



TEXTBOOK TESTBANKS

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# CHAPTER 1

## INTRODUCTION TO ACCOUNTING AND BUSINESS

### DISCUSSION QUESTIONS

1. Some users of accounting information include managers, employees, investors, creditors, customers, and the government.
2. The role of accounting is to provide information for managers to use in operating the business. In addition, accounting provides information to others to use in assessing the economic performance and condition of the business.
3. The corporate form allows the company to obtain large amounts of resources by issuing stock. For this reason, most companies that require large investments in property, plant, and equipment are organized as corporations.
4. No. The business entity assumption limits the recording of economic data to transactions directly affecting the activities of the business. The payment of the interest of \$4,500 is a personal transaction of Josh Reilly and should not be recorded by Dispatch Delivery Service.
5. The land should be recorded at its cost of \$167,500 to Reliable Repair Service. This is consistent with the cost principle.
6.
  - a. No. The offer of \$2,000,000 and the increase in the assessed value should not be recognized in the accounting records.
  - b. Cash would increase by \$2,125,000, land would decrease by \$900,000, and stockholders' equity would increase by \$1,225,000.
7. An account receivable is a claim against a customer for goods or services sold. An account payable is an amount owed to a creditor for goods or services purchased. Therefore, an account receivable in the records of the seller is an account payable in the records of the purchaser.
8. (b) The business realized net income of \$91,000 (\$679,000 – \$588,000).
9. (a) The business incurred a net loss of \$75,000 (\$640,000 – \$715,000).
10.
  - (a) Net income or net loss
  - (b) Common stock and retained earnings at the end of the period
  - (c) Cash at the end of the period

## BASIC EXERCISES

### BE 1–1

**\$190,000.** Under the cost principle, the land should be recorded at the cost to Upstate Metal Roofing.

### BE 1–2

a.

$$\begin{aligned} A &= L + SE \\ \$710,000 &= \$195,000 + SE \\ SE &= \$515,000 \end{aligned}$$

b.

$$\begin{aligned} A &= L + SE \\ \$710,000 + \$125,000 &= \$195,000 + \$25,000 + SE \\ \$835,000 &= \$220,000 + SE \\ SE &= \$615,000 \end{aligned}$$

### BE 1–3

- (2) Expense (Advertising Expense) increases by \$8,500;  
Asset (Cash) decreases by \$8,500.
- (3) Asset (Supplies) increases by \$3,200;  
Liability (Accounts Payable) increases by \$3,200.
- (4) Asset (Accounts Receivable) increases by \$31,750;  
Revenue (Delivery Service Fees) increases by \$31,750.
- (5) Asset (Cash) increases by \$27,700;  
Asset (Accounts Receivable) decreases by \$27,700.

### BE 1–4

| Worldwide Travel<br>Income Statement<br>For the Year Ended July 31, 20Y6 |           |              |
|--------------------------------------------------------------------------|-----------|--------------|
| Fees earned                                                              |           | \$ 1,175,000 |
| Expenses:                                                                |           |              |
| Salary and wages expense                                                 | \$776,000 |              |
| Office expense                                                           | 175,000   |              |
| Miscellaneous expense                                                    | 80,000    |              |
| Total expenses                                                           |           | (1,031,000)  |
| Net income                                                               |           | \$ 144,000   |

## BE 1–5

| Worldwide Travel<br>Statement of Stockholders' Equity<br>For the Year Ended July 31, 20Y6 |                 |                      |           |
|-------------------------------------------------------------------------------------------|-----------------|----------------------|-----------|
|                                                                                           | Common<br>Stock | Retained<br>Earnings | Total     |
| Balances, August 1, 20Y5                                                                  | \$120,000       | \$550,000            | \$670,000 |
| Issued common stock                                                                       | 60,000          |                      | 60,000    |
| Net income for the year                                                                   |                 | 144,000              | 144,000   |
| Dividends                                                                                 |                 | (35,000)             | (35,000)  |
| Balances, July 31, 20Y6                                                                   | \$180,000       | \$659,000            | \$839,000 |
|                                                                                           |                 |                      |           |

## BE 1–6

| Worldwide Travel<br>Balance Sheet<br>July 31, 20Y6 |           |           |
|----------------------------------------------------|-----------|-----------|
| Assets                                             |           |           |
| Cash                                               |           | \$143,450 |
| Accounts receivable                                |           | 42,750    |
| Supplies                                           |           | 3,800     |
| Land                                               |           | 675,000   |
| Total assets                                       |           | \$865,000 |
| Liabilities                                        |           |           |
| Accounts payable                                   |           | \$ 26,000 |
| Stockholders' Equity                               |           |           |
| Common stock                                       | \$180,000 |           |
| Retained earnings                                  | 659,000   |           |
| Total stockholders' equity                         |           | 839,000   |
| Total liabilities and stockholders' equity         |           | \$865,000 |
|                                                    |           |           |

BE 1–7

| Worldwide Travel<br>Statement of Cash Flows<br>For the Year Ended July 31, 20Y6 |              |           |
|---------------------------------------------------------------------------------|--------------|-----------|
| Cash flows from (used for) operating activities:                                |              |           |
| Cash received from customers                                                    | \$ 1,225,000 |           |
| Cash paid for operating expenses                                                | (1,116,050)  |           |
| Net cash flows from operating activities                                        |              | \$108,950 |
| Cash flows from (used for) investing activities:                                |              |           |
| Cash paid for purchase of land                                                  |              | (50,000)  |
| Cash flows from (used for) financing activities:                                |              |           |
| Cash received from issuing common stock                                         | \$ 60,000    |           |
| Cash paid as dividends                                                          | (35,000)     |           |
| Net cash flows used for financing activities                                    |              | 25,000    |
| Net increase in cash                                                            |              | \$ 83,950 |
| Cash balance, August 1, 20Y5                                                    |              | 59,500    |
| Cash balance, July 31, 20Y6                                                     |              | \$143,450 |

