## Chapter 1: Business, Accounting, and You

## Discussion Questions: Key Points

1. The economic events that affect a business are communicated through the accounting function. Language helps us to make sense of the world around us. If we don’t know the language, we will be limited in our ability to operate effectively in the business environment.
2. Valid arguments can be made on both sides of this question. Without technical knowledge an accountant will not be able to provide much value. Without ethics, however, an accountant can be dangerous. Accounting exists because of a need for an objective account of the economic events that affect an entity.
3. Financial statements seek to provide information about the events that have already occurred. For example, the cost principle is used to carry assets on the books. It is up to the user to make projections as to how past transactions are likely to affect future events.
4. Reasons why—reliability, objectivity. Disadvantages—relevance, decision-usefulness.
5. Financial statement uses discussed in the text: allow investors and creditors to make investment decisions, enable suppliers and customers to determine the financial condition of a business, and report to regulatory agencies.
6. It is a separate legal entity from its owners. Factors—liability of owners for business activities, taxation, distribution of income.
7. A = L + SE. Assets—things of value a company has. Liabilities—amount a business owes to third parties. Stockholder’s equity—the amount of assets that is owned by the stockholders.
8. The transactions would have the following effects:
   1. A+, SE+
   2. A+, L+
   3. A+, SE+
   4. A+, A-
9. Income Statement, Statement of Retained Earnings, Balance Sheet, Statement of Cash Flows. The financial statements articulate (join together). The income statement needs to be prepared in order to produce the net income amount that is reported on the statement of retained earnings. The ending balance in retained earnings is needed in order to prepare the balance sheet. The ending balance in cash on the balance sheet and other information is needed for the statement of cash flows.
10. The financial statements are
    1. Balance sheet
    2. Statement of retained earnings
    3. Statement of cash flows
    4. Income statement

## Short Exercises

**(5-10 min.) S 1-1**

1. d
2. a
3. c
4. b

**(5-10 min.) S 1-2**

Answer: d. Cost Principle

**(10-15 min.) S 1-3**

1. e
2. f
3. d
4. g
5. b
6. c
7. a

**(5-10 min.) S 1-4**

a. $82,000 ($106,000 − $24,000)

b. $91,000 ($63,000 + $28,000)

c. $49,000 ($94,000 − $45,000)

**(5-10 min.) S 1-5**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Assets** | **=** | Liabilities | **+** | Stockholder’s Equity |
|  |  |  |  |  |
|  |  | Accounts Notes |  | Stockholder’s |
| Cash + Equipment | = | payable + payable | + | equity |
|  |  |  |  |  |
| $13,000 + $35,000 | = | $9,000 + $5,000 | + | $34,000 |

Based on the accounting equation, Beach has $34,000 of equity in the business. Assets of $48,000 ($13,000 + $35,000) − Liabilities of $14,000 ($9,000 + $5,000) = Stockholder’s equity of $34,000.

**(5-10 min.) S 1-6**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Assets | **=** | Liabilities | **+** | Stockholders’ Equity |
|  |  |  |  |  |
| Cash + Supplies | = |  | + | Stockholders’ equity |
|  |  |  |  |  |
| $36,000 + $1,500 | = | $9,500 | + | $28,000 |

Based on the accounting equation, Boehms has $9,500 of liabilities. Assets of $37,500 ($36,000 + $1,500) − Stockholders’ equity of $28,000 = Liabilities of $9,500

**(5-10 min.) S 1-7**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Assets | **=** | Liabilities | **+** | Stockholders’ Equity |
|  |  |  |  |  |  |
|  | Cash | = | Notes Payable | + | Common Stock |
| Investment | + $15,000 | = |  |  | + $15,000 |
| Borrowing | + 18,000 | = | + $18,000 | + | \_\_\_\_\_\_ |
| Bal. | $33,000 | = | $18,000 | + | $15,000 |

**(5-10 min.) S 1-8**

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | = | **Liabilities** | + | **Stockholders’ Equity** | | | | | | | | | | | |  | | | | | |
|  | **Cash** | + | **Accounts receivable** |  | **Accounts payable** |  | **Common stock** | **+** | **Retained Earnings** | | | | | | | | | |  | | |  | | |
|  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | | **Salary** | | - | | **Dividends** | | | |  | | |  | | |
|  |  |  |  |  |  |  | | **expense** | |  | |  | | | |  | | |  | | |
| a. |  |  | +$62,000 |  |  |  |  |  | + 62,000 | |  | |  | |  | |  | | | |  | | |  | | |
| b. | -$33,000 |  |  |  |  |  |  |  |  |  | + $33,000 | | |  | | | |  |  | | |  | | |

**(5-10 min.) S 1-9**

1. e

2. a

3. c

4. a

5. e

6. e

7. a

8. e

9. d

10. b

11. a

**(5-10 min.) S 1-10**

1. BS
2. BS
3. IS
4. IS
5. BS, RE
6. BS

**(5-10 min.) S 1-11**

1. d
2. e
3. b
4. a
5. c

**(5-10 min.) S 1-12**

1. Increased total assets (Cash)

2. No effect on total assets. The increase in Land offset the decrease in Cash.

3. Decreased total assets (Cash)

4. Increased total assets (Machinery and equipment)

5. Increased total assets (Accounts receivable)

6. Decreased total assets (Cash)

7. No effect on total assets. The increase in Cash offset the decrease in Accounts receivable.

8. No effect on total assets. The increase in Cash offset the decrease in Land.

9. Increased total assets (Cash)

**(5-10 min.) S 1-13**

1. True
2. False ( Increase Supplies; decrease Cash)
3. True
4. True
5. True
6. False (Decrease Cash; decrease Accounts payable)
7. True
8. True
9. False (Decrease Cash; increase Expense/decrease Stockholders’ equity)

**(5-10 min.) S 1-14**

***Req. 1***

1. g. Sold stock to start the business.

2. e. Paid cash to purchase equipment.

3. h. Purchased equipment with a bank loan.

4. a. Earned revenue for services provided, but customer will pay later.

5. d. Paid cash for expenses incurred to operate the business.

6. c. Received cash for revenue earned by providing services.

7. b. Received cash from customers for services completed earlier in the month.

8. f. Received utility bill in the mail. Bill will be paid in 30 days.

***Req. 2***

|  |  |
| --- | --- |
| Revenues (transactions “4” and “6”)………………… | $2,950 |
|  |  |
| Less: Expenses (transactions “5” and “8”)………………..…… | 1,585 |
|  |  |
| Net income………………………………………..…. | $1,365 |

## Exercises

**(10-15 min.) E 1-15A**

Hanson, Corp. $ 44,900 + $10,300 = *$55,200*

Tiny Tots Daycare, Inc. $ 97,000 - $39,000 = *$58,000*

Intermountain, Inc. $107,400 - $91,500 = *$15,900*

**(10-15 min.) E 1-16A**

***Req. 1***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Total** |  | **Total** |  | **Total** |
|  | **Assets** | **−** | **Stockholders’ Equity** | **=** | **Liabilities** |
|  |  |  |  |  |  |
| Beginning….. | $95,000 | − | $62,000 | = | $33,000 |
| Ending……… | $151,000 | − | $105,000 | = | $46,000 |
|  |  |  |  |  |  |
| Increase during the year | |  |  | = | $ 13,000 |

***Req. 2***

Possible reasons for the increase in Liabilities may include:

* Purchases were made on account
* Borrowed money on a note payable

**(10-15 min.) E 1-17A**

***Req. 1***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Total** |  | **Total** |  | **Total** |
|  | **Assets** | **−** | **Liabilities** | **=** | **Stockholders’ Equity** |
|  |  |  |  |  |  |
| Beginning….. | $40,000 | − | $26,000 | = | $14,000 |
| Ending……… | $53,000 | − | $16,000 | = | $37,000 |
|  |  |  |  |  |  |
| Increase during the year | |  |  | = | $23,000 |

