Income statement own Final Account

E-16

Close Income Summary account; record partnership liquidation

Tina, Liz, and Ann are partners. Certain data for their firm follow:

	Tina	*Liz*	*Ann*	*Total*
Capital balances prior to entering effects of 1987 operations	$220,500	$61,500	$145,500	$427,500
Loss for year ended December 31, 1987				45,000
Income and loss ratio	20%	50%	30%	100%

The partners decide to liquidate. There are no liabilities. All of the assets are noncash assets and are sold for $225,000 cash.

a. Prepare the journal entry to close the Income Summary account.

b. Prepare journal entries for the sale of the assets and the distribution of cash to partners. Each partner had invested all of her personal assets in the firm prior to liquidation and will not be able to pay any deficiency in her capital account.

PROBLEMS, SERIES A

P14-1-A

Record formation of partnership from two single proprietorships

Jeff Poole and Brad Lawson decided to form a partnership by combining their business assets and liabilities from their single proprietorships. Income and losses will be shared in a 2:3 ratio to Poole and Lawson, respectively. Balance sheets on November 23, 1987, the date the partnership was formed, are shown below:

JEFF POOLE
Balance Sheet
November 23, 1987

Assets

Cash	$ 16,000
Accounts receivable (net)	46,000
Inventory	68,000
Total assets	$130,000

Liabilities and Owner's Equity

Accounts payable	$ 44,000
Notes payable	36,000
Jeff Poole, capital	50,000
Total liabilities and owner's equity	$130,000

BRAD LAWSON
Balance Sheet
November 23, 1987

Assets

Cash	$ 4,000
Accounts receivable (net)	48,000
Inventory	94,000
Equipment (net)	30,000
Total assets	$176,000

Liabilities and Owner's Equity

Accounts payable	$ 96,000
Brad Lawson, capital	80,000
Total liabilities and owner's equity	$176,000

Current market values for Poole's assets were accounts receivable, $46,000; and inventory, $80,000. For Lawson, market values were accounts receivable, $39,000; inventory, $50,000; and equipment, $36,000.

Required: Prepare journal entries to record the capital contributions by Poole and Lawson in forming their partnership.

P14-2-A

Determine and journalize division of income under alternative provisions

An analysis of Ladd's capital account for the year 1987 showed a beginning balance of $67,500, a capital withdrawal on June 1 of $22,500, and an additional investment on November 1 of $11,250. A similar analysis of partner Breeman's capital account showed a beginning balance of $11,250 and an additional investment on July 1 of $45,000. The balance in the Income Summary account showed net income for the year of $49,500.

Required: Prepare a schedule and the required journal entry to record the distribution of the net income to the partners under each of the following independent assumptions:

a. Ladd and Breeman are allowed annual salaries of $18,000 and $22,500, respectively; 8% interest on average capital balance is to be credited to each partner, and the balance of income and losses is to be shared equally.

b. Equal annual salaries of $22,500 and interest of 6% on beginning capital balance are allowed each partner; the remaining balance is shared in a 2:1 ratio to Ladd and Breeman.

P14-3-A

Determine division of income; prepare statement of partners' capital; journalize income distribution; close drawing accounts

The balances in the capital accounts of K and M at June 30, 1987, were $480,000 and $240,000, respectively. These balances were unchanged during the year. K drew $64,000 during the year, and M drew $72,000. Net income for the year was $320,000.

Required:

a. Compute the income to be distributed to each partner at the end of the year under each of the following independent conditions:

1. Salaries allowed are $48,000 to K and $80,000 to M; remaining income is to be divided in the ratio of the beginning-of-the-year capital account balances.
2. Salaries allowed are $152,000 to K and $128,000 to M; interest at 10% is allowed on capital account balances at the beginning of the year; there were no other provisions relating to the sharing of income and losses in the partnership agreement.

b. Assuming that income is shared as in *(a)*(1) above, prepare a statement of partners' capital for the year.

c. Using the data in *(b)*, prepare entries to distribute the income and to close the drawing accounts.

P14-4-A

Prepare schedule showing division of income under alternative provisions

Chip and Mark formed a partnership on March 1, 1987, by investing $90,000 and $144,000, respectively. On July 1, Chip invested additional capital of $36,000, and Mark invested $54,000. At that time, the partners agreed that, in dividing net income, interest of 10% would be allowed on average capital account balances for the period. On September 1, Chip invested another $174,000, and Mark invested another $132,000. The partnership agreement also allowed monthly drawings of $5,400 for Chip and $7,200 for Mark. Both partners withdrew the allowed amounts. Nothing further was said about the sharing of income and losses. Net income for the year ended February 28, 1988 was $240,000.

Required: Prepare a schedule showing the distribution of income for the year ended February 28, 1988, assuming that:

a. The allowed monthly drawings were salaries and are used in determining the distribution of income.
b. The allowed monthly drawings were normal drawings (not salaries) and are not to be used in determining the distribution of income.

P14-5-A

Prepare schedule showing division of income for several years

Burt and Kent, as partners, have agreed to the following distribution of net income:

1. Salaries of $24,000 to Burt and $18,000 to Kent.
2. A bonus to Burt of 25% of net income in excess of salaries.
3. The remainder divided equally.

Net income for 1986 and 1987 was $90,000 and $30,000, respectively, and in 1988 there was a net loss of $15,000.

