, 2008			
Cash .....	50,000		
Notes Payable .....		50,000	
November 1, 2008			
Cash .....	60,000		
Notes Payable .....		60,000	
December 31, 2008			
Interest Expense .....	3,000		
(\$50,000 X 12% X 6/12)			
Interest Payable .....		3,000	
Interest Expense .....	1,000		
(\$60,000 X 10% X 2/12)			
Interest Payable .....		1,000	
February 1, 2009			
Notes Payable .....	60,000		
Interest Payable .....	1,000		
Interest Expense .....	500		
Cash .....		61,500	
April 1, 2009			
Notes Payable .....	50,000		
Interest Payable .....	3,000		
Interest Expense .....	1,500		
Cash .....		54,500	

**EXERCISE 11-2**

(a) June 1	Cash.....	90,000	
	Notes Payable.....		90,000
(b) June 30	Interest Expense.....	900	
	Interest Payable .....		900
	[( $\$90,000 \times 12\% \times 1/12$ )]		
(c) Dec. 1	Notes Payable.....	90,000	
	Interest Payable .....	5,400	
	( $\$90,000 \times 12\% \times 6/12$ )		
	Cash.....		95,400
(d)	\$5,400		

**EXERCISE 11-3**

WARKENTINNE COMPANY			
Apr. 10	Cash.....	31,500	
	Sales .....		30,000
	Sales Taxes Payable .....		1,500
RIVERA COMPANY			
15	Cash.....	23,540	
	Sales ( $\$23,540 \div 1.07$ ) .....		22,000
	Sales Taxes Payable .....		1,540
	( $\$23,540 - \$22,000$ )		

#### EXERCISE 11-4

(a)	Nov. 30	Cash.....	240,000	
		Unearned Subscriptions .....		240,000
		(12,000 X \$20)		
(b)	Dec. 31	Unearned Subscriptions .....	20,000	
		Subscription Revenue .....		20,000
		(\$240,000 X 1/12)		
(c)	Mar. 31	Unearned Subscriptions.....	60,000	
		Subscription Revenue.....		60,000
		(\$240,000 X 3/12)		

#### EXERCISE 11-5

(a) Estimated warranties outstanding:

<u>Month</u>	<u>Estimate</u>	<u>Units Defective</u>	<u>Outstanding</u>
November	900	600	300
December	<u>960</u>	<u>400</u>	<u>560</u>
Total	<u>1,860</u>	<u>1,000</u>	<u>860</u>

Estimated warranty liability—860 X \$20 = \$17,200.

(b)	Warranty Expense (1,860 X \$20) .....	37,200	
	Estimated Warranty Liability .....		37,200
	Estimated Warranty Liability .....	20,000	
	Repair Parts, Wages Payable, Cash, etc.....		20,000
(c)	Estimated Warranty Liability (500 X \$20) .....	10,000	
	Repair Parts, Wages Payable, Cash, etc.....		10,000

### EXERCISE 11-6

- (a) If a contingency is remote (unlikely to occur), it need not be recorded or disclosed.
- (b) Since the contingency is probable and reasonably estimable, the liability should be recorded in the accounts. In addition, the details should be disclosed in the notes to the financial statements. The journal entry is:

Lawsuit Loss .....	1,000,000	
Lawsuit Liability .....		1,000,000

- (c) If a contingency is reasonably possible, it need not be recorded, but must be disclosed in the notes to the financial statements.

### EXERCISE 11-7

- (a) **JEWETT ONLINE COMPANY**  
**Partial Balance Sheet**

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<b>Current liabilities</b>	
Accounts payable .....	\$ 63,000
Long-term debt due within one year .....	30,000
Unearned ticket revenue .....	24,000
Estimated warranty liability .....	18,000
Sales taxes payable .....	10,000
Interest payable .....	8,000
Total current liabilities .....	<u>\$153,000</u>

- (b) Jewett Online Company's working capital is \$147,000 and its current ratio is 1.96:1. Although a current ratio of 2:1 has been considered the standard for a good credit rating, many companies operate successfully with a current ratio below 2:1.

### EXERCISE 11-8

- (a) Working capital = \$6,466 – \$6,715 = (\$249) million
- (b) Current ratio = \$6,466 ÷ \$6,715 = .96:1

## EXERCISE 11-9

### (a) Current ratio

$$2004 \quad \$8,720 \div \$6,071 = 1.44:1$$

$$2005 \quad \$7,115 \div \$5,238 = 1.36:1$$

### Working capital

$$2004 \quad \$8,720 - \$6,071 = \$2,649 \text{ million}$$

$$2005 \quad \$7,115 - \$5,238 = \$1,877 \text{ million}$$

### (b) Current ratio

$$\$6,915 \div \$5,038 = 1.37:1$$

### Working capital

$$\$6,915 - \$5,038 = \$1,877 \text{ million}$$

It would make its current ratio increase slightly, but its working capital would remain the same.