***Req. 2***

Possible reasons for the increase in Stockholders’ equity may include:

* Sold stock
* Earned net income

**(15-20 min.) E 1-18A**

|  |  |  |  |
| --- | --- | --- | --- |
|  |  | **Aug. 31, 2016** | **Sept. 30, 2016** |
|  | Total assets | $105,000 | $180,000 |
| - | Total liabilities | $(75,000) | $(129,000) |
| =  -  = | Stockholders’ equity  Common stock  Retained earnings | $30,000  (10,000)  $20,000 | $51,000  (10,000)  $41,000 |

**Assumption A**: No dividends were paid

|  |  |  |  |
| --- | --- | --- | --- |
| $41,000 ending balance | | = | $20,000 Beg bal + Net income - dividends |
| $41,000 | = | | $20,000 + Net income - 0 |
| $21,000 | = | | Net income |

**Assumption B**: $10,000 of dividends were paid

|  |  |  |  |
| --- | --- | --- | --- |
| $41,000 ending balance | | = | $20,000 Beg bal + Net income - dividends |
| $41,000 | = | | $20,000 + Net income – $10,000 |
| $31,000 | = | | Net income |

**Assumption C**: $16,000 of dividends were paid

|  |  |  |  |
| --- | --- | --- | --- |
| $41,000 ending balance | | = | $20,000 Beg bal + Net income - dividends |
| $41000 | = | | $20,000 + Net income - $16,000 |
| $37,000 | = | | Net income |

**(15-20 min.) E 1-19A**

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | | | | | | | | | = | **Liabilities** | | | | | | | + | **Stockholders’ Equity** | | | | | | | | | | | | | | | | |  | | | |  | |
|  | **Cash** | + | | | **Medical supplies** | | + | | | **Land** | | | | |  | | **Accounts payable** | | | | | |  | | **Common stock** | | | | **+** | | **Retained Earnings** | | | | | | | | | | | | | | |
| **August** |  |  | | |  | |  | | |  | | | | |  | |  | | | | | |  | |  | | | |  | | **Service revenue** | | | | **–** | | **Rent expense** | | |  |  | | | | |
| **–** | **Utilities**  **expense** | | | | |
| **2** | + 60,000 |  | | |  | |  | | |  | | | | |  | |  | | | | | |  | | + 60,000 | | | |  | |  | | | |  | |  | | |  |  | | | | |
| **6** | - 45,000 |  | | |  | |  | | | +45,000 | | | | |  | |  | | | | | |  | |  | | | |  | |  | | | |  | |  | | |  |  | | | | |
| **11** |  |  | | | + 700 | |  | | |  | | | | |  | | + 700 | | | | | |  | |  | | | |  | |  | | | |  | |  | | |  |  | | | | |
| **15** | No entry | |  | |  | | | |  | | |  | | | | | |  | |  | | | | | |  | |  | | | |  | |  | | |  | | |  |
| **17** | + 10,000 |  | | |  | |  | | |  | | | | |  | |  | | | | | |  | |  | | | |  | | + 10,000 | | | |  | |  | | |  |  | | | | |
| **19** | - 1,400 |  | | |  | |  | | |  | | | | |  | |  | | | | | |  | |  | | | |  | |  | | | |  | | + 1,400 | | |  |  | | | | |
| **22** | + 300 |  | | | - 300 | |  | | |  | | | | |  | |  | | | | | |  | |  | | | |  | |  | | | |  | |  | | |  |  | | | | |
| **25** |  |  | | |  | |  | | |  | | | | |  | | +175 | | | | | |  | |  | | | |  | |  | | | |  | |  | | |  | +175 | | | | |
| **30** | -100 |  | | |  | |  | | |  | | | | |  | | -100 | | | | | |  | |  | | | |  | |  | | | |  | |  | | |  |  | | | | |
| Bal. | $23,800 | + | | | $400 | | + | | | $45,000 | | | | | = | | $775 | | | | | | + | | $60,000 | | | | + | | $10,000 | | | | **–** | | $1,400 | | | **–** | $175 | | | | |
|  |  | | |  | |  | |  | | |  | | | | |  | | |  | | | | |  | | |  | | |  | | |  | | |  | |  | | | |  | |  | | |

**(10-15 min.) E 1-20A**

***Req. 1***

The business is a corporation, as shown by the fact that it has a common stock account.

***Req. 2***

|  |  |  |  |
| --- | --- | --- | --- |
| **Fitness Fanatics, Inc.** | | | |
| **Balance Sheet** | | | |
| **March 31, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $ 15,000 | Accounts payable | $3,300 |
| Accounts receivable | 600 | Note payable | 5,000 |
| Supplies | 700 | Total liabilities | 8,300 |
| Office equipment | 10,300 | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 6,000 |
|  |  | Retained earnings | 12,300 |
|  |  | Total Stockholders’ equity | 18,300 |
|  |  | Total liabilities and |  |
| Total assets | $26,600 | stockholders’ equity | $26,600 |

***Req. 3***

The balance sheet reports the financial position of a company at a given point in time and that Assets = Liabilities + Stockholders’ Equity.

**(15-20 min.) E 1-21A**

***Req. 1***

|  |  |  |  |
| --- | --- | --- | --- |
| **Account** | **Type of Account** | **Account** | **Type of Account** |
| Office furniture | Asset | Rent expense | Expense |
| Utilities expense | Expense | Cash | Asset |
| Accounts payable | Liability | Office supplies | Asset |
| Notes payable | Liability | Salaries expense | Expense |
| Service revenue | Revenue | Salaries payable | Liability |
| Accounts receivable | Asset | Property tax expense | Expense |
| Supplies expense | Expense | Equipment | Asset |
|  |  |  |  |

***Req. 2***

|  |  |  |
| --- | --- | --- |
| **Annis Consulting, Inc.** | | |
| **Income Statement** | | |
| **For the Year Ended December 31, 2016** | | |
| Service Revenue |  | $141,500 |
|  |  |  |
| Expenses |  |  |
| Salaries expense | $41,000 |  |
| Rent expense | 40,000 |  |
| Utilities expense | 13,500 |  |
| Supplies expense | 3,800 |  |
| Property tax expense | 2,000 |  |
| Total expenses |  | 100,300 |
| Net income |  | $ 41,200 |

Results of operations for 2016: Net income of $41,200

**(15-20 min.) E 1-21A Cont.**

***Req 3***

|  |  |
| --- | --- |
| **Annis Consulting, Inc.**  **Statement of Retained Earnings**  **For the Year Ended December 31, 2016** | |
| Retained earnings, Jan. 1, 2016 | $0 |
| Add: Net income | 41,200 |
| Subtotal | 41,200 |
| Less: Dividends | **5,000** |
| Retained earnings, Dec. 31, 2016 | $36,200 |

The dividends for the year were $5,000. ($0 + $41,200 - $36,200)

**(15-20 min.) E 1-22A**

***Req 1***

|  |  |  |
| --- | --- | --- |
|  |  | **Anderson Sign, Inc.** |
| Beginning: | |  |
|  | Assets | $ 133,000 |
| − | Liabilities | 25,000 |
| = | Stockholders’ Equity | *$ 108,000* |

***Req 2***

|  |  |  |
| --- | --- | --- |
|  |  |  |
| Ending: | |  |
|  | Assets | $ 154,000 |
| − | Liabilities | 70,000 |
| = | Stockholders’ Equity | *$ 84,000* |

***Req 3***

|  |  |  |
| --- | --- | --- |
|  | Ending Stockholders’ equity | $84,000 |
| - | Beginning Stockholders’ equity | 108,000 |
| = | Change in Stockholders’ equity | (24,000) |
| - | Sale of stock | 19,000 |
| = | Change in retained earnings | (43,000) |
| + | Dividends | 40,000 |
| = | Net loss | ($3,000) |

Note: The change in Retained earnings equals Net income minus Dividends. So, Dividends are added back to the change in Retained earnings to arrive at Net income.**(10-15 min.) E 1-23B**