Required: Prepare schedules showing the distribution of the income and losses to the partners for each of the years 1986, 1987, and 1988.

P14-6-A

Prepare adjusting and closing entries, income statement, statement of partners' capital, and balance sheet

The following trial balance was taken for the Black and Gold partnership on December 31, 1987:

BLACK AND GOLD
Trial Balance
December 31, 1987

	Debits	*Credits*
Cash	$ 30,800	
Accounts Receivable	45,000	
Allowance for Doubtful Accounts		$ 750
Inventory	27,750	
Equipment	52,500	
Accumulated Depreciation—Equipment		12,750
Prepaid Insurance	682	
Accounts Payable		38,250
Black, Capital		27,750
Gold, Capital		54,750
Black, Drawing	700	
Gold, Drawing	9,000	
Sales		412,500
Purchases	330,000	
Selling Expenses	30,000	
Administrative Expenses	24,750	
Other Revenue		4,432
	$551,182	$551,182

The articles of copartnership for Black and Gold provide for the distribution of income and losses in the following manner:

1. Each partner is allowed 6% interest per year on his capital investment as of the beginning of the year.
2. Black is allowed a salary of $22,500 and Gold a salary of $27,000 per year as a distribution of income.
3. The remaining income and losses are to be divided equally.

Your analysis of the books and records discloses the following data that require consideration: the ending inventory is $23,250; 1% of sales is to be added to the allowance for doubtful accounts; and depreciation on the equipment should be recorded at 10% of cost. Black's capital account includes a credit for $3,000 invested on July 15 of the current year. Prepaid insurance at December 31, 1987, should be $60.

Required: You are to prepare the following for the partnership:

a. Adjusting and closing journal entries.
b. An income statement for the year.
c. A statement of partners' capital for the year.
d. A balance sheet for December 31, 1987.

P14-7-A

Record admission of new partner

Jim and Ray are partners who share income and losses in a 3:2 ratio. They decided to admit Kelly as a new partner at a time when their capital account balances were $480,000 for Jim and $240,000 for Ray.

Required: Prepare journal entries to record Kelly's admission to the partnership in each of the following unrelated situations:

a. Kelly acquired one half of Jim's interest for $250,000 cash paid to Jim personally.
b. Kelly acquired one fifth of Jim's equity for $100,000 cash and one fourth of Ray's equity for $62,000 cash. Both amounts were paid to the partners personally.
c. Kelly invested $180,000 for a 20% interest in capital.
d. Kelly invested $120,000 and was granted a 15% interest in capital because the old partnership was badly in need of cash to pay maturing debts.
e. Kelly invested $420,000 for a one-third interest in capital; her admission was recorded using the bonus method.

P14-8-A

Record admission of new partner

C and L are partners who have capital account balances of $60,000 and $30,000, respectively, and who share income and losses in a 3:2 ratio. They negotiated the admission of T to their partnership.

Required: Prepare journal entries to record T's admission to the partnership under each of the following unrelated situations:

a. T invested $54,000 cash and received a one-third interest in the capital of the new firm. The bonus method is used to record T's admission.
b. T invested $40,500 for a one-third interest in capital. T was granted a bonus upon joining the firm.
c. T invested sufficient cash to secure exactly a 40% interest in the new firm.

P14-9-A

Record withdrawal of partner

On July 31, 1987, Joe Howe, a member of the company of Howe and Orr, decided to retire. The partners have shared income and losses equally. On this date, their capital balances were Joe Howe, $160,000; Beth Howe, $200,000; and Mike Orr, $120,000.

Required: Prepare entries to record the withdrawal of Joe Howe under each of the following unrelated assumptions. All payments are made in cash, and the assets are not to be revalued.

a. Joe Howe was paid $160,000.
b. Joe Howe was paid $168,000.
c. Joe Howe was paid $148,000.

P14-10-A

Record withdrawal of partner

T, U, and V are partners who share income and losses in a 4:2:2 ratio. On December 31, 1987, T decided to retire. At that time, the partners' capital account balances were:

T, capital	$60,000
U, capital	52,500
V, capital	90,000

Required: Prepare entries to record the retirement of T in each of the following unrelated situations:

a. The partners agreed that inventory was undervalued by $27,000 and that the books should be adjusted to reflect market values. After the books were adjusted, T received cash equal to the balance in his capital account.
b. The partners agreed that inventory was undervalued on the books by $27,000, but the books should *not* be adjusted to reflect market values. T was paid cash equal to the balance that would have been shown in his capital account if the increase to market value had been recorded.
c. The partners agreed that the amount shown for inventory was $18,000 more than its current market value, but the inventory was *not* to be adjusted to reflect market values. T was paid cash equal to the balance that would have been in his capital account if the books had been adjusted.

ARTHUR SWAIN
Balance Sheet
September 4, 1987

Assets

Cash	$ 28,000
Accounts receivable (net)	34,000
Inventory	40,000
Total assets	$102,000

Liabilities and Owner's Equity

Accounts payable	$ 44,000
Arthur Swain, capital	58,000
Total liabilities and owner's equity	$102,000

An appraisal of the assets showed market values for the assets of Fisher as follows: accounts receivable, $28,000; inventory, $24,000; and equipment, $30,000. A similar appraisal placed the following market values upon Swain's assets: accounts receivable, $34,000; and inventory, $26,000.

