

SOLUTION TO EXAM 2, FALL 2020

Question 1: Multiple Choice

1. B 2. C 3. D 4. C
5. C [Correct balance = \$12,956.73 – \$2,112.19 = \$10,844.54.
Correct balance = Cash balance per books – \$654.19 = \$10,844.54
Cash balance per books = \$10,844.54 + \$654.19 = \$11,498.73

Question 2: Accounting for doubtful accounts

(a)

Schedule of Accounts Receivable by Age			
December 31, 2020 Accounts Receivable	Age of Accounts Receivable	Expected Percentage Uncollectible	Allowance for doubtful accounts
140,000	Not yet due	0.75%	1,050
60,000	1-30 days past due	4%	2,400
19,000	31-60 days past due	10%	1,900
5,000	61-90 days past due	60%	3,000
7,000	Over 90 days past due	90%	6,300
Totals			\$14,650

(b)

Bad debt expense	19,850	
Allowance for doubtful accounts		19,850

Calculation: \$44,000 – \$49,200 + Bad debts expense = \$14,650; → Bad debts expense = \$19,850

The determination of bad debts expense could be shown as:

Allowance for doubtful accounts			
		44,000	Beginning balance
Write-offs during the year	49,200		
	5,200		Ending balance before adjustment
		19,850	Bad debts expense (computed)
		14,650	Ending balance based on aging of A/R

c)

S&R Company	
Partial Statement of Financial Position	
As at December 31, 2020	
Current Assets	
Accounts Receivable	\$231,000
Less: Allowance for doubtful accounts	<u>14,650</u>
Net realizable accounts receivable	<u>\$216,350</u>

Question 3: Accounting for inventory and cost of sales

Req. a)

Weighted Average Cost = $\frac{\text{Cost of goods available for sale (COGAS)}}{\text{Number of units available for sale (NUAS)}}$

COGAS after second purchase = $(10,000 - 8,000) \times \$1.50 + (2,500 \times \$2.00) = \$8,000$

NUAS = $2,000 + 2,500 = 4,500$

WAC2 = $\$8,000 / 4,500 = \1.78 per unit (rounded)

Number of units in ending inventory = $4,500 - 2,500 = 2,000$

Cost of ending inventory = $(\$1.78 \times 2,000) = \mathbf{\$3,560}$

Cost of sales = $(8,000 \times \$1.50) + (2,500 \times \$1.78) = \$12,000 + \$4,450 = \mathbf{\$16,450}$ Or

COS = COGAS – Ending inventory = $(\$15,000 + \$5,000) - \$3,560 = \mathbf{\$16,440}$ (difference due to rounding)

Gross profit = Sales – COS

= $(8,000 \times \$4.50) + (2,500 \times \$4.80) - 16,450$ (or 16,440 depending on COS above)

= $\$48,000 - 16,450 = \mathbf{\$31,550}$

Gross profit percentage = Gross profit / Sales = $\$31,550 / \$48,000 = 0.66$ (rounded)

Req. b)

(d) Dec. 17	Accounts receivable	12,000	
	Sales revenue (2,500 x \$4.80)		12,000
	Cost of sales	4,450	
	Inventory (2,500 x \$1.78)		4,450

Req. c)

Inventory turnover ratio = Cost of sales / Average inventory
= \$16,450 / ((\$7000 + 3,560)/2) = \$16,450 / \$5,280 = 3.1155 = 3.12

The company buys and sells its inventory 3.12 times per year.

Req. d)

The gross profit will be higher if Dora Corporation used a periodic inventory system and the FIFO method. The reason is that the FIFO method produces a lower cost of sales than the weighted average cost method (or the weighted-average cost method produces a higher cost of sales than FIFO) when unit costs are rising.