Lundy Plumbing Corp. $50,500 + $13,300 = *$63,800*

Sanchez Hardware, Inc. $95,000 - $34,000 = *$61,000*

Cutter & Son Cleaners, Inc. $117,900 - $88,200 = *$29,700*

**(10-15 min.) E 1-24B**

***Req. 1***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Total |  | Total |  | Total |
|  | Assets | − | Stockholders’ Equity | = | Liabilities |
|  |  |  |  |  |  |
| Beginning….. | $94,000 | − | $10,000 | = | $84,000 |
| Ending……… | $151,000 | − | $112,000 | = | $39,000 |
|  |  |  |  |  |  |
| Decrease during the year | |  |  | = | $ 45,000 |

***Req. 2***

Possible reasons for the decrease in Liabilities may include:

* Made payments on account
* Paid money on a note payable

**(10-15 min.) E 1-25B**

***Req. 1***

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Total |  | Total |  | Total |
|  | Assets | − | Liabilities | = | Stockholders’ Equity |
|  |  |  |  |  |  |
| Beginning….. | $50,000 | − | $18,000 | = | $32,000 |
| Ending……… | $39,000 | − | $10,000 | = | $29,000 |
|  |  |  |  |  |  |
| Decrease during the year | |  |  | = | $ 3,000 |

**(10-15 min.) E 1-25B (cont)**

***Req. 2***

Possible reasons for the decrease in Stockholders’ equity may include:

* Paid dividends
* Incurred a net loss

**(15-20 min.) E 1-26B**

|  |  |  |  |
| --- | --- | --- | --- |
|  |  | **Aug. 31, 2016** | **Sep. 30, 2016** |
|  | Total assets | $125,000 | $175,000 |
| - | Total liabilities | $(69,000) | $(125,000) |
| =  -  = | Stockholders’ equity  Common stock  Retained earnings | $56,000  (45,000)  $11,000 | $50,000  (45,000)  $5,000 |

**Assumption A**: No dividends were paid.

|  |  |  |  |
| --- | --- | --- | --- |
| $5,000 ending balance | | = | $11,000 Beg bal + Net income - Dividends |
| $5,000 | = | | $11,000 + Net income - 0 |
| ($6,000) | = | | Net loss |

**Assumption B**: $8,000 of dividends were paid.

|  |  |  |  |
| --- | --- | --- | --- |
| $5,000 ending balance | | = | $11,000 Beg bal + Net income - Dividends |
| $5,000 | = | | $11,000 + Net income – $8,000 |
| $2,000 | = | | Net income |

**Assumption C**: $16,000 of dividends were paid.

|  |  |  |  |
| --- | --- | --- | --- |
| $5,000 ending balance | | = | $11,000 Beg bal + Net income - Dividends |
| $5,000 | = | | $11,000 + Net income - $16,000 |
| $10,000 | = | | Net income |

**(15-20 min.) E 1-27B**

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | | = | **Liabilities** | + | **Stockholders’ Equity** | | | | |  |  |
|  | **Cash** | + | **Medical supplies** | + | **Land** |  | **Accounts payable** |  | **Common stock** | **+** | **Retained Earnings** | | | | |
| **July** |  |  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | **Rent expense** |  | **Utilities expense** |
| **–** |
| **2** | + 80,000 |  |  |  |  |  |  |  | + 80,000 |  |  |  |  |  |  |
| **6** | - 65,000 |  |  |  | + 65,000 |  |  |  |  |  |  |  |  |  |  |
| **11** |  |  | + 800 |  |  |  | + 800 |  |  |  |  |  |  |  |  |
| **15** | No entry required | | |  |  |  |  |  |  |  |  |  |  |  |  |
| **17** | + 12,000 |  |  |  |  |  |  |  |  |  | + 12,000 |  |  |  |  |
| **19** | - 2,400 |  |  |  |  |  |  |  |  |  |  |  | + 2,400 |  |  |
| **22** | + 300 |  | - 300 |  |  |  |  |  |  |  |  |  |  |  |  |
| **25** |  |  |  |  |  |  | + 235 |  |  |  |  |  |  |  | + 235 |
| **30** | -250 |  |  |  |  |  | - 250 |  |  |  |  |  |  |  |  |
| Bal. | $24,650 | + | $500 | + | $65,000 | = | $785 | + | $80,000 | + | $12,000 | **–** | $2,400 | **–** | $235 |

**(10-15 min.) E 1-28B**

***Req. 1***

The business is a corporation, as shown by the fact that it has a common stock account.

***Req. 2***

|  |  |  |  |
| --- | --- | --- | --- |
| **Jerome’s Coffee Shop, Inc.** | | | |
| **Balance Sheet** | | | |
| **March 31, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $ 22,000 | Accounts payable | $1,800 |
| Accounts receivable | 2,100 | Note payable | 5,000 |
| Supplies | 500 | Total liabilities | 6,800 |
| Office equipment | 15,100 | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 2,000 |
|  |  | Retained earnings | 30,900 |
|  |  | Total Stockholders’ equity | 32,900 |
|  |  | Total liabilities and |  |
| Total assets | $39,700 | stockholders’ equity | $39,700 |

***Req. 3***

The balance sheet reports the financial position of a company at a given point in time and that Assets = Liabilities + Stockholders’ Equity.

**(15-20 min.) E 1-29B**

***Req. 1***

|  |  |  |  |
| --- | --- | --- | --- |
| Account | Type of Account | Account | Type of Account |
| Office furniture | Asset | Rent expense | Expense |
| Utilities expense | Expense | Cash | Asset |
| Accounts payable | Liability | Office supplies | Asset |
| Notes payable | Liability | Salaries expense | Expense |
| Service revenue | Revenue | Salaries payable | Liability |
| Accounts receivable | Asset | Property tax expense | Expense |
| Supplies expense | Expense | Equipment | Asset |
|  |  |  |  |

***Req. 2***

|  |  |  |
| --- | --- | --- |
| **Andover Consulting, Inc.** | | |
| **Income Statement** | | |
| **For the Year Ended December 31, 2016** | | |
| Service Revenue |  | $139,500 |
|  |  |  |
| Expenses |  |  |
| Salaries expense | $50,000 |  |
| Rent expense | 36,000 |  |
| Utilities expense | 14,200 |  |
| Supplies expense | 4,000 |  |
| Property tax expense | 2,200 |  |
| Total expenses |  | 106,400 |
| Net income |  | $ 33,100 |

Results of operations for 2016: Net income of $33,100.

**(15-20 min.) E 1-29B Cont.**

***Req 3***

|  |  |
| --- | --- |
| **Andover Consulting, Inc.**  **Statement of Retained Earnings**  **For the Year Ended December 31, 2016** | |
| Retained earnings, Jan. 1, 2016 | $0 |
| Add: Net income | 33,100 |
| Subtotal | 33,100 |
| Less: Dividends | 15,000 |
| Retained earnings, Dec. 31, 2016 | $18,100 |

The dividends for the year were $15,000 ($0 + $33,100 - $18,100).

**(15-20 min.) E 1-30B**

***Req 1***

|  |  |  |
| --- | --- | --- |
|  |  | **Eliason, Inc.** |
| Beginning: | |  |
|  | Assets | $ 44,000 |
| − | Liabilities | 20,000 |
| = | Stockholders’ Equity | *$ 24,000* |

***Req 2***

|  |  |  |
| --- | --- | --- |
|  |  |  |
| Ending: | |  |
|  | Assets | $ 104,000 |
| − | Liabilities | 25,000 |
| = | Stockholders’ Equity | *$ 79,000* |

***Req 3***

|  |  |  |
| --- | --- | --- |
|  | Ending Stockholders’ equity | $79,000 |
| - | Beginning Stockholders’ equity | 24,000 |
| = | Change in Stockholders’ equity | 55,000 |
| - | Sale of stock | 12,000 |
| = | Change in retained earnings | 43,000 |
| + | Dividends | 60,000 |
| = | Net income | $103,000 |

Note: The change in Retained earnings equals Net income minus Dividends. So, Dividends are added back to the change in Retained earnings to arrive at Net income.