## EXERCISE 11-10

(a) 1. Regular 40 X \$15.00 = \$600.00

Overtime 2 X \$22.50 = 45.00

Gross earnings \$645.00

2. FICA taxes—\$51.60 = (\$645 X 8%).

3. Federal income taxes \$55.

4. State income taxes \$12.90 = (\$645 X 2%).

5. Net pay \$500.50 = (\$645.00 – \$51.60 – \$55.00 – \$12.90 – \$25.00).

(b) Office Wages Expense .....	645.00	
FICA Taxes Payable .....		51.60
Federal Income Taxes Payable .....		55.00
State Income Taxes Payable .....		12.90
Health Insurance Payable .....		25.00
Wages Payable .....		500.50

## EXERCISE 11-11

- C. Ogle**       $\$4,000 \times 8\% = \$320$ . Ogle's total gross earnings for the year are  $\$87,500 = (\$83,500 + \$4,000)$ , which is below the  $\$90,000$  maximum for FICA taxes.
- D. Delgado**       $\$3,900 \times 8\% = \$312$ . Delgado's total gross earnings for the year are  $\$90,100$ . Thus,  $\$3,900$  of the gross earnings ( $\$4,000 - \$100$ ) for this pay period are subject to FICA taxes.
- L. Jeter**       $\$2,400 \times 8\% = \$192$ . Jeter's total gross earnings for the year are  $\$91,600$ . Thus, only  $\$2,400$  of the gross earnings ( $\$4,000 - \$1,600$ ) for this pay period are subject to FICA taxes.
- T. Spivey**       $\$0$ . Spivey's gross earnings prior to this pay equal the maximum amount subject to FICA taxes. Thus, none of the gross earnings in the December 31 pay period is subject to FICA taxes.

## EXERCISE 11-12

(a) See next page.

(b) Jan. 31	Wages Expense .....	1,837.00	
	FICA Taxes Payable.....		146.96
	Federal Income Taxes Payable.....		129.00
	Health Insurance Payable.....		60.00
	Wages Payable.....		1,501.04

# EXERCISE 11-12 (Continued)

(a)

## AIVAMAR COMPANY

### Payroll Register

For the Week Ending January 31

Employee	Total Hours	Earnings			Deductions				Net Pay
		Regular	Overtime	Gross Pay	FICA Taxes	Federal Income Taxes	Health Insurance	Total	
M. Hashmi	46	\$ 480.00	\$108.00	\$ 588.00	\$ 47.04	\$ 34.00	\$10.00	\$ 91.04	\$ 496.96
E. Benson	42	520.00	39.00	559.00	44.72	37.00	25.00	106.72	452.28
K. Kern	44	600.00	90.00	690.00	55.20	58.00	25.00	138.20	551.80
<b>Totals</b>		<b>\$1,600.00</b>	<b>\$237.00</b>	<b>\$1,837.00</b>	<b>\$146.96</b>	<b>\$129.00</b>	<b>\$60.00</b>	<b>\$335.96</b>	<b>\$1,501.04</b>

## EXERCISE 11-12 (Continued)

(b)	Jan. 31	Payroll Tax Expense.....	260.86	
		FICA Taxes Payable.....		146.96
		Federal Unemployment Taxes		
		Payable (\$1,837 X .8%).....		14.70
		State Unemployment Taxes		
		Payable (\$1,837 X 5.4%).....		99.20

## EXERCISE 11-13

- (a) (1) \$ 1,100 [\$10,000 see (2) below – \$8,900].  
(2) \$10,000 (FICA taxes \$800 ÷ 8%).  
(3) \$ 300 (\$10,000 X 3%).  
(4) \$ 2,340 (\$10,000 – \$7,660).  
(5) \$ 6,000 (\$10,000 – \$4,000).

