

**NATIONAL UNIVERSITY OF SINGAPORE**

**EC2204: Financial Accounting for Economists**

**Semester 1, AY2019/2020**

**Time allowed: 2 Hours**

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**INSTRUCTIONS TO CANDIDATES**

1. Write your student number only. Do not write your name.
2. This assessment paper contains FIVE (5) questions and comprises SIX (6) printed pages, including this page.
3. Answer ALL questions.
4. Start each question on a new page.
5. This is a CLOSED book examination.
6. You may use a scientific (non-graphing) calculator.
7. The total mark for this paper is 50.

**Question 1:**

The management team of Strawberry Shortcake Limited is preparing its annual financial statements. The statements are complete except for the statement of cash flows. The completed comparative balance sheets and income statement are as follows:

Balance Sheet on the following dates:

	<u>30 June 2019</u>	<u>30 June 2018</u>
<b>Assets:</b>		
Cash	\$ 50,000	\$ 72,000
Accounts Receivable	80,000	70,000
Merchandise Inventory	60,000	65,000
Property and Equipment	110,000	60,000
Less: Accumulated Depreciation	<u>(30,000)</u>	<u>(15,000)</u>
<b>Total Assets</b>	<u><b>\$270,000</b></u>	<u><b>\$252,000</b></u>
<b>Liabilities:</b>		
Accounts Payable	\$ 10,000	\$ 12,000
Salaries and Wages Payable	2,000	1,000
Notes Payable, Long-Term	50,000	60,000
<b>Stockholders' Equity:</b>		
Common Stock	100,000	80,000
Retained Earnings	<u>108,000</u>	<u>99,000</u>
<b>Total Liabilities and Stockholders' Equity</b>	<u><b>\$270,000</b></u>	<u><b>\$252,000</b></u>

Income Statement for the year ended 30 June 2019

Sales	\$200,000
Cost of Goods Sold	110,000
Depreciation Expense	15,000
Other Expenses	<u>50,000</u>
<b>Net Profit</b>	<u><b>\$ 25,000</b></u>

Other information from the company's records includes the following:

- Bought equipment for cash, \$50,000.
- Paid \$10,000 on long-term note payable.
- Issued new shares of common stock for \$20,000 cash.
- Cash dividends of \$16,000 were declared and paid to stockholders.
- Accounts Payable arose from inventory purchases on credit.
- Income Tax Expense (\$4,000) and Interest Expense (\$3,000) were paid in full at the end of both years and are included in Other Expenses.

(a) (6 marks) Prepare the Statement of Cash Flows for the year ended 30 June 2019.

(b) (4 marks) Using the Statement of Cash Flows, evaluate the financial stability of the company for the year.

**Question 2:**

Consider a new start-up Blueberry Muffin Limited which began business on 1 January 2018 by issuing all of its 1,000,000 authorized shares of its \$1 par value common stock for \$40 per share.

On 30 June 2018, the company declared a cash dividend of \$2 per share to shareholders of record on 31 July 2018.

On 30 August 2018, the company paid the cash dividend.

On 1 November 2018, the company reacquired 200,000 of its own shares of stock for \$50 per share.

On 22 December 2018, the company resold 100,000 of these shares for \$60 per share.

- (a) (6 marks) Prepare all of the necessary journal entries to record the events described above.
- (b) (4 marks) Given that the net profit for the year was \$6,000,000, prepare the shareholders' equity section of the balance sheet on 31 December 2018.

**Question 3:**

- (a) (3 marks) Identify the role of the matching principle in accounting for long-lived assets.
- (b) (3 marks) If an entity overstates its ending inventory for the current year, what are the effects on the income statement and balance sheet?
- (c) (4 marks) During a period of rapidly rising inventory prices and a significant increase in inventory, a financial analyst made the following statement:

"I rank a company's earning power by using earnings per share. You do not need to understand accounting policies in order to compare earnings per share of two companies."

Respond to the statement made by the financial analyst relating to the implications of choosing an inventory valuation method.