**Problems**

**(20-25 min.) P 1-31A**

***Req. 1***

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | | | | = | **Liabilities** | + | **Stockholders’ Equity** | | | | | | |
|  | **Cash** | + | **Accounts receivable** | + | **Supplies** | + | **Office furniture** |  | **Accounts payable** |  | **Common stock** | **+** | **Retained Earnings** | | | | |
| **June** |  |  |  |  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | **Rent expense** | **–** | **Dividends** |
|  |  |
| **3** | \* |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **5** | + 95,000 |  |  |  |  |  |  |  |  |  | + 95,000 |  |  |  |  |  |  |
| **Bal.** | $95,000 | + | $0 | + | $0 | + | $0 | = | $0 | + | $95,000 | + | $0 | **–** | $0 | **–** | $0 |
| **7** | - 450 |  |  |  | + 450 |  |  |  |  |  |  |  |  |  |  |  |  |
| **Bal.** | $94,550 | + | $0 | + | $450 | + | $0 | = | $0 | + | $95,000 | + | $0 | **–** | $0 | **–** | $0 |
| **9** |  |  |  |  |  |  | + 4,700 |  | + 4,700 |  |  |  |  |  |  |  |  |
| **Bal.** | $94,550 | + | $0 | + | $450 | + | $4,700 | = | $4,700 | + | $95,000 | + | $0 | **–** | $0 | **–** | $0 |
| **10** | \* |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **14** | \*\* |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **20** |  |  | + 3,800 |  |  |  |  |  |  |  |  |  | + 3,800 |  |  |  |  |
| **Bal.** | $94,550 | + | $3,800 | + | $450 | + | $4,700 | = | $4,700 | + | $95,000 | + | $3,800 | **–** | $0 | **–** | $0 |
| **27** | - 1,500 |  |  |  |  |  |  |  |  |  |  |  |  |  | + 1,500 |  |  |
| **Bal.** | $93,050 | + | $3,800 | + | $450 | + | $4,700 | = | $4,700 | + | $95,000 | + | $3,800 | **–** | $1,500 | **–** | $0 |
| **29** | - 2,000 |  |  |  |  |  |  |  | - 2,000 |  |  |  |  |  |  |  |  |
| **Bal.** | $91,050 | + | $3,800 | + | $450 | + | $4,700 | = | $2,700 | + | $95,000 | + | $3,800 | **–** | $1,500 | **–** | $0 |
| **30** | - 500 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | + 500 |
| **Bal.** | $90,550 | + | $3,800 | + | $450 | + | $4,700 | = | $2,700 | + | $95,000 | + | $3,800 | **–** | $1,500 | **–** | $500 |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| \* Represents a personal, not a business transaction | | | | | | |  |  |  |  |  |  |  |  |  |  |  |
| \*\* Not a transaction as there was no financial impact | | | | | | |  |  |  |  |  |  |  |  |  |  |  |

***Req. 2***

|  |  |  |  |
| --- | --- | --- | --- |
| a. | Total assets | = | $99,500 ($90,550 + $3,800+ $450 + $4,700) |
|  |  |  |  |
| b. | Total liabilities | = | $2,700 |
|  |  |  |  |
| c. | Total stockholder’s equity | = | $96,800 ($95,000 + $3,800 - $1,500 - $500) |
|  |  |  |  |
| d. | Net income for June | = | $2,300 ($3,800 − $1,500) |

**(25-30 min.) P 1-32A**

***Req. 1***

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | | | | = | **Liabilities** | + | **Stockholders’ Equity** | | | | | | |
|  | **Cash** | + | **Accounts receivable** | + | **Supplies** | + | **Equipment** |  | **Accounts payable** |  | **Common stock** | **+** | **Retained Earnings** | | | | |
| **Apr.** |  |  |  |  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | **Salaries expense** | **–** | **Dividends** |
|  |  |
| **Beg. bal.** | $1,380 | + | $3,820 | + | $0 | + | $28,000 | = | $4,500 | + | $24,000 | + | $6,700 | **–** | $2,000 | **–** | $0 |
| **a.** | + 8,000 |  |  |  |  |  |  |  |  |  | + 8,000 |  |  |  |  |  |  |
| **Bal.** | $9,380 | + | $3,820 | + | $0 | + | $28,000 | = | $4,500 | + | $32,000 | + | $6,700 | **–** | $2,000 | **–** | $0 |
| **b.** | -4,500 |  |  |  |  |  |  |  | -4,500 |  |  |  |  |  |  |  |  |
| **Bal.** | $4,880 | + | $3,820 | + | $0 | + | $28,000 | = | $0 | + | $32,000 | + | $6,700 | **–** | $2,000 | **–** | $0 |
| **c.** | + 3,500 |  |  |  |  |  |  |  |  |  |  |  | + 3,500 |  |  |  |  |
| **Bal.** | $8,380 | + | $3,820 | + | $0 | + | $28,000 | = | $0 | + | $32,000 | + | $10,200 | **–** | $2,000 | **–** | $0 |
| **d.** | + 400 |  | - 400 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Bal.** | $8,780 | + | $3,420 | + | $0 | + | $28,000 | = | $0 | + | $32,000 | + | $10,200 | **–** | $2,000 | **–** | $0 |
| **e.** |  |  |  |  | + 1,300 |  |  |  | + 1,300 |  |  |  |  |  |  |  |  |
| **Bal.** | $8,780 | + | $3,420 | + | $1,300 | + | $28,000 | = | $1,300 | + | $32,000 | + | $10,200 | **–** | $2,000 | **–** | $0 |
| **f.** |  |  | + 5,500 |  |  |  |  |  |  |  |  |  | + 5,500 |  |  |  |  |
| **Bal.** | $8,780 | + | $8,920 | + | $1,300 | + | $28,000 | = | $1,300 | + | $32,000 | + | $15,700 | **–** | $2,000 | **–** | $0 |
| **g.** | +10,000 |  |  |  |  |  |  |  |  |  | + 10,000 |  |  |  |  |  |  |
| **Bal.** | $18,780 | + | $8,920 | + | $1,300 | + | $28,000 | = | $1,300 | + | $42,000 | + | $15,700 | **–** | $2,000 | **–** | $0 |
| **h.** | - 2,500 |  |  |  |  |  |  |  |  |  |  |  |  |  | + 2,500 |  |  |
| **Bal.** | $16,280 | + | $8,920 | + | $1,300 | + | $28,000 | = | $1,300 | + | $42,000 | + | $15,700 | **–** | $4,500 | **–** | $0 |
| **i.** | +175 |  |  |  | - 175 |  |  |  |  |  |  |  |  |  |  |  |  |
| **Bal.** | $16,455 | + | $8,920 | + | $1,125 | + | $28,000 | = | $1,300 | + | $42,000 | + | $15,700 | **–** | $4,500 | **–** | $0 |
| **j.** | -800 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | +800 |
| **Bal.** | $15,655 | + | $8,920 | + | $1,125 | + | $28,000 | = | $1,300 | + | $42,000 | + | $15,700 | **–** | $4,500 | **–** | $800 |

**(25-30 min.) P 1-32A (cont.)**

***Req. 2***

|  |  |  |
| --- | --- | --- |
| **Interiors by Design Inc.** | | |
| **Income Statement** | | |
| **Month Ended April 30, 2016** | | |
| Revenues |  |  |
| Service revenue |  | $15,700 |
| Expenses |  |  |
| Salaries expense |  | 4,500 |
| Net income |  | $11,200 |

***Req. 3***

|  |  |
| --- | --- |
| **Interiors by Design, Inc.**  **Statement of Retained Earnings**  **Month Ended April 30, 2016** | |
| Retained earnings, April 1, 2016 | $0 |
| Add: Net income | 11,200 |
| Subtotal | 11,200 |
| Less: Dividends | 800 |
| Retained earnings, April 30, 2016 | $10,400 |