Required: Prepare journal entries to record the capital contributions of Fisher and Swain to their newly formed partnership.

P14-2-B

Determine and journalize division of income under alternative provisions; close drawing accounts

An analysis of the capital accounts for 1987 of Clark and Dixon, partners, showed:

Clark

Jan. 1	Balance	$135,000
June 1	Capital withdrawal	22,500
Nov. 1	Additional investment	33,750

Dixon

Jan. 1	Balance	$ 22,500
July 1	Additional investment	45,000

The balance in the Income Summary account showed net income of $67,500 for 1987.

Required: Prepare a schedule showing the distribution of the net income under each of the following unrelated assumptions with regard to income distribution. Also prepare the entries to distribute the income and to close the drawing accounts. (Note: In each instance assume drawings were equal to salaries allowed for each partner.)

a. Clark and Dixon are allowed annual salaries of $18,000 and $22,500, respectively; 8% interest is allowed on average capital balances; and the balance of the income is shared equally.

b. Equal annual salaries of $27,000 are allowed to each partner; interest of 10% is allowed on capital balances at the beginning of the year; and the balance is shared in a 3:2 ratio between Clark and Dixon.

P14-3-B

Determine division of income; prepare entries to distribute income and close drawing accounts; prepare schedule of changes in partners' capital accounts

The S and C partnership has the following agreement for the sharing of income and losses: (1) S is to be allowed interest of 10% on her capital account balance as of the beginning of the year; (2) C is to be allowed a salary of $3,600 per month; and (3) any remaining balance of income or loss is to be shared equally. The net income for 1987 was $108,000.

Required: *a.* Assuming that S's and C's capital account balances on January 1, 1987, were $360,000 and $90,000, respectively, prepare a schedule showing the distribution of net income and the entry required to record it.

P14–11–A

Record partnership liquidation

The ABC partnership was liquidated on January 2, 1987. Before any of the company's $780,000 of assets (all noncash) were sold, the liabilities and capital account credit balances were:

Accounts Payable	$400,000
A, Capital	40,000
B, Capital	160,000
C, Capital	180,000

The assets were sold for $540,000. Income and losses are shared equally.

Required: Prepare the journal entries to record the sale of the assets (credit an Assets account) and the distribution of the cash to creditors and partners. Assume that none of the partners has other assets to cover a debit balance in his capital account.

P14–12–A

Record partnership liquidation

The partners of the MNO Company decided to liquidate because of their creditors' demands for payment of amounts owed. The March 31, 1987, balance sheet data for the partnership follows:

Cash	$ 45,000	Accounts payable	$247,500
Accounts receivable	97,500	Moore, capital	112,500
Merchandise inventory	135,000	Neal, capital	135,000
Plant and equipment	397,500	Oscar, capital	180,000
	$675,000		$675,000

The noncash assets were sold on April 1, 1987, for ~~[illegible]~~ 5,90,000 The partners share income and losses in a 50:25:25 ratio, respectively.

Required: Prepare journal entries to record the sale of the assets and the distribution of cash to creditors and partners. ~~Assume that partners developing debit balances in their capital accounts are not able to pay them from other assets.~~

PROBLEMS, SERIES B

P14–1–B

Record formation of partnership from two single proprietorships

Karen Fisher and Arthur Swain, who have been in business as single proprietors, decided to combine all of their business assets and liabilities in a new partnership in which they will share income and losses equally. Balance sheets of the two individuals on the date of the formation of the partnership are shown below:

KAREN FISHER
Balance Sheet
September 4, 1987

Assets

Cash	$ 8,000
Accounts receivable (net)	30,000
Inventory	18,000
Equipment (net)	40,000
Total assets	$96,000

Liabilities and Owner's Equity

Accounts payable	$46,000
Karen Fisher, capital	50,000
Total liabilities and owner's equity	$96,000

b. Prepare the entry needed to close the drawing accounts of the partners, which had the following balances (before closing) on December 31, 1987; S, zero; and C, $43,200.
c. Present a schedule showing the changes occurring in 1987 in the capital account of each partner.

P14-4-B

Prepare schedules showing division of income under alternative provisions

The capital account balances (unchanged during the year) on December 31, 1987, for T and G, partners, are $360,000 for T and $180,000 for G. T withdrew $36,000, and G withdrew $90,000 during the year, with all withdrawals charged to the respective drawing accounts. The net loss for the year was $36,000.

Required: Prepare schedules showing the distribution of income to each partner for the year 1987 under each of the following provisions:

a. Salaries are allowed of $27,000 to T and $67,500 to G; remaining income is divided according to capital account balances at the beginning of the year.
b. Salaries are allowed of $18,000 to T and $30,000 to G; interest of 10% is allowed on capital account balances at the beginning of the year; no further provisions relating to income sharing are included in the partnership agreement.

P14-5-B

Prepare schedules showing division of income at various amounts of income and loss

David and Scott are partners in a retail hardware store. Their partnership agreement calls for salaries to David and Scott of $24,000 and $48,000, respectively, and interest of 10% on average capital for the year. Any remaining balance is to be shared equally.

During 1987, each partner drew his allowed salary; there were no withdrawals in excess of allowed salaries. The capital accounts of the two partners remained unchanged during the year at $120,000 for David and $180,000 for Scott.

