P3-1, E2-11, AP2-3

P1–3 Comparing Net Earnings with Cash Flow (A Challenging Problem)

Choice Chicken Company was organized on January 1, 2020. At the end of the first quarter (three months) of operations, the owner prepared a summary of its activities as shown in the first row of the following tabulation:

		Computation of:	
Summary of Transactions		**Net Earnings = R – E**	**Cash**
a.	Services performed for customers, $85,000, of which $15,000 remained uncollected at the end of the quarter.	+$85,000	+$70,000
b.	Cash borrowed from the local bank, $25,000 (one-year note).	0	+ 25,000
c.	Small service truck purchased at the end of the quarter to be used in the business for two years starting the next quarter: cost, $8,000 cash.	0	- 8,000
d.	Wages earned by employees, $36,000, of which one-sixth remained unpaid at the end of the quarter.	- 36,000	- 30,000
e.	Service supplies purchased for use in the business, $4,000 cash, of which $1,000 were unused (still on hand) at the end of the quarter.	- 3,000	- 4,000
f.	Other operating expenses, $31,000, of which one-half remained unpaid at the end of the quarter.	- 31,000	- 15,500
Based only on these transactions, compute the following for the quarter:			
Net earnings (or loss)		+ 15,000	
Cash inflow (or outflow)			+ 37,500

Required:

1. For each of the six transactions given in this tabulation, enter what you consider the correct amounts. Enter a zero when appropriate. The first transaction is illustrated.

2. For each transaction, explain the basis for your responses.

E2–11 Analyzing the Effects of Transactions in T-Accounts

Grady Service Company Inc. was organized by Chris Grady and five other investors. The following events occurred during the year:

a. Received $63,000 cash from the investors; each was issued 1,400 shares.
b. Purchased equipment for use in the business at a cost of $16,000; one-fourth was paid in cash, and the company signed a note for the balance, payable in six months.
c. Signed an agreement with a cleaning service to pay it $200 per week for cleaning the corporate offices.
d. Lent $2,500 to one of the investors, who signed a note due in six months.
e. Issued shares to additional investors, who contributed $6,000 in cash and a lot of land valued at $15,000.
f. Paid the amount of the note payable in (*b*).
g. Chris Grady borrowed $10,000 for personal use from a local bank and signed a note payable in one year.

Required:

1. Prepare journal entries for each transaction. If an event does not require a journal entry, explain the reason. Use the account titles listed in (2).
2. Create T-accounts for the following accounts: cash, note receivable, equipment, land, note payable, and contributed capital. Beginning balances are zero. For each of the preceding transactions, record the effects of the transaction in the appropriate T-accounts. Include good referencing and totals for each T-account.
3. Using the balances in the T-accounts, fill in the following amounts for the accounting equation:

Assets $______ = Liabilities $______ + Shareholders' Equity $______

1.

	General Journal	Debit	Credit
a.	Cash (+A)	63,000	
	Contributed capital (+SE)		63,000
	Issuance of shares for cash.		
b.	Equipment (+A)	16,000	
	Cash (-A) (16,000 /4)		4,000
	Note payable (+L)		12,000
c.	No exchange → No entry		
d.	Note receivable (+A)	2,500	
	Cash (-A)		2,500
e.	Cash (+A)	6,000	
	Land (+A)	15,000	
	Contributed capital (+SE)		21,000
f.	Note payable (-L)	12,000	
	Cash (-A)		12,000
e.	No entry, separate entity assumption		

2.

+	Cash (CA)		–
Beg.	0		
a.	63,000		
e.	6,000	4,000	b.
		2,500	d.

+	Note Receivable (CA)		–
Beg.	0		
d.	2,500		
End.	2,500		

		12,000	f.
End.	50,500		

+	Equipment (NCA)		−
Beg.	0		
b.	16,000		
End.	16,000		

+	Land (NCA)		−
Beg.	0		
e.	15,000		
End.	15,000		

−	Note Payable (CL)		+
		0	Beg.
f.	12,000	12,000	b.
		0	End.

−	Contributed Capital (SE)		+
		0	Beg.
		63,000	a.
		21,000	e.
		84,000	End.

3.

A = L + SE; $84,000 = $0 + $84,000

AP2–3 Recording Transactions in T-Accounts, Preparing a Statement of Financial Position, and Evaluating the Current Ratio

Modern Interiors Inc. is a leading interior design company and manufacturer and retailer of home furnishings. The following is adapted from Modern Interiors's recent annual financial statements for fiscal year ended on June 30. Dollar amounts are in thousands.