***Req.4***

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Interiors by Design, Inc.** | | | | |
| **Balance Sheet** | | | | |
| **April 30, 2016** | | | | |
| ASSETS | | LIABILITIES | | |
| Cash | $ 15,655 | Accounts payable | $ 1,300 | |
| Accounts receivable | 8,920 |  |  | |
| Supplies | 1,125 | STOCKHOLDERS’ EQUITY | | |
| Equipment | 28,000 | Common stock | | 42,000 |
|  |  | Retained earnings | | 10,400 |
|  |  | Total Stockholders’ equity | | 52,400 |
|  |  |  | |  |
|  |  |  | |  |
|  |  | Total liabilities and | |  |
| Total assets | $53,700 | stockholder’s equity | | $53,700 |

**(20-25 min.) P 1-33A**

***Req. 1***

|  |  |  |  |
| --- | --- | --- | --- |
| **Account** | **Type of Account** | **Account** | **Type of Account** |
| Accounts Receivable | Asset | Cash | Asset |
| Note Payable | Liability | Accounts Payable | Liability |
| Retained Earnings | Stockholders’ equity | Advertising Expense | Stockholders’ equity |
| Salaries Expense | Stockholders’ equity | Service Revenue | Stockholders’ equity |
| Equipment | Asset | Common Stock | Stockholders’ equity |
| Insurance Expense | Stockholders’ equity | Rent Expense | Stockholders’ equity |
| Utilities Expense | Stockholders’ equity | Supplies | Asset |

***Req. 2***

**a.**

|  |  |  |
| --- | --- | --- |
| **Gear Heads, Inc.** | | |
| **Income Statement** | | |
| **Year Ended December 31, 2016** | | |
| Service revenue |  | $92,800 |
| Expenses |  |  |
| Salaries expense | $16,600 |  |
| Rent Expense | 4,800 |  |
| Advertising expense | 3,700 |  |
| Insurance expense | 3,200 |  |
| Utilities expense | 2,300 |  |
| Total expenses |  | 30,600 |
| Net Income |  | $62,200 |

**b.**

|  |  |
| --- | --- |
| **Gear Heads, Inc.**  **Statement of Retained Earnings**  **Year Ended December 31, 2016** | |
| Retained earnings, December 31, 2015 | $19,700 |
| Add: Net income | 62,200 |
| Subtotal | 81,900 |
| Less: Dividends | 45,000 |
| Retained earnings, December 31, 2016 | $36,900 |

**c.**

|  |  |  |  |
| --- | --- | --- | --- |
| **Gear Heads, Inc.** | | | |
| **Balance Sheet** | | | |
| **December 31, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $14,700 | Accounts payable | $ 6,500 |
| Accounts receivable | 9,300 | Notes payable | 17,000 |
| Supplies | 1,400 | Total liabilities | 23,500 |
| Equipment | 68,000 |  |  |
|  |  | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 33,000 |
|  |  | Retained earnings | 36,900 |
|  |  | Total stockholders’ equity | 69,900 |
|  |  | Total liabilities and |  |
| Total assets | $93,400 | stockholders’ equity | $93,400 |

**(25-30 min.) P 1-34A**

***Req. 1***

|  |  |  |  |
| --- | --- | --- | --- |
| **Account** | **Type of Account** | **Account** | **Type of Account** |
| Accounts payable | Liability | Interest expense | Stockholders’ equity |
| Accounts receivable | Asset | Land | Asset |
| Advertising expense | Stockholders’ equity | Note payable | Liability |
| Building | Asset | Property tax expense | Stockholders’ equity |
| Cash | Asset | Rent expense | Stockholders’ equity |
| Common stock | Stockholders’ equity | Salaries expense | Stockholders’ equity |
| Dividends | Stockholders’ equity | Salaries payable | Liability |
| Equipment | Asset | Service revenue | Stockholders’ equity |
| Insurance expense | Stockholders’ equity | Supplies | Asset |

***Req. 2***

|  |  |  |
| --- | --- | --- |
| **Extreme Sports, Inc.** | | |
| **Income Statement** | | |
| **Year Ended October 31, 2016** | | |
| Service revenue |  | $190,000 |
| Expenses |  |  |
| Salaries expense | $61,000 |  |
| Rent expense | 22,000 |  |
| Advertising expense | 19,000 |  |
| Interest expense | 5,500 |  |
| Property tax expense | 4,300 |  |
| Insurance expense | 2,800 |  |
| Total expenses |  | 114,600 |
| Net Income |  | $ 75,400 |

|  |  |
| --- | --- |
| **Extreme Sports, Inc.**  **Statement of Retained Earnings**  **Year Ended October 31, 2016** | |
| Retained earnings, October 31, 2015 | $94,900 |
| Add: Net income | 75,400 |
| Subtotal | 170,300 |
| Less: Dividends | 36,000 |
| Retained earnings, October 31, 2016 | $134,300 |

**(continued) P 1-34A**

***Req. 3***

|  |  |  |  |
| --- | --- | --- | --- |
| **Extreme Sports, Inc.** | | | |
| **Balance Sheet** | | | |
| **October 31, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $18,000 | Accounts payable | $ 18,000 |
| Accounts receivable | 14,000 | Salaries payable | 6,000 |
| Supplies | 1,300 | Notes payable | 65,000 |
| Land | 35,000 | Total liabilities | 89,000 |
| Equipment | 50,000 |  |  |
| Building | 125,000 | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 20,000 |
|  |  | Retained earnings | 134,300 |
|  |  | Total stockholders’ equity | 154,300 |
|  |  | Total liabilities and |  |
| Total assets | $243,300 | stockholders’ equity | $243,300 |

***Req. 4***

1. $75,400 (Net profit = net income).
2. Increase of $39,400 ($75,400 Net income minus $36,000 Dividends).

c. $243,300 (Total economic resources = total assets).

d. $ 89,000 (Total owed = total liabilities).

**(20-25 min.) P 1-35A**

|  |  |  |  |
| --- | --- | --- | --- |
| **Valley Realty, Inc.** | | | |
| **Balance Sheet** | | | |
| **November 30, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $9,400 | Accounts payable | $ 1,800 |
| Accounts receivable | 3,200 | Salaries payable | 2,150 |
| Supplies | 440 | Notes payable | 5,300 |
| Equipment | 17,300 | Total liabilities | 9,250 |
|  |  |  |  |
|  |  | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 9,000 |
|  |  | Retained earnings | 12,090 |
|  |  | Total stockholders’ equity | 21,090 |
|  |  | Total liabilities and |  |
| Total assets | $30,340 | stockholders’ equity | $30,340 |