(b)	Feb. 28	Warehouse Wages Expense.....	6,000	
		Store Wages Expense .....	4,000	
		FICA Taxes Payable .....		800
		Federal Income Taxes		
		Payable .....		1,140
		State Income Taxes Payable .....		300
		Union Dues Payable.....		100
		Wages Payable.....		7,660
	28	Wages Payable .....	7,660	
		Cash.....		7,660

## EXERCISE 11-14

(a)	FICA tax (\$760,000 X 8%).....	\$60,800
	SUTA tax (\$100,000 X 5.4%).....	5,400
	FUTA tax (\$100,000 X 0.8%).....	800
	Total payroll tax .....	<u>\$67,000</u>
(b)	Payroll Tax Expense.....	67,000
	FICA Taxes Payable.....	60,800
	State Unemployment Taxes Payable .....	5,400
	Federal Unemployment Taxes Payable .....	800



**\*EXERCISE 11-15**

Mar. 31	Vacation Benefits Expense .....	2,400	
	(10 X 2 X \$120)		
	Vacation Benefits Payable .....		2,400
31	Pension Expense (\$40,000 X 10%).....	4,000	
	Pension Liability.....		4,000

**\*EXERCISE 11-16**

1.	Vacation Benefits Expense .....	12,000	
	Vacation Benefits Payable.....		12,000
	(20 X 5 X \$120)		
2.	Pension Expense.....	100,000	
	Cash .....		70,000
	Pension Liability .....		30,000
3.	Vacation Benefits Payable .....	2,160	
	Cash .....		2,160
	(18 X 1 X \$120)		

# SOLUTIONS TO PROBLEMS

<b>PROBLEM 11-1A</b>
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(a)	Jan. 5	Cash.....	22,680		
		Sales ( $\$22,680 \div 108\%$ ).....		21,000	
		Sales Taxes Payable .....		1,680	
		( $\$22,680 - \$21,000$ )			
	12	Unearned Service Revenue.....	10,000		
		Service Revenue.....		10,000	
	14	Sales Taxes Payable .....	7,700		
		Cash.....		7,700	
	20	Accounts Receivable .....	43,200		
		Sales .....		40,000	
		Sales Taxes Payable .....		3,200	
		( $800 \times \$50 \times 8\%$ )			
	21	Cash.....	18,000		
		Notes Payable.....		18,000	
	25	Cash.....	12,420		
Sales ( $\$12,420 \div 108\%$ ).....			11,500		
Sales Taxes Payable .....			920		
( $\$12,420 - \$11,500$ )					
(b)	(1)	Jan. 31	Interest Expense.....	40	
		Interest Payable .....			40
		( $\$18,000 \times 8\% \times 1/12 =$ \$120; $\$120 \times 1/3$ )			
	(2)	Jan. 31	Warranty Expense.....	2,800	
			( $\$40,000 \times 7\%$ ) Estimated Warranty Liability .....		

## PROBLEM 11-1A (Continued)

### (c) Current liabilities

Notes payable .....	\$18,000
Accounts payable .....	52,000
Unearned service revenue (\$16,000 – \$10,000) .....	6,000
Sales taxes payable (\$1,680 + \$3,200 + \$920) .....	5,800
Estimated warranty liability .....	2,800
Interest payable .....	<u>40</u>
Total current liabilities .....	<u>\$84,640</u>

<b>PROBLEM 11-2A</b>
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(a)	Jan.	2	Merchandise Inventory or		
			Purchases.....	30,000	
			Accounts Payable.....		30,000
Feb.	1		Accounts Payable .....	30,000	
			Notes Payable .....		30,000
Mar.	31		Interest Expense .....	450	
			(\$30,000 X 9% X 2/12)		
			Interest Payable .....		450
Apr.	1		Notes Payable .....	30,000	
			Interest Payable .....	450	
			Cash .....		30,450
July	1		Equipment.....	51,000	
			Cash .....		11,000
			Notes Payable .....		40,000
Sept.	30		Interest Expense .....	1,000	
			(\$40,000 X 10% X 3/12)		
			Interest Payable .....		1,000
Oct.	1		Notes Payable .....	40,000	
			Interest Payable .....	1,000	
			Cash .....		41,000
Dec.	1		Cash .....	15,000	
			Notes Payable .....		15,000
Dec.	31		Interest Expense .....	100	
			(\$15,000 X 8% X 1/12)		
			Interest Payable .....		100

# **PROBLEM 11-2A (Continued)**

**(b)**

Notes Payable			
4/1	30,000	2/1	30,000
10/1	40,000	7/1	40,000
		12/1	15,000
		12/31 Bal.	15,000

Interest Payable			
4/1	450	3/31	450
10/1	1,000	9/30	1,000
		12/31	100
		12/31 Bal.	100

Interest Expense			
3/31	450		
9/30	1,000		
12/31	100		
12/31 Bal.	1,550		

**(c) Current liabilities**

Notes payable .....	\$15,000	
Interest payable .....	<u>100</u>	\$15,100

**(d) Total interest is \$1,550.**

# PROBLEM 11-3A

(a)