Required: Present schedules showing the distribution of net income assuming that the income statement for 1987 showed:

a. $144,000 of net income.
b. $60,000 of net income.
c. A net loss of $24,000.

P14-6-B

Prepare adjusting and closing entries, income statement, statement of partners' capital, and balance sheet

Bass and Carr are partners operating a retail store having a fiscal year ending on June 30. Their partnership agreement calls for annual salaries of $18,000 to Bass and $24,000 to Carr, interest of 8% on average capital account balances throughout the year, and the equal sharing of the balance of the income. Their June 30, 1987, trial balance follows:

BASS AND CARR
Trial Balance
June 30, 1987

	Debits	*Credits*
Cash	$ 60,600	
Accounts Receivable	96,000	
Inventory, July 1, 1986	43,200	
Accounts Payable		$ 61,200
Notes Payable		30,000
Bass, Capital		42,000
Carr, Capital		30,000
Bass, Drawing	12,000	
Carr, Drawing	15,000	
Sales		642,000
Purchases	408,000	
Purchase Returns		6,000
Employee Salaries and Wages	18,000	
Rent Expense	78,000	
Delivery Expense	25,200	
Store Expense	55,200	
	$811,200	$811,200

Question Final Account

QUESTIONS

1. What account titles are likely to appear in the ledger of a merchandising company that do not appear in the ledger of a service enterprise?
2. What entry is made to record a sale of merchandise on account?
3. Describe trade discounts and chain discounts.
4. Sales discounts and sales returns and allowances are deducted from sales on the income statement to arrive at net sales. Why not deduct these directly from the Sales account by debiting sales each time a sales discount, return, or allowance occurs?
5. What are the two basic procedures for accounting for inventory? How do these two procedures differ?
6. What useful purpose does the Purchases account serve?
7. What do the letters FOB stand for? When terms are *FOB destination,* who incurs the cost of freight?
8. What type of an expense is delivery expense? Where is it reported in the income statement?
9. Periodic inventory is said to afford little control over inventory. Explain why.
10. How does the accountant arrive at the total dollar amount of the inventory after taking a physical inventory?
11. How is cost of goods sold determined under periodic inventory procedure?
12. If the cost of goods available for sale and the cost of the ending inventory are known, what other amount appearing on the income statement can be calculated?
13. What are the major sections in a classified income statement for a merchandising company, and in what order do they appear?
14. What is gross margin? Why might management be interested in the percentage of gross margin to net sales?

EXERCISES

E–1

Apply rules of debit and credit for merchandise-related accounts

In the following table, indicate how each account shown is increased and decreased (debit or credit), and indicate the normal balance (debit or credit).

Title of Account	***Increased by (debit or credit)***	***Decreased by (debit or credit)***	***Normal balance (debit or credit)***
Merchandise Inventory			
Sales			
Sales Returns and Allowances			
Sales Discounts			
Accounts Receivable			
Purchases			
Purchase Returns and Allowances			
Purchase Discounts			
Accounts Payable			
Transportation-In			

E–2

Prepare entries for merchandise purchase/sale, return, and allowance on both buyer's and seller's books

a. The Duncan Company purchased $15,000 of merchandise from the Short Company on account. Before paying its account, the Duncan Company returned damaged merchandise with an invoice price of $3,200. Assuming use of periodic inventory procedure, prepare entries on both companies' books to record both the purchase/sale and the return.

b. Show how any of the required entries would change assuming that the Short Company granted an allowance of $1,200 on the damaged goods instead of giving permission to return the merchandise.

E-3

Determine end of discount period and prepare entry to record payment

What is the last payment date on which the cash discount can be taken on goods sold on March 5 for $32,000; terms 3/10/EOM, n/60? Assume that the bill is paid on this date, and prepare the correct entry on both the buyer's and seller's books to record the payment.

E-4

Calculate effect of trade and cash discounts on payment

You have purchased merchandise with a list price of $8,000. Because you are a wholesaler, you are granted trade discounts of 30%, 20%, and 10%. The cash discount terms are 2/EOM, n/60. How much will you remit if you pay the invoice by the end of the month of purchase? How much will you remit if you do not pay the invoice until the following month?

E-5

Determine cost of goods sold

The A Company uses periodic inventory procedure. Determine the cost of goods sold for the company assuming purchases during the period were $12,000, transportation-in was $90, purchase returns and allowances were $300, beginning inventory was $7,500, purchase discounts were $600, and ending inventory was $3,900.

E-6

Prepare entries for purchase, transportation-in, purchase discounts, and payment

The Franco Company purchased goods for $9,200 on June 14 under the following terms: 3/10, n/30; FOB shipping point, freight collect. The bill for the freight amounted to $300.

a. Assume that the invoice was paid within the discount period, and prepare all entries required on Franco Company's books.
b. Assume that the invoice was paid on July 11. Prepare the entry to record the payment made on that date.

E-7

Prepare partial work sheet using merchandise-related accounts

Given the balances shown in the partial trial balance, indicate how the balances would be treated in the work sheet. The ending inventory is $32. (The amounts are unusually small for ease in rewriting the numbers.)

Account Title	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Balance Sheet	
	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit
Merchandise Inventory	40									
Sales		280								
Sales Discounts	6									
Sales Returns and Allowances	16									
Purchases	200									
Purchase Discounts		4								
Purchase Returns and Allowances		8								
Transportation-In	12									

E-8

Prepare and post closing entries using T-accounts

Using the data in Exercise E-7:

a. Prepare closing entries for the accounts shown above. Do not close the Income Summary account.
b. Show in T-account format how the accounts would appear after this portion of the closing process has been completed.