**(20-25 min.) P 1-36B**

***Req. 1***

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | | | | = | **Liabilities** | + | **Stockholders’ Equity** | | | | | | |
|  | **Cash** | + | **Accounts receivable** | + | **Supplies** | + | **Office furniture** |  | **Accounts payable** |  | **Common stock** | **+** | **Retained Earnings** | | | | |
| **Nov** |  |  |  |  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | **Rent expense** | **–** | **Dividends** |
|  |  |
| **3** | \* |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **5** | + 55,000 |  |  |  |  |  |  |  |  |  | + 55,000 |  |  |  |  |  |  |
| **Bal.** | $55,000 | + | $0 | + | $0 | + | $0 | = | $0 | + | $55,000 | + | $0 | **–** | $0 | **–** | $0 |
| **7** | -450 |  |  |  | + 450 |  |  |  |  |  |  |  |  |  |  |  |  |
| **Bal.** | $54,550 | + | $0 | + | $450 | + | $0 | = | $0 | + | $55,000 | + | $0 | **–** | $0 | **–** | $0 |
| **9** |  |  |  |  |  |  | +3,800 |  | +3,800 |  |  |  |  |  |  |  |  |
| **Bal.** | $54,550 | + | $0 | + | $450 | + | $3,800 | = | $3,800 | + | $55,000 | + | $0 | **–** | $0 | **–** | $0 |
| **10** | \* |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **14** | \*\* |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **20** |  |  | +4,000 |  |  |  |  |  |  |  |  |  | +4,000 |  |  |  |  |
| **Bal.** | $54,550 | + | $4,000 | + | $450 | + | $3,800 | = | $3,800 | + | $55,000 | + | $4,000 | **–** | $0 | **–** | $0 |
| **27** | -1,400 |  |  |  |  |  |  |  |  |  |  |  |  |  | +1,400 |  |  |
| **Bal.** | $53,150 | + | $4,000 | + | $450 | + | $3,800 | = | $3,800 | + | $55,000 | + | $4,000 | **–** | $1,400 | **–** | $0 |
| **29** | -2,500 |  |  |  |  |  |  |  | - 2,500 |  |  |  |  |  |  |  |  |
| **Bal.** | $50,650 | + | $4,000 | + | $450 | + | $3,800 | = | $1,300 | + | $55,000 | + | $4,000 | **–** | $1,400 | **–** | $0 |
| **30** | -800 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | + 800 |
| **Bal.** | $49,850 | + | $4,000 | + | $450 | + | $3,800 | = | $1,300 | + | $55,000 | + | $4,000 | **–** | $1,400 | **–** | $800 |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| \* Represents a personal, not a business transaction | | | | | | |  |  |  |  |  |  |  |  |  |  |  |
| \*\* Not a transaction as there was no financial impact | | | | | | |  |  |  |  |  |  |  |  |  |  |  |

***Req. 2***

|  |  |  |  |
| --- | --- | --- | --- |
| a. | Total assets | = | $58,100 ($49,850+ $4,000 + $450 + $3,800) |
|  |  |  |  |
| b. | Total liabilities | = | $1,300 |
|  |  |  |  |
| c. | Total stockholder’s equity | = | $56,800($55,000 + $4,000 - $1,400 - $800) |
|  |  |  |  |
| d. | Net income for November | = | $2,600 ($4,000 − $1,400) |

**(25-30 min.) P 1-37B**

***Req. 1***

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | | | | = | **Liabilities** | + | **Stockholders’ Equity** | | | | |  |  |
|  | **Cash** | + | **Accounts receivable** | + | **Supplies** | + | **Equipment** |  | **Accounts payable** |  | **Common stock** | **+** | **Retained Earnings** | | |  |  |
| **June** |  |  |  |  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | **Salaries expense** | **–** | **Dividends** |
|  |  |
| **Beg. bal.** | $1,610 | + | $3,070 | + | $0 | + | $25,000 | = | $4,500 | + | $20,000 | + | $6,700 | **–** | $1,520 | **–** | $0 |
| **a.** | +16,000 |  |  |  |  |  |  |  |  |  | + 16,000 |  |  |  |  |  |  |
| **Bal.** | $17,610 | + | $3,070 | + | $0 | + | $25,000 | = | $4,500 | + | $36,000 | + | $6,700 | **–** | $1,520 | **–** | $0 |
| **b.** | -4,500 |  |  |  |  |  |  |  | -4,500 |  |  |  |  |  |  |  |  |
| **Bal.** | $13,110 | + | $3,070 | + | $0 | + | $25,000 | = | $0 | + | $36,000 | + | $6,700 | **–** | $1,520 | **–** | $0 |
| **c.** | + 5,000 |  |  |  |  |  |  |  |  |  |  |  | + 5,000 |  |  |  |  |
| **Bal.** | $18,110 | + | $3,070 | + | $0 | + | $25,000 | = | $0 | + | $36,000 | + | $11,700 | **–** | $1,520 | **–** | $0 |
| **d.** | +1,150 |  | - 1,150 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Bal.** | $19,260 | + | $1,920 | + | $0 | + | $25,000 | = | $0 | + | $36,000 | + | $11,700 | **–** | $1,520 | **–** | $0 |
| **e.** |  |  |  |  | +800 |  |  |  | + 800 |  |  |  |  |  |  |  |  |
| **Bal.** | $19,260 | + | $1,920 | + | $800 | + | $25,000 | = | $800 | + | $36,000 | + | $11,700 | **–** | $1,520 | **–** | $0 |
| **f.** |  |  | 4,500 |  |  |  |  |  |  |  |  |  | + 4,500 |  |  |  |  |
| **Bal.** | $19,260 | + | $6,420 | + | $800 | + | $25,000 | = | $800 | + | $36,000 | + | $16,200 | **–** | $1,520 | **–** | $0 |
| **g.** | +9,000 |  |  |  |  |  |  |  |  |  | +9,000 |  |  |  |  |  |  |
| **Bal.** | $28,260 | + | $6,420 | + | $800 | + | $25,000 | = | $800 | + | $45,000 | + | $16,200 | **–** | $1,520 | **–** | $0 |
| **h.** | - 2,200 |  |  |  |  |  |  |  |  |  |  |  |  |  | + 2,200 |  |  |
| **Bal.** | $26,060 | + | $6,420 | + | $800 | + | $25,000 | = | $800 | + | $45,000 | + | $16,200 | **–** | $3,720 | **–** | $0 |
| **i.** | +250 |  |  |  | - 250 |  |  |  |  |  |  |  |  |  |  |  |  |
| **Bal.** | $26,310 | + | $6,420 | + | $550 | + | $25,000 | = | $800 | + | $45,000 | + | $16,200 | **–** | $3,720 | **–** | $0 |
| **j.** | -1,000 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | +1,000 |
| **Bal.** | $25,310 | + | $6,420 | + | $550 | + | $25,000 | = | $800 | + | $45,000 | + | $16,200 | **–** | $3,720 | **–** | $1,000 |

**(25-30 min.) P 1-37B (cont.)**

***Req. 2***

|  |  |  |
| --- | --- | --- |
| **Interiors on Demand, Inc.** | | |
| **Income Statement** | | |
| **Month Ended June 30, 2016** | | |
| Revenues |  |  |
| Service revenue |  | $16,200 |
| Expenses |  |  |
| Salaries expense |  | 3,720 |
| Net income |  | $12,480 |

***Req. 3***

|  |  |
| --- | --- |
| **Interiors on Demand, Inc.**  **Statement of Retained Earnings**  **Month Ended June 30, 2016** | |
| Retained earnings, June 1, 2016 | $0 |
| Add: Net income | 12,480 |
| Subtotal | 12,480 |
| Less: Dividends | 1,000 |
| Retained earnings, June 30, 2016 | $11,480 |

***Req.4***

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Interiors on Demand, Inc.** | | | | |
| **Balance Sheet** | | | | |
| **June 30, 2016** | | | | |
| ASSETS | | LIABILITIES | | |
| Cash | $ 25,310 | Accounts payable | $ 800 | |
| Accounts receivable | 6,420 |  |  | |
| Supplies | 550 | STOCKHOLDERS’ EQUITY | | |
| Equipment | 25,000 | Common stock | | 45,000 |
|  |  | Retained earnings | | 11,480 |
|  |  | Total Stockholders’ equity | | 56,480 |
|  |  |  | |  |
|  |  |  | |  |
|  |  | Total liabilities and | |  |
| Total assets | $57,280 | stockholder’s equity | | $57,280 |

**(20-25 min.) P 1-38B**

***Req. 1***

|  |  |  |  |
| --- | --- | --- | --- |
| **Account** | **Type of Account** | **Account** | **Type of Account** |
| Accounts Receivable | Asset | Cash | Asset |
| Note Payable | Liability | Accounts Payable | Liability |
| Retained Earnings | Stockholders’ equity | Advertising Expense | Stockholders’ equity |
| Salaries Expense | Stockholders’ equity | Service Revenue | Stockholders’ equity |
| Equipment | Asset | Common Stock | Stockholders’ equity |
| Insurance Expense | Stockholders’ equity | Rent Expense | Stockholders’ equity |
| Utilities Expense | Stockholders’ equity | Supplies | Asset |