## DEL HARDWARE Payroll Register For the Week Ending March 15, 2008

Earnings				Deductions							Store	Office
Employee	Hours	Regular	Over- time	Gross Pay	FICA	Fed.	State	U.F.	Total	Net Pay	Wages Expense	Wages Expense
Joe Devena	40	600.00	0	600.00	48.00	72.00	18.00	5.00	143.00	457.00	600.00	
Mary Keener	42	600.00	45.00	645.00	51.60	47.00	19.35	5.00	122.95	522.05	645.00	
Andy Dye	44	520.00	78.00	598.00	47.84	60.00	17.94	8.00	133.78	464.22	598.00	
Kim Shen	46	520.00	117.00	637.00	50.96	61.00	19.11	5.00	136.07	500.93		637.00
Totals		2,240.00	240.00	2,480.00	198.40	240.00	74.40	23.00	535.80	1,944.20	1,843.00	637.00

**PROBLEM 11-3A (Continued)**

(b)	Mar. 15	Store Wages Expense .....	1,843.00	
		Office Wages Expense .....	637.00	
		FICA Taxes Payable .....		198.40
		Federal Income Taxes Payable .....		240.00
		State Income Taxes Payable .....		74.40
		United Fund Contributions Payable .....		23.00
		Wages Payable .....		1,944.20
15		Payroll Tax Expense .....	352.16	
		FICA Taxes Payable .....		198.40
		(\$2,480 X 8%)		
		Federal Unemployment Taxes Payable (\$2,480 X .8%).....		19.84
		State Unemployment Taxes Payable (\$2,480 X 5.4%) .....		133.92
(c)	Mar. 16	Wages Payable .....	1,944.20	
		Cash .....		1,944.20
(d)	Mar. 31	FICA Taxes Payable .....	396.80	
		(\$198.40 + \$198.40)		
		Federal Income Taxes Payable .....	240.00	
		Cash .....		636.80

<b>PROBLEM 11-4A</b>
----------------------

(a)	Jan. 10	Union Dues Payable .....	870.00	
		Cash.....		870.00
12		FICA Taxes Payable.....	760.00	
		Federal Income Taxes Payable.....	1,204.60	
		Cash.....		1,964.60
15		U.S. Savings Bonds Payable .....	360.00	
		Cash.....		360.00
17		State Income Taxes Payable .....	108.95	
		Cash.....		108.95
20		Federal Unemployment Taxes Payable.....	288.95	
		State Unemployment Taxes Payable.....	1,954.40	
		Cash.....		2,243.35
31		Office Salaries Expense .....	26,600.00	
		Store Wages Expense.....	28,400.00	
		FICA Taxes Payable.....		4,400.00
		Federal Income Taxes Payable.....		2,158.00
		State Income Taxes Payable.....		454.00
		United Fund Contributions Payable.....		1,888.00
		Union Dues Payable .....		400.00
		Wages Payable.....		45,700.00
31		Wages Payable.....	45,700.00	
		Cash.....		45,700.00



**PROBLEM 11-4A (Continued)**

(b)	1. Jan.	31	Payroll Tax Expense .....	7,810.00	
			FICA Taxes Payable .....		4,400.00
			(\$55,000 X 8%)		
			Federal Unemployment Taxes Payable (\$55,000 X .8%) .....		440.00
			State Unemployment Taxes Payable (\$55,000 X 5.4%) .....		2,970.00
*2.		31	Vacation Benefits Expense.....	3,300.00	
			(\$55,000 X 6%) Vacation Benefits Payable .....		3,300.00

<b>PROBLEM 11-5A</b>
----------------------

(a)	Administrative Salaries Expense.....	200,000	
	Electricians' Wages Expense.....	370,000	
	FICA Taxes Payable.....		38,800
	Federal Income Taxes Payable.....		174,400
	State Income Taxes Payable .....		17,100
	United Fund Contributions Payable.....		27,500
	Hospital Insurance Premiums Payable .....		17,200
	Wages Payable.....		295,000

(b)	Payroll Tax Expense.....	43,255	
	FICA Taxes Payable (\$485,000 X 8%) .....		38,800
	Federal Unemployment Taxes Payable .....		1,080
	(\$135,000 X .8%)		
	State Unemployment Taxes Payable .....		3,375
	(\$135,000 X 2.5%)		

(c)					
		Wages, Tips, Other Compensation	Federal Income Tax Withheld	State Income Tax Withheld	FICA Wages
	<u>Employee</u>				<u>FICA Tax Withheld</u>
	Jane Eckman	\$59,000	\$28,500	\$1,770 (1)	\$59,000
	Sharon Bishop	26,000	10,200	780 (2)	26,000

(1) \$59,000 X 3%.