E-9

Supply missing terms in formulas showing income statement relationships

In each of the following equations supply the missing term(s):

a. Net sales = Gross sales − (____________ ____________ + Sales returns and allowances).
b. Cost of goods sold = Beginning inventory + Net cost of purchases − ____________ ____________.
c. Gross margin = ____________ ____________ − Cost of goods sold.
d. Net income from operations = ____________ ____________ − Operating expenses.
e. Net income = Net income from operations + ____________ ____________ − ____________ ____________.

E-10

Supply missing amounts in the income statement

In each case below use the information provided to calculate the missing information:

	Case 1	*Case 2*	*Case 3*
Gross sales	200,000	?	?
Sales discounts	?	8,000	6,000
Sales returns and allowances	6,000	14,000	10,000
Net sales	190,000	378,000	?
Merchandise inventory, January 1	80,000	?	120,000
Purchases	120,000	240,000	?
Purchase discounts	2,400	4,200	4,000
Purchase returns and allowances	7,600	9,800	10,000
Net purchases	110,000	?	210,000
Transportation-in	8,000	12,000	10,000
Net cost of purchases	118,000	238,000	?
Cost of goods available for sale	?	338,000	340,000
Merchandise inventory, December 31	?	120,000	140,000
Cost of goods sold	100,000	?	200,000
Gross margin	?	160,000	100,000

PROBLEMS, SERIES A

P5-1-A

Journalize merchandise transactions for two different companies

a. The following transactions were entered into by the Kemp Carpet Company in August 1987:

Transactions:

Aug. 2 Sold merchandise on account for $30,000; terms 2/10, n/30, FOB destination.
18 Received payment for the sale of August 2.
20 A total of $1,000 of the merchandise sold on August 2 was returned, and a full refund was made because it was the wrong merchandise.
28 An allowance of $1,600 was granted on the sale of August 2 because some merchandise was found to be damaged. $1,600 cash was returned to the customer.

b. The Evans Furniture Company engaged in the following transactions in August 1987:

Transactions:

Aug. 4 Purchased merchandise on account at a cost of $14,000; terms 2/10, n/30, FOB shipping point.
6 Paid freight of $200 on the purchase of August 4.
10 Sold goods for $10,000; terms 2/10, n/30.
12 Returned $2,400 of the merchandise purchased on August 4.
14 Paid the amount due on the purchase of August 4.

Required: Prepare journal entries for the transactions.

P5-2-A

Journalize merchandise transactions on both buyer's and seller's books

The Abbott Auto Parts Company purchased merchandise with a list price of $40,000, FOB destination, freight prepaid, from Cooper Company, on August 15, 1987. Trade discounts of 20% and 10% were allowed, and credit terms were 2/10, n/30. Cooper Company paid the freight charges of $500 on August 16. On August 17, Abbott Company requested a purchase allowance of $940 because some of the merchandise had been damaged in transit. On August 20, the Cooper Company granted the allowance. Payment was made on the last day of the discount period.

Required: Record all the entries required on the books of both the buyer and the seller.

P5-3-A

Journalize merchandise transactions on both buyer's and seller's books

On August 1, 1987, the Kelley Hardware Store bought merchandise from the Pittman Company, $18,000 list price, FOB destination. The seller prepaid the freight of $120 on August 1, 1987. Terms included trade discounts of 30% and 10% and a cash discount of 2/10/EOM, n/60. On August 8, 1987, the Kelley Hardware Store returned $1,500 (at list price) of the merchandise. The balance due was paid on September 10, 1987.

Required: Journalize all entries required on the books of both the buyer and the seller.

P5-4-A

Prepare and post journal entries, and prepare trial balance and classified income statement

The Maddox Company engaged in the following transactions in the month of June 1987:

Transactions:

June 1 The owner, Paul Maddox, invested $40,000 cash and $15,000 of inventory in the business.
3 Merchandise was purchased on account, $20,000; terms 2/10, n/30, FOB shipping point.
4 Paid freight on the June 3d purchase, $550.
7 Merchandise was purchased on account, $10,000; terms 2/10, n/30, FOB destination.
10 Sold merchandise on account, $24,000; terms 2/10, n/30, FOB shipping point.
11 Returned $3,000 of the merchandise purchased on June 3.
12 Paid the amount due on the purchase of June 3.
13 Sold merchandise on account, $25,000; terms 2/10, n/30, FOB destination.
14 Paid freight on sale of June 13, $1,500.
20 Paid the amount due on the purchase of June 7.
21 $5,000 of the goods sold on June 13 were returned for credit.
22 Received the amount due on sale of June 13.
25 Received the amount due on sale of June 10.
29 Paid rent for the administration building for June, $2,000.
30 Paid sales salaries of $6,000 for June.
30 Purchased merchandise on account, $5,000; terms 2/10, n/30, FOB shipping point.

Additional data:

The inventory on hand on June 30 was $30,000.

Required:

a. Prepare journal entries for the transactions.
b. Post the journal entries to the proper ledger accounts.
c. Prepare a trial balance as of June 30, 1987.
d. Prepare a classified income statement.