***Req. 2***

**a.**

|  |  |  |
| --- | --- | --- |
| **Classic Cars, Inc.** | | |
| **Income Statement** | | |
| **Year Ended December 31, 2016** | | |
| Service Revenue |  | $68,900 |
| Expenses |  |  |
| Salaries Expense | $22,600 |  |
| Rent Expense | 7,700 |  |
| Advertising Expense | 3,100 |  |
| Insurance Expense | 2,800 |  |
| Utilities Expense | 1,400 |  |
| Total expenses |  | 37,600 |
| Net Income |  | $31,300 |

**b.**

|  |  |
| --- | --- |
| **Classic Cars, Inc.**  **Statement of Retained Earnings**  **Year Ended December 31, 2016** | |
| Retained earnings, December 31, 2015 | $22,300 |
| Add: Net income | 31,300 |
| Subtotal | 53,600 |
| Less: Dividends | 20,000 |
| Retained earnings, December 31, 2016 | $33,600 |

**(25-30 min.) P 1-38B (cont.)**

**c.**

|  |  |  |  |
| --- | --- | --- | --- |
| **Classic Cars, Inc.** | | | |
| **Balance Sheet** | | | |
| **December 31, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $12,300 | Accounts payable | $ 6,150 |
| Accounts receivable | 11,600 | Note payable | 18,000 |
| Supplies | 850 | Total liabilities | 24,150 |
| Equipment | 65,000 |  |  |
|  |  | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 32,000 |
|  |  | Retained earnings | 33,600 |
|  |  | Total stockholders’ equity | 65,600 |
|  |  | Total liabilities and |  |
| Total assets | $89,750 | stockholders’ equity | $89,750 |

**(25-30 min.) P 1-39B**

***Req. 1***

|  |  |  |  |
| --- | --- | --- | --- |
| **Account** | **Type of Account** | **Account** | **Type of Account** |
| Accounts payable | Liability | Interest expense | Stockholders’ equity |
| Accounts receivable | Asset | Land | Asset |
| Advertising expense | Stockholders’ equity | Note payable | Liability |
| Building | Asset | Property tax expense | Stockholders’ equity |
| Cash | Asset | Rent expense | Stockholders’ equity |
| Common stock | Stockholders’ equity | Salaries expense | Stockholders’ equity |
| Dividends | Stockholders’ equity | Salaries payable | Liability |
| Equipment | Asset | Service revenue | Stockholders’ equity |
| Insurance expense | Stockholders’ equity | Supplies | Asset |

***Req. 2***

|  |  |  |
| --- | --- | --- |
| **The Fitness Guru, Inc.** | | |
| **Income Statement** | | |
| **Year Ended August 31, 2016** | | |
| Service revenue |  | $166,000 |
| Expenses |  |  |
| Salaries expense | $92,000 |  |
| Rent expense | 22,000 |  |
| Advertising expense | 15,000 |  |
| Interest expense | 5,000 |  |
| Property tax expense | 4,500 |  |
| Insurance expense | 2,200 |  |
| Total expenses |  | 140,700 |
| Net Income |  | $ 25,300 |

|  |  |
| --- | --- |
| **The Fitness Guru, Inc.**  **Statement of Retained Earnings**  **Year Ended August 31, 2016** | |
| Retained earnings, August 31, 2015 | $87,100 |
| Add: Net income | 25,300 |
| Subtotal | 112,400 |
| Less: Dividends | 29,000 |
| Retained earnings, August 31, 2016 | $83,400 |

**(continued) P 1-39B**

***Req. 3***

|  |  |  |  |
| --- | --- | --- | --- |
| **The Fitness Guru, Inc.** | | | |
| **Balance Sheet** | | | |
| **August 31, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $16,000 | Accounts payable | $ 15,000 |
| Accounts receivable | 14,000 | Salaries payable | 5,000 |
| Supplies | 1,400 | Note payable | 70,000 |
| Land | 37,000 | Total liabilities | 90,000 |
| Equipment | 40,000 |  |  |
| Building | 135,000 | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 70,000 |
|  |  | Retained earnings | 83,400 |
|  |  | Total stockholders’ equity | 153,400 |
|  |  | Total liabilities and |  |
| Total assets | $243,400 | stockholders’ equity | $243,400 |

***Req. 4***

a. $25,300 (Net profit = net income).

b. Decrease of $3,700 ($25,300 Net income minus $29,000 Dividends).

c. $243,400 (Total economic resources = total assets).

d. $ 90,000 (Total owed = total liabilities).

**(20-25 min.) P 1-40B**

|  |  |  |  |
| --- | --- | --- | --- |
| **Highland Realty, Inc.** | | | |
| **Balance Sheet** | | | |
| **September 30, 2016** | | | |
| ASSETS | | LIABILITIES | |
| Cash | $9,000 | Accounts payable | $ 2,000 |
| Accounts receivable | 1,400 | Salaries payable | 1,100 |
| Supplies | 600 | Notes payable | 5,700 |
| Equipment | 8,300 | Total liabilities | 8,800 |
|  |  |  |  |
|  |  | STOCKHOLDERS’ EQUITY | |
|  |  | Common stock | 9,000 |
|  |  | Retained earnings | 1,500 |
|  |  | Total stockholders’ equity | 10,500 |
|  |  | Total liabilities and |  |
| Total assets | $19,300 | stockholders’ equity | $19,300 |

## Continuing Exercise

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **<BOX NUM="5" ID="BX10.01.005" TY="BX10"><UNTBL><COLHD>** | **Assets** | | | | |  |  | **=** | **Liabilities** | **+** | **Stockholders’ Equity** | | | | |
| <COLH2> | Cash | + | Accounts receivable | + | Supplies | + | Equipment | = | Accounts payable | + | Common stock | + | Retained Earnings | | |
| May |  |  |  |  |  |  |  |  |  |  |  |  | Service revenue | – | Utilities  expense |
| 1 | +1,500 |  |  |  |  |  |  |  |  |  | +1,500 |  |  |  |  |
| 3 |  |  |  |  |  |  | +1,908 |  | +1,908 |  |  |  |  |  |  |
| 5 | -125 |  |  |  | +125 |  |  |  |  |  |  |  |  |  |  |
| 6 |  |  | +375 |  |  |  |  |  |  |  |  |  | +375 |  |  |
| 17 | +275 |  |  |  |  |  |  |  |  |  |  |  | +275 |  |  |
| 28 | -65 |  |  |  |  |  |  |  |  |  |  |  |  |  | +65 |
| 30 | +150 |  | -150 |  |  |  |  |  |  |  |  |  |  |  |  |
| Bal | 1,735 | + | 225 | + | 125 | + | 1,908 | = | 1,908 | + | 1,500 | + | 650 | - | 65 |