(2) \$26,000 X 3%.

<b>PROBLEM 11-1B</b>
----------------------

(a)	Jan. 1	Cash .....	30,000	
		Notes Payable .....		30,000
	5	Cash .....	10,400	
		Sales ( $\$10,400 \div 104\%$ ).....		10,000
		Sales Taxes Payable .....		400
		( $\$10,400 - \$10,000$ )		
	12	Unearned Service Revenue .....	9,000	
		Service Revenue .....		9,000
	14	Sales Taxes Payable .....	5,800	
		Cash .....		5,800
	20	Accounts Receivable .....	48,672	
		Sales .....		46,800
		Sales Taxes Payable .....		1,872
		( $900 \times \$52 \times 4\%$ )		
	25	Cash .....	18,720	
		Sales ( $\$18,720 \div 104\%$ ).....		18,000
		Sales Taxes Payable .....		720
		( $\$18,720 - \$18,000$ )		
(b) (1)	Jan. 31	Interest Expense .....	200	
		Interest Payable .....		200
		( $\$30,000 \times 8\% \times 1/12$ )		
(2)	Jan. 31	Warranty Expense .....	2,340	
		( $\$46,800 \times 5\%$ )		
		Estimated Warranty Liability .....		2,340

**PROBLEM 11-1B (Continued)**

<b>(c) Current liabilities</b>	
Notes payable.....	<b>\$30,000</b>
Accounts payable .....	<b>42,500</b>
Unearned service revenue (\$15,000 – \$9,000) .....	<b>6,000</b>
Sales taxes payable (\$400 + \$1,872 + \$720) .....	<b>2,992</b>
Estimated warranty liability .....	<b>2,340</b>
Interest payable .....	<b>200</b>
Total current liabilities.....	<b><u>\$84,032</u></b>

<b>PROBLEM 11-2B</b>
----------------------

(a)	Jan.	2	Merchandise Inventory or		
			Purchases .....	18,000	
			Accounts Payable .....		18,000
	Feb.	1	Accounts Payable .....	18,000	
			Notes Payable .....		18,000
	Mar.	31	Interest Expense.....	300	
			(\$18,000 X 10% X 2/12)		
			Interest Payable .....		300
	Apr.	1	Notes Payable .....	18,000	
			Interest Payable .....	300	
			Cash.....		18,300
	July	1	Equipment .....	35,000	
			Cash.....		11,000
			Notes Payable .....		24,000
	Sept.	30	Interest Expense.....	600	
			(\$24,000 X 10% X 3/12)		
			Interest Payable .....		600
	Oct.	1	Notes Payable .....	24,000	
			Interest Payable .....	600	
			Cash.....		24,600
	Dec.	1	Cash.....	10,000	
			Notes Payable .....		10,000
	Dec.	31	Interest Expense.....	100	
			(\$10,000 X 12% X 1/12)		
			Interest Payable .....		100

**PROBLEM 11-2B (Continued)**

**(b)**

Notes Payable			
4/1	18,000	2/1	18,000
10/1	24,000	7/1	24,000
		12/1	10,000
		12/31 Bal.	10,000

Interest Payable			
4/1	300	3/31	300
10/1	600	9/30	600
		12/31	100
		12/31 Bal.	100

Interest Expense			
3/31	300		
9/30	600		
12/31	100		
12/31 Bal.	1,000		

<b>(c) Current liabilities</b>			
Notes payable.....		\$10,000	
Interest payable .....		<u>100</u>	\$10,100

**(d) Total interest is \$1,000.**

# PROBLEM 11-3B

(a)

## HILLER DRUG STORE

### Payroll Register

For the Week Ended February 15, 2008

Earnings				Deductions							Store	Office
Employee	Hours	Regular	Over-time	Gross Pay	FICA	Fed.	State	U.F.	Total	Net Pay	Wages Expense	Wages Expense
L. Steck	39	585.00	0	585.00	46.80	54.00	17.55	0	118.35	466.65	585.00	
S. Jabar	42	520.00	39.00	559.00	44.72	33.00	16.77	5.00	99.49	459.51	559.00	
M. Cape	44	480.00	72.00	552.00	44.16	61.00	16.56	7.50	129.22	422.78	552.00	
L. Wild	46	480.00	108.00	588.00	47.04	46.00	17.64	5.00	115.68	472.32		588.00
Totals		2,065.00	219.00	2,284.00	182.72	194.00	68.52	17.50	462.74	1,821.26	1,696.00	588.00