P5-5-A

Prepare work sheet, classified income statement and balance sheet, and closing entries

The following data are for the Oakes Lamp Company:

OAKES LAMP COMPANY
Trial Balance
December 31, 1987

	Debits	*Credits*
Cash	$ 57,200	
Accounts Receivable	48,300	
Prepaid Insurance	2,900	
Merchandise Inventory, 1/1/87	41,600	
Land	60,000	
Store Building	110,000	
Accumulated Depreciation—Store Building		$ 33,000
Store fixtures	55,600	
Accumulated Depreciation—Store Fixtures		11,120
Accounts Payable		37,900
Oakes, Capital		220,180
Sales		551,500
Sales Discounts	3,700	
Sales Returns and Allowances	2,000	
Purchases	312,900	
Purchase Discounts		2,600
Purchase Returns and Allowances		1,400
Transportation-In	7,300	
Sales Salaries Expense	64,000	
Advertising Expense	12,000	
Delivery Expense	4,600	
Office Salaries Expense	74,000	
Interest Revenue		400
Interest Expense	2,000	
	$858,100	$858,100

Additional data:

1. Depreciation expense on the store building is $2,200.
2. Depreciation expense on the store fixtures is $5,560.
3. Accrued sales salaries are $1,400.
4. Insurance expired in 1987 is $2,500. Insurance is an administrative expense.
5. Cost of merchandise inventory on hand December 31, 1987, is $55,500.

Required: Prepare:

a. A work sheet for the year ended December 31, 1987.
b. A classified income statement. The only administrative expenses are office salaries and insurance.
c. A classified balance sheet.
d. The required closing entries.

P5-6-A

Prepare and post journal entries; prepare work sheet, classified income statement, classified balance sheet, and closing entries

The Connors Cabinet Company was organized May 1, 1987, and engaged in the following transactions:

Transactions:

May 1 Ron Connors invested $300,000 in his new business.
1 Purchased merchandise on account from the Robertson Company, $15,600; terms n/60, FOB shipping point.
3 Sold merchandise for cash, $9,600.
6 Paid transportation charges on May 1 purchase, $480 cash.
7 Returned $1,200 of merchandise to the Robertson Company due to improper size.

May 10 Requested and received an allowance of $600 from the Robertson Company for improper quality of certain items.
14 Sold merchandise on account to Lewis Company, $6,000; terms 2/20, n/30.
16 Issued cash refund for return of merchandise relating to sale made on May 3, $60.
18 Purchased merchandise on account from White Company invoiced at $9,600; terms 2/15, n/30, FOB shipping point.
18 Received a bill for freight charges of $300 from the Ace Trucking Company on the purchase from White Company.
19 Lewis Company returned $120 of merchandise purchased on May 14.
24 Returned $960 of defective merchandise to White Company. Received full credit.
28 Lewis Company remitted balance due on sale of May 14.
31 Paid White Company for the purchase of May 18 after adjusting for transaction of May 24.
31 Paid miscellaneous selling expenses of $2,400.
31 Paid miscellaneous administrative expenses of $3,600.

Additional data:

The May 31 inventory is $19,200.

Required: From the information for the Connors Cabinet Company:

a. Journalize the transactions. Round all amounts to the nearest dollar.
b. Post the entries to the proper ledger accounts.
c. Prepare a work sheet as of May 31. There were no adjusting entries.
d. Prepare a classified income statement for May.
e. Prepare and post the required closing entries.

PROBLEMS, SERIES B

P5-1-B

Journalize merchandise transactions for two different companies

a. The Norris Sporting Goods Company engaged in the following transactions in April 1987:

Transactions:

Apr. 1 Sold merchandise on account for $32,000; terms 2/10, n/30, FOB destination.
5 $4,800 of the goods sold on account on April 1 were returned for full credit. Payment for these goods had not yet been received.
8 A sales allowance of $640 was granted on the merchandise sold on April 1 because the merchandise was damaged in shipment.
10 Payment was received for the net amount due from the sale of April 1.

b. Classic Stereo Company engaged in the following transactions in July 1987:

Transactions:

July 2 Purchased stereo merchandise on account at a cost of $4,800; terms 2/10, n/30, FOB destination.
15 Sold $3,200 of the merchandise purchased on July 2 for $7,200; terms 2/10, n/30, FOB destination.
16 Paid freight costs on the merchandise sold, $240.
20 Classic Stereo Company was granted an allowance of $320 on the purchase of July 2 because of damaged merchandise.
31 Paid the amount due on the purchase of July 2.

Required: Prepare journal entries to record the transactions. Round all amounts to the nearest dollar.

P5-2-B

Journalize merchandise transactions on both buyer's and seller's books

On July 2, 1987, the Calvary Musical Instrument Company purchased merchandise with a list price of $8,000 from the Reynolds Company. The terms were 3/EOM, n/60, FOB shipping point, freight collect. Trade discounts of 15%, 10%, and 5% were granted by the Reynolds Company. The Calvary Musical Instrument Company paid the freight bill of $184 on July 5. On July 6, an employee discovered that merchandise with a list price of $640 had been seriously damaged in transit; these items were returned for full credit. Calvary Musical Instrument Company made payment on the last day of the discount period.

Required: Prepare all the necessary entries for the Calvary Musical Instrument Company.