Req. e)

- Understatement of COS by \$890 or 900 (depending on calculation)
*Calculation: [$\$1.78 \times (2,500 - 2,000)$] = 800 **OR** $\$1.78 \times 2,500 = \$4,450 = \text{Ending Inv}$; $\text{COS} = \$20,000 - 4,450 = \$15,550$; $\text{Change in COS} = \$16,450 - 15,550 = \$900 \text{ understatement}$*
- Overstatement of income tax expense by \$267 ($\$890 \times 30\%$) **OR** \$270 ($\$900 \times 30\%$)

Question 4: Long-lived Assets

Req. a)

Total acquisition cost: $\$313,000 + 7,000 = \$320,000$

Note that the delivery of furniture and fixtures was paid by the supplier, not Walton, the additional fees are applicable to prepare the building only, and the financing cost should not be included in the acquisition cost except in the case of construction of an asset by Walton and only during the period of construction.

Total appraised value: $\$70,000 + 52,500 + 227,500 = \$350,000$

Land: $(\$70,000/350,000) \times 320,000 = \$64,000$

Building: $(\$227,500 / 350,000) \times 320,000 + \$2,000 = \$210,000$

Furniture and Fixtures: $(\$52,500 / \$350,000) \times 320,000 = \$48,000$

Req. b)

Building Depreciation = $(\$210,000 - 30,000) / 20 = \$9,000$

Depreciation expense	9,000
Accumulated Depreciation – Building	9,000

Req. c)

2019: FF Depreciation = $\$48,000 \times 2/5 = \$19,200$

Note that the residual value should not be subtracted from the acquisition cost.

2020: FF Depreciation = $(\$48,000 - 19,200) \times 2/5 = \$28,800 \times 2/5 = \$11,520$.

Req. d)

Depreciation expense – Furniture and fixtures	2,221
Accumulated Depreciation – Furniture and Fixtures	2,221

Depreciation for 2023 = $\$6,221 \times 2/5 = \$2,488$

Carrying amount after depreciation = $\$6,221 - 2,488 = \$3,733 < \$4,000$ residual value

The depreciation expense for 2023 is revised to ensure that the carrying amount does not falls below \$4,000.

Depreciation expense for 2023 = $\$6,221 - 4,000 = \$2,221$

Req. e)

Carrying value of Furniture and Fixtures = \$4,000; Sold for \$5,000 cash

Cash	5,000
Accumulated Depreciation - Furniture and Fixtures	44,000
Furniture and Fixtures	48,000
Gain on sale of Furniture and Fixtures	1,000

Question 5: Journal Entries

December 1:	Inventory	22,000
	Cash	2,000
	Accounts Payable	20,000
December 1:	Cash	40,000
	Note payable (short-term)	40,000
December 3:	Accounts Receivable	15,000
	Deferred (Unearned) revenue	15,000
	Sales Revenue	30,000
	Cost of Sales	19,500
	Inventory	19,500
	<i>Calculation: $\\$30,000 \times (1 - 0.35)$</i>	
December 9:	Accounts Payable	20,000
	Cash	19,600
	Inventory	400

December 25: Cash	15,000
Accounts receivable	15,000

December 27: No journal entry (Chapter 9)

This is a contingent liability. Since no estimate can be made, no accrual is required.
Monmouth should disclose the contingency in the notes to the financial statements.

December 31: Interest Expense	150
Cr Cash	150

Calculation: $40,000 \times 0.045 / 12 = 1,800 / 12 = 150$

December 31: Salaries Expense (Chapter 9)	16,200
Cash	11,950
Canada Pension Plan (CPP) Payable	1,200
Employment Insurance (EI) Payable	250
Income taxes withheld	2,800
Salaries Expense	1,550
Canada Pension Plan (CPP) Payable	1,200
Employment Insurance (EI) Payable	350

Calculation of EI: $= \$250 \times 1.4 = \350

NOTE: The two entries can be combined as follows:

Salaries Expense	17,750
Cash	11,950
Canada Pension Plan (CPP) Payable	2,400
Employment Insurance (EI) Payable	600
Income taxes withheld	2,800

Calculation of EI: $= \$250 + \$250 \times 1.4 = \$600$