**Question 4:**

- (a) (4 marks) Orchard Blossom Limited adjusts its books each month. The trial balance at 31 March 2018 *before adjustments* is as follows:

	<u>Debit</u>	<u>Credit</u>
Cash	\$10,920	
Accounts Receivable	9,620	
Supplies	1,300	
Prepaid Insurance	3,120	
Equipment	26,000	
Accumulated Depreciation: Equipment		\$ 10,400
Unearned Service Revenue		6,500
Share Capital		5,200
Retained Earnings		23,400
Dividends	1,560	
Service Revenue Earned		16,510
Salaries Expense	7,800	
Utilities Expense	390	
Rent Expense	<u>1,300</u>	
	\$62,010	<u>\$62,010</u>

- (i) According to service contracts, \$4,810 of the Unearned Service Revenue has been earned in March. Determine the amount of Service Revenue earned to be reported in the March income statement.
- (ii) On 1 March 2018, Orchard Blossom Limited paid in advance for four months' insurance. Determine the necessary adjusting entries at 31 March 2018.
- (iii) The equipment had an estimated useful life of five years with no residual value.

Given that the firm used a straight-line depreciation method, compute the book value of the equipment at 31 March 2018 (after the proper March adjustment is recorded).

- (b) (6 marks) Lemon Meringue is an American based company that reports its financial statements using the U.S. dollars. Prepare journal entries to record each of the following events for Lemon Meringue.
- (i) **10 October 2018:** Purchased merchandise on account from Le Croissant, a French company, for 80,000 euros. The exchange rate was \$0.82 U.S. dollars per Euro.
  - (ii) **2 November 2018:** Paid Le Croissant for the merchandise purchased on October 1. The exchange rate at this date was \$0.83 U.S. dollars per Euro.
  - (iii) **15 November 2018:** Sold merchandise to Oishi Desu, a Japanese company, for 300,000 yen on account. The rate of exchange was 0.0091 U.S. dollars per yen.
  - (iv) **20 November 2018:** The Japanese company, Oishi Desu, paid the full amount. The exchange rate was 0.0090 U.S. dollars per yen.
  - (v) **5 December 2018:** Sold merchandise to Pisa Mon, an Italian company, for \$24,000. The exchange rate is 0.81 U.S. dollars per Euro. The Italian company agrees to pay in U.S. dollars.
  - (vi) **18 December 2018:** Collected the full amount from the Italian company, Pisa Mon. The exchange rate is 0.79 U.S. dollars per Euro.

**Question 5:**

- (a) (6 marks) Given below are comparative balance sheets and an income statement for Raspberry Torte in the Year 2017.

Raspberry Torte Balance Sheets in the Year 2017			Raspberry Torte Income Statement	
	31 December	1 January	For the year ended 31 December 2017	
Equipment (net)	\$ 57,200	\$66,300	Sales	\$228,800
Inventory	32,500	36,400	Cost of goods sold	(137,540)
Accounts receivable	46,800	37,700	Gross profit on sales	\$ 91,260
Cash	<u>15,600</u>	<u>15,600</u>	Operating expenses	<u>(75,868)</u>
	<u>\$152,100</u>	<u>\$156,000</u>	Operating profit	\$ 15,392
			Interest expense and income taxes	<u>(9,100)</u>
Accounts payable	26,000	28,600	Net Profit	<u>\$ 6,292</u>
Dividends payable	7,800	3,900		
Long-term note payable	14,300	14,300		
Share capital, \$5 par	72,800	72,800		
Retained earnings	<u>31,200</u>	<u>36,400</u>		
	<u>\$152,100</u>	<u>\$156,000</u>		

- (i) Calculate the Cash Conversion Cycle of Raspberry Torte.  
State your assumptions clearly.
- (ii) Evaluate the profitability of Raspberry Torte using different financial ratios.
- (b) (4 marks) Consider the balance sheet of Plum Pudding as of 31 December 2018.

Plum Pudding  
Balance Sheet as as of 31 December 2018

Equipment (net)	\$ 30,000	Current Liabilities	10,000
Inventory	1,000	Long Term Bonds	6,000
Accounts receivable	1,000		<u>\$16,000</u>
Cash	10,000		
	<u>\$42,000</u>	Share capital, \$5 par	16,000
		Retained earnings	<u>10,000</u>
			<u>\$26,000</u>

The management is considering using \$3,000 of excess cash to prepay \$3,000 of outstanding bonds. Discuss the implications on the liquidity and solvency ratios of Plum Pudding.

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