P5-3-B

Journalize merchandise transactions on both buyer's and seller's books

The Saxon Ski Shop purchased merchandise on March 1, 1987, from the Locke Company at a list price of $12,000, FOB shipping point. Trade discounts of 30%, 25%, and 5% were granted. Cash discount terms were 2/EOM, n/60. The buyer paid the freight of $248 on March 4, 1987. The buyer notified the seller that a $1,200 credit should be granted against the amount due because of damaged merchandise. The seller granted the allowance on March 25, 1987.

Required: Assuming payment on March 31, record all entries on the books of both the buyer and seller.

P5-4-B

Prepare and post journal entries, and prepare trial balance and classified income statement

The data for the month of June 1987 given below are for the Tate Company:

Transactions:

June 1 The Tate Company was organized, and the owner, Sam Tate, invested $105,000 cash, $35,000 of merchandise, and a $30,000 plot of land.
4 Merchandise was purchased for cash, $45,000; FOB shipping point.
9 Cash of $1,050 was paid to a trucking company for delivery of the merchandise purchased June 4.
13 The company sold merchandise on account, $30,000; terms 2/10, n/30.
15 The company sold merchandise on account, $24,000; terms 2/10, n/30.
16 Of the merchandise sold May 13, $3,300 was returned for credit.
20 Salaries for services received were paid as follows: to office employees, $3,300; to salespersons, $8,700.
22 The company collected the amount due on $26,700 of the accounts receivable arising from the sale of June 13.
24 The company purchased merchandise on account at a cost of $36,000; terms 2/10, n/30, FOB shipping point.
26 $6,000 of the merchandise purchased June 24 was returned to the vendor for credit.
27 A trucking company was paid $750 for delivery to the Tate Company of the goods purchased June 24.
29 The company sold merchandise on account, $40,000; terms 2/10, n/30.
30 Sold merchandise for cash, $18,000.
30 Payment was received for the sale of June 15.
30 Paid store rent for June, $4,500.
30 Paid the amount due on the purchase of June 24.

Additional data:

The inventory on hand at the close of business June 30 was $70,000 at cost.

Required:

a. Prepare journal entries for the transactions.
b. Post the journal entries to the proper ledger accounts.
c. Prepare a trial balance as of June 30, 1987.
d. Prepare a classified income statement for the month ended June 30, 1987.

P5-5-B

Prepare work sheet, classified income statement and balance sheet, and closing entries

The following data are for the Wilson Lumber Company:

WILSON LUMBER COMPANY
Trial Balance
December 31, 1987

	Debits	*Credits*
Cash	$ 21,192	
Accounts Receivable	47,856	
Merchandise Inventory	85,560	
Sales Supplies on Hand	1,608	
Prepaid Fire Insurance	1,440	
Prepaid Rent	17,280	
Store Equipment	26,400	
Accumulated Depreciation—Store Equipment		$ 5,280
Accounts Payable		30,840
Wilson, Capital		125,892
Sales		336,708
Sales Returns and Allowances	1,548	
Purchases	150,252	
Purchase Returns and Allowances		1,212
Transportation-In	2,352	
Sales Salaries Expense	41,520	
Advertising Expense	23,400	
General Office Expense	2,964	
Office Salaries Expense	24,240	
Officers' Salaries Expense	48,000	
Legal and Auditing Expense	3,000	
Telephone and Telegraph Expense	1,440	
Interest Revenue		300
Interest Expense	180	
	$500,232	$500,232

Additional data as of December 31, 1987:

1. Prepaid fire insurance expired, $1,020.
2. Sales supplies consumed, $1,098.
3. Prepaid rent expired during the year, $15,180.
4. Depreciation expense on store equipment, $2,640.
5. Accrued sales salaries, $1,200.
6. Accrued office salaries, $900.
7. Merchandise inventory on hand, $105,000.

Required: Prepare:

a. A work sheet for the year ended December 31, 1987.
b. A classified income statement. The only selling expenses are sales salaries, advertising, sales supplies, and depreciation—store equipment.
c. A classified balance sheet.
d. The December 31, 1987, closing entries.

P5-6-B

Prepare and post journal entries; prepare work sheet, classified income statement, classified balance sheet, and closing entries

The Hall Western Wear Company is a wholesaler of western wear clothing. The company sells its merchandise to retailers. The company entered into the following transactions in May 1987:

Transactions:

May 1 The Hall Western Wear Company was organized as a single proprietorship. Mark Hall invested the following assets in the business: $154,000 cash, $56,000 merchandise, and $35,000 land.
1 Paid rent on administrative offices for May, $8,400.
5 The company purchased merchandise from Andco Company on account, $63,000; terms 2/10, n/30. Freight terms were FOB shipping point.

May 8 Cash of $2,800 was paid to a trucking company for delivery of the merchandise purchased May 5.
14 The company sold merchandise on account, $105,000; terms 2/10, n/30.
15 Paid Andco Company the amount due on the purchase of May 5.
16 Of the merchandise sold May 14, $4,620 was returned for credit.
19 Salaries for services received were paid for the month of May as follows: office employees, $5,600; and salespersons, $11,200.
24 The company collected the amount due on $42,000 of the accounts receivable arising from the sale of May 14.
25 The company purchased merchandise on account from Hill Company, $50,400; terms 2/10, n/30. Freight terms were FOB shipping point.
27 Of the merchandise purchased May 25, $8,400 was returned to the vendor.
28 A trucking company was paid $700 for delivery to the Hall Western Wear Company of the goods purchased May 25.
29 The company sold merchandise on open account, $5,040; terms 2/10, n/30.
30 Cash sales were $24,696.
30 Cash of $33,600 was received from the sale of May 14.
31 Paid Hill Company for the merchandise purchased on May 25, taking into consideration the merchandise returned on May 27.