Cash and cash equivalents	$ 57,701	Accounts payable	$ 16,961
Accounts receivable	12,293	Accrued liabilities	43,793
Inventories	149,483	Deferred revenue	62,960
Prepaid expenses and other current assets	23,621	Long-term debt	14,339
Property, plant, and equipment	270,198	Other non-current liabilities	29,273
Intangible assets	45,128	Contributed capital	43,051
Long-term investments	7,330	Retained earnings	357,845
Other non-current assets	2,468		

Assume that the following transactions ($ in thousands) occurred in the first quarter ended September 30 of the fiscal year:

a. Issued 1,600 additional shares for $1,020 in cash.
b. Purchased $3,400 in additional intangibles for cash.
c. Ordered $43,500 in wood and other raw materials for the manufacturing plants.
d. Sold equipment at its cost for $4,020 cash.
e. Purchased $2,980 in long-term investments for cash.
f. Purchased property, plant, and equipment; paid $1,830 in cash and signed additional long-term notes for $9,400.
g. Sold at cost other assets for $310 cash.
h. Declared $300 in dividends, payable in October.

1.

+	Cash and Cash Equivalents (CA)		–
Beg.	57,701		
a.	1,020	3,400	a.
d.	4,020	2,980	e.
g.	310	1,830	f.
End.			

+	Accounts Receivable (CA)		–
Beg.	12,293		
End.			

+	Inventories (CA)		–
Beg.	149,483		
End.			

+	Prepaid Expenses & Other CA		–
Beg.	26,321		
End.			

+	Property, Plant and Equip. (NCA)		–
Beg.	270,198		
f.	11,230	4,020	d.
End.			

+	Intangible Assets (NCA)		–
Beg.	45,128		
a.	3,400		
End.			

+	Long-Term Investments (NCA)		–
Beg.	7,330		
e.	2,980		
End.			

+	Other Non-current Assets (NCA)		–
Beg.	2,468		
		310	g.
End.			

–	Accounts Payable (CL)		+
		16,961	Beg.
			End.

–	Accrued Liabilities (CL)		+
		43,793	Beg.
			End.

–	Deferred Revenue (CL)		+
		62,960	Beg.
			End.

–	Dividends Payable (CL)		+
		0	Beg.
		300	h.
			End.

Required:

1. Create T-accounts for each of the accounts listed above, including a new account Dividends Payable. Enter the balances at June 30 as the beginning balances for the quarter (in thousands of dollars).
2. Record each of the transactions for the first quarter ended September 30 in the T-accounts (including referencing) and determine the ending balances.
3. Explain your response to event (*c*).
4. Prepare a trial balance at September 30.

–	Long-Term Debt (NCL)		+
		14,339	Beg.
		9,400	f.
			End.

–	Other Non-current Liab. (NCL)		+
		29,273	Beg.
			End.

–	Contributed Capital (SE)		+
		43,051	Beg.
		1,020	a.
			End.

–	Retained Earnings (SE)		+
		357,845	Beg.
h.	300		
			End.

4.

Modern Interiors Inc.
Trial Balance
At September 30
(in thousands of dollars)

	Debit	**Credit**
Cash and cash equivalents	$ 54,841	
Accounts receivable	12,293	
Inventories	149,483	
Prepaid expenses and other current assets	23,621	
Property, plant, and equipment	277,408	
Intangible assets	48,528	
Long-term investments	10,310	
Other non-current assets	2,158	
Accounts payable		$ 16,961
Accrued liabilities		43,793
Deferred revenue		62,960
Dividends payable		300
Long-term debt (current portion, $2,731)		23,739
Other non-current liabilities		29,273
Contributed capital		44,071
Retained earnings		357,545
Totals	$578,642	$578,642

5. Prepare a classified statement of financial position at September 30. The company's accountant determined that $2,731 of long-term debt must be paid during the next fiscal year.

5.

Modern Interiors Inc.
Statement of Financial Position
At September 30
(in thousands of dollars)

Assets	
Current assets	
Cash and cash equivalents	$ 54,841
Accounts receivable	12,293
Inventories	149,483
Prepaid expenses and other current assets	23,621
Total current assets	240,238
Property, plant, and equipment	277,408
Intangible assets	48,528
Long-term investments	10,310
Other non-current assets	2,158
Total Assets	$578,642
Liabilities	
Current liabilities	
Accounts payable	$ 16,961
Deferred revenue	62,960
Accrued liabilities	43,793
Dividends payable	300
Current portion of long-term debt	2,731
Total current liabilities	126,745
Long-term debt	21,008
Other non-current liabilities	29,273
Total Liabilities	177,026
Shareholders' Equity	
Contributed capital	44,071
Retained earnings	357,545
Total Shareholders' Equity	401,616
Total Liabilities and Shareholders' Equity	$578,642

6. Compute the current ratio at September 30. Round your answer to two decimal places. What does this suggest about Modern Interiors Inc.?

6. Current Ratio = Current Assets/Current Liabilities = $240,238 / $126,745 = 1.9