**PROBLEM 11-3B (Continued)**

(b)	Feb. 15	Store Wages Expense.....	1,696.00	
		Office Wages Expense .....	588.00	
		FICA Taxes Payable.....		182.72
		Federal Income Taxes Payable.....		194.00
		State Income Taxes Payable .....		68.52
		United Fund Payable .....		17.50
		Wages Payable.....		1,821.26
15		Payroll Tax Expense.....	324.33	
		FICA Taxes Payable.....		182.72
		(\$2,284 X 8%)		
		Federal Unemployment Taxes Payable (\$2,284 X .8%).....		18.27
		State Unemployment Taxes Payable (\$2,284 X 5.4%).....		123.34
(c)	Feb. 16	Wages Payable.....	1,821.26	
		Cash.....		1,821.26
(d)	Feb. 28	FICA Taxes Payable.....	365.44	
		(\$182.72 + \$182.72)		
		Federal Income Taxes Payable.....	194.00	
		Cash.....		559.44



<b>PROBLEM 11-4B</b>
----------------------

(a)	Jan. 10	Union Dues Payable.....	250.00	
		Cash .....		250.00
12		FICA Taxes Payable .....	662.20	
		Federal Income Taxes Payable .....	1,254.60	
		Cash .....		1,916.80
15		U.S. Savings Bonds Payable.....	350.00	
		Cash .....		350.00
17		State Income Taxes Payable .....	102.15	
		Cash .....		102.15
20		Federal Unemployment Taxes		
		Payable .....	312.00	
		State Unemployment Taxes		
		Payable .....	1,954.40	
		Cash .....		2,266.40
31		Office Salaries Expense.....	22,600.00	
		Store Wages Expense .....	27,400.00	
		FICA Taxes Payable .....		4,000.00
		Federal Income Taxes		
		Payable .....		1,970.00
		State Income Taxes		
		Payable .....		430.00
		Union Dues Payable.....		400.00
		United Fund Contributions		
		Payable .....		1,800.00
31		Wages Payable .....	41,400.00	
		Cash .....		41,400.00

**PROBLEM 11-4B (Continued)**

(b)	1.	Jan. 31	Payroll Tax Expense.....	7,100.00	
			FICA Taxes Payable .....		4,000.00
			(\$50,000 X 8%)		
			Federal Unemployment Taxes		
			Payable (\$50,000 X .8%) .....		400.00
			State Unemployment Taxes		
			Payable (\$50,000 X 5.4%) .....		2,700.00
*2.	31		Vacation Benefits Expense .....	2,500.00	
			(\$50,000 X 5%)		
			Vacation Benefits Payable .....		2,500.00

<b>PROBLEM 11-5B</b>
----------------------

(a)	Administrative Salaries Expense .....	200,000	
	Electricians' Wages Expense .....	320,000	
	FICA Taxes Payable .....		36,000
	Federal Income Taxes Payable .....		159,000
	State Income Taxes Payable .....		15,600
	United Fund Contributions Payable .....		25,000
	Hospital Insurance Premiums Payable .....		15,800
	Wages Payable .....		268,600

(b)	Payroll Tax Expense .....	39,960	
	FICA Taxes Payable (\$450,000 X 8%) .....		36,000
	Federal Unemployment Taxes Payable .....		960
	(\$120,000 X .8%)		
	State Unemployment Taxes Payable .....		3,000
	(\$120,000 X 2.5%)		

(c)					
		Wages, Tips, Other	Federal Income Tax	State Income Tax	
	<u>Employee</u>	<u>Compensation</u>	<u>Withheld</u>	<u>Withheld</u>	<u>FICA Wages</u>
	R. Lopez	\$60,000	\$27,500	\$1,800 (1)	\$60,000
	K. Vopat	27,000	11,000	810 (2)	27,000

(1) \$60,000 X 3%.

(2) \$27,000 X 3%.

- (a) Total current liabilities at December 31, 2005, \$9,406 million. PepsiCo's total current liabilities increased by \$2,654 (\$9,406 – \$6,752) million over the prior year.
- (b) In Note 2 under the subheading "Commitments and Contingencies," PepsiCo states: "We recognize liabilities for contingencies and commitments when a loss is probable and estimable."
- (c) The components of current liabilities are:

Short-term obligations .....	\$2,889,000,000
Accounts payable and other current liabilities .....	5,971,000,000
Income taxes payable .....	<u>546,000,000</u>
Total current liabilities.....	<u>\$9,406,000,000</u>

- (a) PepsiCo's largest current liability was "accounts payable and other liabilities" at \$5,971 million. Its total current liabilities were \$9,406 million. Coca-Cola's largest current liability was "loans and notes payable" at \$4,518 million. Its total current liabilities were \$9,836 million.