Additional data:

The inventory on hand at the close of business on May 31 is $99,680.

Required: From the data given for the Hall Western Wear Company:

a. Prepare journal entries for the transactions.
b. Post the journal entries to the proper ledger accounts.
c. Prepare a work sheet. (There were no adjusting journal entries.)
d. Prepare a classified income statement for the month ended May 31, 1987.
e. Prepare a classified balance sheet as of May 31, 1987.
f. Prepare and post the necessary closing entries.

BUSINESS DECISION PROBLEM

Prepare income statement and balance sheet for merchandising company

Tom Steele taught physical education classes at Brooke High School for 20 years. In 1986, Tom's uncle died and left Tom $100,000. Tom quit his teaching job in December of 1986 and opened a hardware store in January of 1987. On January 2, 1987, Tom deposited $60,000 in a checking account opened in the store's name, Steele's Hardware Store. During the first week of January, Tom rented a building and paid the first year's rent of $4,800 in advance. Also during that week, he purchased the following assets for cash:

Delivery truck	$10,000
Store equipment	5,000
Office equipment	3,000

During the remainder of the first six months of 1987, Tom received cash of $70,000 from customers and disbursed cash of $52,000 for merchandise purchases and $15,000 for operating expenses.

Tom never took an accounting course, but he was familiar with the term **net income.** He decided to compute his net income for the first six months of 1987 and prepared the following schedule:

Cash receipts		$ 70,000
Cash disbursements:		
Delivery truck	$10,000	
Store equipment	5,000	
Office equipment	3,000	
Prepaid rent	4,800	
Merchandise purchases . .	52,000	
Operating expenses . . .	15,000	89,800
Net loss		$(19,800)

Assume that the depreciation amounts for the six-month period are as follows:

Delivery truck	$1,000
Store equipment	250
Office equipment	175

Also assume that you obtained the following information:

1. Steele owes $8,000 to creditors for merchandise purchases.
2. Customers owe Steele $10,000 on June 30, 1987 for goods purchased.
3. Merchandise costing $16,000 is on hand at the end of the six months.

Required: a. Do you agree with Tom Steele's statement that his hardware store suffered a net loss of $19,800 for the six months ended June 30, 1987? If not, show how you would determine the net income (or net loss).

b. Is it possible to prepare a balance sheet on June 30, 1987, or does Mr. Steele have to wait until December 31, 1987, to prepare a balance sheet? If a balance sheet can be prepared on June 30, 1987, prepare one.

BUSINESS SITUATION FOR DISCUSSION

Retailers: Head Off Credit Cards with Cash Discounts?*

Michael Levy and Charles A. Ingene

Calls for a cashless society appeared regularly in the business press in the 1970s. Futurists predicted that plastic cards, both credit and debit, would replace green paper. Alas, polish for the crystal ball is in order. High interest rates and state usury laws have caused many retailers to examine their consumer credit policies for ways to wipe out red ink. Many retailers are experimenting with new strategies.

* * * * *

Exxon, Amoco, Sohio, and Mobil have been trying out various ways of offering discounts for cash in lieu of credit card sales. Mobil has lowered its wholesale price while adding a 3% processing fee for credit sales to induce station managers to favor cash sales. As a result, signs have sprouted at Mobil stations offering consumers gasoline at 4 cents a gallon less if they pay cash.

Retailers of other goods have jumped on the bandwagon too. Breuners, a furniture dealer in California, offers a 5% discount for cash, while 4 Day Tire Stores, also based in California, advertises 2%.

The idea received a boost in the summer of 1981 when Congress passed the Cash Discount Act, permitting businesses to give discounts exceeding 5% to consumers paying cash. Previously, a rebate of more than 5% was considered a finance charge levied against credit card users and was therefore illegal.

The retailer incurs two costs in each credit card transaction: the factoring fee to convert the charge to cash and the interest expense arising from the time lag between the sale and collection of funds. If, for example, his cost of capital is 20%, if an average six days elapse between the sale and collection of the proceeds, and if the factor's fee is 5%, then $10,000 in credit sales are equivalent to $9,472 in cash sales. The retailer could offer a cash discount of 5.3% and still be as well off as with a credit card sale.

Although many retailers might like to reject credit cards altogether because of their expense, up to now they have been ill-advised to take this step unless most of their competitors followed suit. Otherwise, they could suffer a differential disadvantage.

The retailer should consider four elements before adopting a discount-for-cash policy:

The reasons why his customers use credit cards. If it's just because they like the convenience of not carrying cash or consider it an advantage to buy now and pay later, they are candidates for a cash discount strategy. If, however, customers *need* the credit in order to make a purchase, a small cash reduction for cash payment probably would not deter their use of credit cards.

The proportion of his volume made up by cash sales. If the proportion is high, a discount-for-cash policy would give many customers who would have paid cash anyway a "free" deduction. Obviously, the effect on the retailer's earnings would not be healthy.

The cost of implementing the new policy. Computerized cash registers permit programming of a dis-

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