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Assets** | | | | |  |  |  |  | = | **Liabilities** | | | + | **Stockholders’ Equity** | | | | | | | | |
|  | **Cash** | + | **Accounts receivable** | + | **Supplies** | + | **Equipment** | + | **Vehicles** |  | **Accounts payable** | + | **Note payable** |  | **Common stock** | **+** | **Retained Earnings** | | | | | | |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | **Service revenue** | **–** | **Salaries**  **expense** |  | **Utilities expense** | - | **Dividends** |
| **-** |
| 3/1 | +22,000 |  |  |  |  |  |  |  | +13,000 |  |  |  |  |  | +35,000 |  |  |  |  |  |  |  |  |
| 3/3 | -3,600 |  |  |  |  |  | +3,600 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| 3/7 |  |  |  |  | +900 |  |  |  |  |  | +900 |  |  |  |  |  |  |  |  |  |  |  |  |
| 3/12 | +850 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | +850 |  |  |  |  |  |  |
| 3/15 | -620 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | +620 |  |  |  |  |
| 3/16 | +13,000 |  |  |  |  |  |  |  | -13,000 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| 3/18 |  |  |  |  |  |  |  |  | +35,800 |  |  |  | +35,800 |  |  |  |  |  |  |  |  |  |  |
| 3/21 |  |  | +3,200 |  |  |  |  |  |  |  |  |  |  |  |  |  | +3,200 |  |  |  |  |  |  |
| 3/27 | -150 |  |  |  |  |  |  |  |  |  | -150 |  |  |  |  |  |  |  |  |  |  |  |  |
| 3/30 | +1,900 |  | -1,900 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| 3/31 |  |  |  |  |  |  |  |  |  |  | +250 |  |  |  |  |  |  |  |  |  | +250 |  |  |
| 3/31 | -1,500 |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  | +1,500 |
| Bal | 31,880 | + | 1,300 | + | 900 | + | 3,600 | + | 35,800 | = | 1,000 | + | 35,800 | + | 35,000 | + | 4,050 | - | 620 | - | 250 | - | 1,500 |

## Continuing Problem

***Req 1***

**Continuing Problem (cont.)**

**Req 2**

**Fitness Equipment Doctor, Inc.  
 Income Statement**

**Month Ended March 31, 2016**

|  |  |  |
| --- | --- | --- |
| Service revenue  Expenses:  Salaries expense  Utilities expense  Total expenses  Net Income | $620  250 | $4,050  870  $3,180 |

***Req 3***

**Fitness Equipment Doctor, Inc.  
Statement of Retained Earnings**

**For the Month Ended March 31, 2016**

|  |  |
| --- | --- |
| Retained Earnings, March 1, 2016  Add: Net Income for the Month  Subtotal  Less: Dividends  Retained Earnings, March 31, 2016 | $0  3,180  3,180  1,500  $1,680 |

***Req 4***

**Fitness Equipment Doctor, Inc.  
 Balance Sheet**

**March 31, 2016**

|  |  |  |  |
| --- | --- | --- | --- |
| ASSETS |  | LIABILITIES |  |
| Cash  Accounts receivable  Supplies  Equipment  Vehicles  Total Assets | $31,880  1,300  900  3,600  35,800        $73,480 | Accounts payable  Note Payable  Total Liabilities    STOCKHOLDERS’ EQUITY  Common Stock  Retained Earnings  Total Stockholders’ Equity  Total Liabilities and Stockholders’ Equity | $1,000  35,800  $36,800  $35,000  1,680  36,680  $73,480 |

***Req 5***

It is unknown how much Adam was earning at his previous job and, after only one month of operations, it is probably too early to tell. However, Fitness Equipment Doctor, Inc. made almost $3,200 of profit for its very first month of operations. So, it appears that Adam probably made a good decision.

## Continuing Financial Statement Analysis Problem

1.

“Our mission is to be recognized by our customers as the #1 sports and fitness specialty omni-channel retailer that serves and inspires athletes and outdoor enthusiasts to achieve their personal best through the relentless improvement of everything we do.

2.

Dick’s is an upscale, retail merchandiser of quality sporting and fitness products. Dicks operates four types of retail stores. The four types are:

• Dick’s Sporting Goods

• Gold Galaxy

• Field and Stream

• True Runner

3.

Dick’s sells a wide assortment of sporting and fitness merchandise. The products Dick’s sells are purchased from manufacturers. Many of these manufacturers produce national brand merchandise such as Nike, Under Armor, and others. However Dick’s also sells private brands that are exclusive to Dick’s. This private-brand merchandise is purchased from manufacturers under exclusive agreements.

4.

Dicks’ customers are sports and fitness enthusiasts of all ages.

5.

Answers will vary. Students will talk about what they like and dislike about Dick’s. The focus should be whether they are providing value to its stakeholders, including customers, employees, suppliers, society, lenders, and especially owners. Students should think about earning profits, but also acknowledge the importance of when the profits are earned (time) and the risk associated with profits. With this, the importance of accounting can be stressed (i.e., recognizing, measuring, recording, and reporting financial information).

## Ethics in Action

**Case #1**

* What Lisa proposed is not unethical as long as the assets contributed can legitimately be used in the business and the stockholders’ equity accounts properly reflect the contribution. The business entity principle recognizes the difference between the personal assets of the owners and the assets owned by the business. When assets are contributed to the business by the owners, proper accounting will reflect the transaction. Should a business need additional assets, there is nothing wrong or improper for an owner to contribute additional assets that can be used in the business.
* What Mike proposed is unethical. His plan would provide information that would not be reliable as the “sales” would be nothing more than disguised owner distributions. Inflating the income statement by including fictitious sales is unethical, misleading and not allowable. Mike should not provide false information that is unreliable.

There is nothing unethical about a business wanting to improve its Balance Sheet by properly adding more business assets. It would be unacceptable, however, for a business to temporarily add more assets just to improve the Balance Sheet in order to obtain a loan and remove those assets once the loan is granted.

**Case #2**

* The Balance Sheet should follow Generally Accepted Accounting Principles, and thus the assets should be listed at the total cost of $2,100,000. This would also provide for more reliable data as well.
* Only one Balance Sheet can be provided, and it needs to comply with Generally Accepted Accounting Principles. Adding supplemental footnote disclosures would be acceptable. However, providing another Balance Sheet not following generally accepted accounting principles would be misleading and confusing and therefore unacceptable.

## Financial Analysis

1. No solution.

2. The total assets were $1,792,209,000 as of December 31, 2014. This was an increase from the $1,605,588,000 as of December 31, 2013.

3. No solution.

5. Total revenues in 2014 were $2,100,590,000. This is an increase from the $1,684,996,000 in 2013 which was an increase from $1,669,563,000 in 2012.

## Industry Analysis

Columbia Sportswear’s stockholders have a claim to 75.6% ($1,355,234/$1,792,209) of company assets compared to only 64.5% ($1,350,300/$2,095,083) for Under Armour’s Stockholders. (Numbers in thousands.)

## Small Business Analysis

The CPA tells you, “The income statement is not the only financial statement that will affect your cash balance. The income statement only gives you the results of your operations. If all you did during the year was to collect revenue and pay out expenses, then the net income would directly correspond to the increase in your cash balance. But there are other aspects of BCS Consultants as well. There’s the financing aspect, borrowing money and paying money back, as well as the investment aspect, buying and disposing of fixed assets. These will also affect your cash balance. In addition, the payment of dividends decreases the cash balance.

“You purchased a piece of equipment during the year for $12,000 and paid cash for it. That decreased your cash by $12,000. You paid down your Note at the bank from $75,000 to $58,000 during the year. That used $17,000 in cash. And you paid yourself a dividend of $15,000. None of these three items will appear on the income statement because they are not revenues or expenses, but each of them affects cash.”

So here’s the recap of what happened to cash for the year:

Cash balance, Dec. 31, 2015 $38,000

Increase for net income 2016 36,000

Decrease for equipment purchased (12,000)

Decrease for Note payment (17,000)

Decrease for Dividends paid 2016 (15,000)

Cash Balance, Dec. 31, 2016 $30,000 - a decrease of $8,000

## Written Communication

In your e-mail back to this potential new client, you would want to list the four basic types of business organizations available to most small businesses today. These were outlined in your chapter, and they are sole proprietor, partnership, corporation and limited liability company. Of course, you would want to elaborate on the tax advantages and disadvantages of each of these types of organizations (that discussion is beyond the scope of our text) as well as talk briefly about the legal aspects of each of them. But remember, we are not attorneys. Leave the high-level discussions about legal liability to them.

However, because we are accountants, we can certainly tell this potential new client about the benefits of having an accountant as part of the team of professionals that is necessary to help achieve success in today’s business climate. Accountants “keep score”. They help ensure that the business is running profitably. They help to determine what the true cost is for one unit of the product that you are selling. They prepare financial statements for the stakeholders of the business. They speak the language of business.