(b)	(in millions)	PepsiCo	Coca-Cola
(1)	Working capital	$\$10,454 - \$9,406 = \$1,048$	$\$10,250 - \$9,836 = \$414$
(2)	Current ratio	$\frac{\$10,454}{\$9,406} = 1.11:1$	$\frac{\$10,250}{\$9,836} = 1.04:1$

- (c) Based on this information, it appears that both companies are only narrowly liquid. The working capital levels are both low, as are the current ratios.

- (a) A worker who performs services for you is your employee if you can control what will be done and how it will be done. This is so even when you give the employee freedom of action. What matters is that you have the right to control the details of how the services are performed. Get Pub. 15-A, Employer's Supplemental Tax Guide, for more information on how to determine whether an individual providing services is an independent contractor or an employee.**

**Generally, people in business for themselves are not employees. For example, doctors, lawyers, veterinarians, construction contractors, and others in an independent trade in which they offer their services to the public are usually not employees. However, if the business is incorporated, corporate officers who work in the business are employees.**

- (b) Payments for the services of a child under the age of 18 who works for his or her parent in a trade or business (sole proprietorship or a partnership in which each partner is a parent of the child) are not subject to social security and Medicare taxes. If these services are for work other than in a trade or business, such as domestic work in the parent's private home, they are not subject to social security and Medicare taxes until the child reaches 21.**
- (c) Any employee without a social security card can get one by completing Form SS-5, Application for a Social Security Card.**
- (d) Tips your employee receives are generally subject to withholding. Your employee must report cash tips to you by the 10th of the month after the month the tips are received. The report should include tips you paid over to the employee for charge customers and tips the employee received directly from customers. No report is required for months when tips are less than \$20. Your employee reports the tips on Form 4070, Employee's Report of Tips to Employer, or on a similar statement.**

### **BYP 11-3 (Continued)**

- (e) In general, you must deposit income tax withheld and both the employer and employee social security and Medicare taxes (minus any advance EIC payments). You must deposit by using the Electronic Federal Tax Payment System (EFTPS) or by mailing or delivering a check, money order, or cash to an authorized financial institution or Federal Reserve bank using Form 8109 Federal Tax Deposit Coupon. However, some taxpayers are required to deposit by electronic funds transfer.**

**(a) METCALFE SERVICES INC.**

<u>Months</u>	<u>Number of Employees</u>	<u>Days Worked</u>	<u>Daily Rate</u>	<u>Cost</u>
January–March	2	60 (20 X 3)	\$75	\$ 9,000
April–May	3	50 (25 X 2)	75	11,250
June–October	2	90 (18 X 5)	75	13,500
November–December	3	46 (23 X 2)	75	10,350
<b>Total Cost</b>				<u><b>\$44,100</b></u>

**PERMANENT EMPLOYEES**

Salaries (\$21,000 X 2).....		\$42,000
Additional payroll costs		
FICA taxes (8% X \$42,000).....	\$3,360	
Federal unemployment taxes.....	112	
(.8% X \$14,000)		
State unemployment taxes .....	756	
(5.4% X \$14,000)		
Medical and dental insurance .....	960	5,188
(2 X \$40 X 12)		<u><b>\$47,188</b></u>

Kensington Processing Company would save \$3,088 (\$47,188 – \$44,100), as shown, by discharging the two employees and accepting the Metcalfe Services Inc. plan.

**(b) Donna should consider the following additional factors:**

- (1) The effect on the morale of the continuing employees if two employees are terminated.**
- (2) The anticipated efficiency of Metcalfe Services Inc. workers compared to the efficiency of the two employees who would be terminated.**
- (3) The effect on management control and supervision of using Metcalfe Services Inc. personnel.**
- (4) The time that may be required to indoctrinate the different Metcalfe Services Inc. personnel into the Kensington Processing Company's procedures.**



**Dear Mr. Quaney:**

**In response to your request, I wish to explain the types of taxes that are involved in determining the payroll and in recording and paying employer payroll taxes.**

**The taxes that are involved in determining the payroll are as follows:**

- 1. FICA taxes. These taxes were enacted by Congress to provide workers with supplemental retirement, employment disability, and medical benefits. These benefits are financed by a tax levied on employees' earnings. The tax rate and tax base are set by Congress and both change intermittently. Our text uses a rate of 8% on the first \$90,000 of gross earnings. FICA taxes are withheld by the employer and then remitted to the government. These taxes are not an expense to the employer.**
- 2. Federal income taxes. Employers are required to withhold federal income taxes from employees each pay period. The amount depends on the employee's gross earnings, the number of allowances claimed by the employee, and the length of the pay period. The amounts withheld are remitted by the employer to the government. These taxes are not an expense to the employer.**
- 3. State and city income taxes. Where applicable, these income taxes are similar to federal income taxes.**

**There are three types of payroll taxes that are levied on employers that are recognized as payroll tax expense by the employer.**

- 1. FICA taxes. The employer must match each employee's FICA contribution. The employer's tax is subject to the same rate and maximum earnings applicable to the employee.**

## **BYP 11-5 (Continued)**

- 2. Federal unemployment taxes. These taxes provide benefits to employees who lose their jobs through no fault of their own. The tax is 6.2% on the first \$7,000 of gross earnings paid to each employee during a calendar year. The employer is allowed a maximum credit of 5.4% on the federal rate for contributions to state unemployment taxes.**
- 3. State unemployment taxes. These taxes also provide benefits to employees who lose their jobs. The basic rate is usually 5.4% on the first \$7,000 of wages paid to an employee during the year.**

**Very truly yours,**

- (a) The stakeholders in this situation are:**
- ▶ **Daniel Longan, owner and manager.**
  - ▶ **Sixteen part-time employees of Daniel's.**
  - ▶ **Gina Watt, public accountant.**
- (b) Not withholding federal and state taxes from employees' payroll is both illegal and unethical. Also, not paying FICA taxes, and state and federal unemployment taxes, is illegal and unethical.**
- (c) Gina Watt, as Daniel's public accountant, should not be an accomplice to improper payroll deductions and accounting. Gina should constantly remind Daniel of the consequences of his illegal payroll payments and the unrecorded payments. She should advise Daniel that not only is the government deprived of its proper tax revenues, but employees are deprived of social security and possibly Medicare credits as well as workmen's compensation insurance.**
- (d) An important internal control principle is to make no payments from cash receipts. All cash receipts should be deposited daily intact in the bank and all disbursements should be made by properly authorized and signed checks.**

The answer to these questions depends on the state in which the student resides. It also will be depend on the year chosen, although we expect that the results will be much the same whether they pick any rates between 2005 and 2008. We provide a solution for this problem using the state of Wisconsin as an example. It should be pointed out that certain taxes can be deducted for computing federal income tax but are ignored in our computation.

- (a) Wisconsin state income taxes for a single person with a taxable income of \$60,000 is \$3,710.80. The tax rate between \$17,680 and \$132,580 is \$950.30 plus 6.5 percent over \$17,680. Therefore the computation is as follows:

$$\begin{array}{rcl}
 (\$60,000 - \$17,680) \times 6.5\% & = & \$2,750 \\
 \text{Base rate} & & \underline{950} \\
 \text{Total state income tax} & & \underline{\underline{\$3,710}}
 \end{array}$$

- (b) The property tax on a \$200,000 home at 2.1% is \$4,200.
- (c) The state gasoline tax in Wisconsin is 32.9 cents per gallon and the federal gasoline tax is 18.4 cents per gallon. Your total taxes on gasoline are computed as follows:
- $$400 \text{ gallons} \times (\$0.329 + \$0.184) = \underline{\underline{\$205}}$$
- (d) In Wisconsin the state sales tax rate is 5% and excludes food and prescription drug purchases. Therefore the sales tax is \$200 (\$4,000 X 5%).
- (e) The social security rate is 7.65% on income of \$60,000 or \$4,590.
- (f) Federal income taxes for a single person with a taxable income of \$60,000 is \$11,538. The tax rate between \$30,650 and \$74,200 is \$4,220 plus 25% over \$30,650. Therefore the computation is as follows:

$$\begin{array}{rcl}
 (\$60,000 - \$30,650) \times 25\% & = & \$ 7,338 \\
 \text{Base rate} & & \underline{4,220} \\
 \text{Total tax} & & \underline{\underline{\$11,538}}
 \end{array}$$

## **BYP 11-7 (Continued)**

**The total taxes paid therefore are computed as follows, based on a \$60,000 income amount:**

<b>State income tax .....</b>	<b>\$ 3,710</b>
<b>Property tax on home.....</b>	<b>4,200</b>
<b>Gasoline tax.....</b>	<b>205</b>
<b>Sales tax .....</b>	<b>200</b>
<b>Social security tax.....</b>	<b>4,590</b>
<b>Federal income tax.....</b>	<b><u>11,538</u></b>
<b>Total tax .....</b>	<b><u>\$24,443</u></b>

**The percentage of total taxes to income is therefore 41% (\$24,443/\$60,000), given the information above.**