BE 1–8

| a.                                                | Dec. 31,<br>20Y4 | Dec. 31,<br>20Y3 |
|---------------------------------------------------|------------------|------------------|
| Total liabilities.....                            | \$4,085,000      | \$2,880,000      |
| Total stockholders' equity.....                   | \$4,300,000      | \$3,600,000      |
| Ratio of liabilities to stockholders' equity..... | 0.95*            | 0.80**           |

\*  $\$4,085,000 \div \$4,300,000$

\*\*  $\$2,880,000 \div \$3,600,000$

b. Increased

**EXERCISES****Ex. 1–1**

- a.
- |                  |                   |                   |
|------------------|-------------------|-------------------|
| 1. manufacturing | 6. merchandising  | 11. service       |
| 2. manufacturing | 7. manufacturing  | 12. service       |
| 3. manufacturing | 8. service        | 13. manufacturing |
| 4. service       | 9. manufacturing  | 14. service       |
| 5. merchandising | 10. merchandising | 15. merchandising |
- b. The accounting equation is relevant to all companies. It serves as the basis of the accounting information system.

**Ex. 1–2**

As in many ethics issues, there is no one right answer. Oftentimes, disclosing only what is legally required may not be enough. In this case, it would be best for the company's chief executive officer to disclose both reports to the county representatives. In doing so, the chief executive officer could point out any flaws or deficiencies in the fired researcher's report.

**Ex. 1–3**

- a.
- |      |      |       |
|------|------|-------|
| 1. M | 5. O | 9. X  |
| 2. L | 6. O | 10. O |
| 3. O | 7. X |       |
| 4. M | 8. L |       |
- b. A business transaction is an economic event or condition that directly changes an entity's financial condition or results of operations.

**Ex. 1–4**

Kroger's stockholders' equity:  $\$49,086 - \$39,657 = \$9,429$

Procter & Gamble's stockholders' equity:  $\$117,208 - \$70,354 = \$46,854$

**Ex. 1–5**

Dollar Tree's stockholders' equity:  $\$21,722 - \$14,003 = \$7,719$

Target's stockholders' equity:  $\$53,811 - \$40,984 = \$12,827$

**Ex. 1–6**

- a. Aquadyne Designs: \$3,000,000 ( $\$1,000,000 + \$2,000,000$ )
- b. Morales & Associates: \$2,500,000 ( $\$6,000,000 - \$3,500,000$ )
- c. Omega Power Consultants: \$6,000,000 ( $\$10,000,000 - \$4,000,000$ )

**Ex. 1–7**

- a. \$1,270,000 ( $\$2,450,000 - \$1,180,000$ )
- b. \$1,580,000 ( $\$1,270,000 + \$825,000 - \$515,000$ )
- c. \$835,000 ( $\$1,270,000 - \$375,000 - \$60,000$ )
- d. \$2,115,000 ( $\$1,270,000 + \$725,000 + \$120,000$ )
- e. Net income: \$630,000 ( $\$3,300,000 - \$1,400,000 - \$1,270,000$ )

**Ex. 1–8**

- a. (2) liability
- b. (1) asset
- c. (3) stockholders' equity (revenue)
- d. (1) asset
- e. (3) stockholders' equity (expense)
- f. (3) stockholders' equity (expense)

**Ex. 1–9**

- a. Increases assets and increases stockholders' equity.
- b. Decreases assets and decreases stockholders' equity.
- c. Decreases assets and decreases stockholders' equity.
- d. Increases assets and increases liabilities.
- e. Increases assets and increases stockholders' equity.

**Ex. 1–10**

- a. (1) Total assets increased \$183,000 ( $\$298,000 - \$115,000$ ).  
(2) No change in liabilities.  
(3) Stockholders' equity increased \$183,000.
- b. (1) Total assets decreased \$80,000.  
(2) Total liabilities decreased \$80,000.  
(3) No change in stockholders' equity.
- c. No, it is false that a transaction always affects at least two elements (Assets, Liabilities, or Stockholders' Equity) of the accounting equation. Some transactions affect only one element of the accounting equation. For example, purchasing supplies for cash only affects assets.

**Ex. 1–11**

1. (a) increase
2. (a) increase
3. (b) decrease
4. (b) decrease

**Ex. 1–12**

- |      |       |
|------|-------|
| 1. c | 6. c  |
| 2. a | 7. d  |
| 3. e | 8. a  |
| 4. e | 9. e  |
| 5. c | 10. e |

**Ex. 1–13**

- a. (1) Provided catering services for cash, \$71,800.  
 (2) Purchase of land for cash, \$15,000.  
 (3) Payment of cash for expenses, \$47,500.  
 (4) Purchase of supplies on account, \$1,100.  
 (5) Paid cash dividends, \$5,000.  
 (6) Payment of cash to creditors, \$4,000.  
 (7) Recognition of cost of supplies used, \$1,500.
- b. \$300 ( $\$40,300 - \$40,000$ )
- c. \$17,800 ( $-\$5,000 + \$71,800 - \$49,000$ )
- d. \$22,800 ( $\$71,800 - \$49,000$ )
- e. \$17,800 ( $\$22,800 - \$5,000$ )

**Ex. 1–14**

**No.** It would be incorrect to say that the business had incurred a net loss of \$8,000. The excess of the dividends over the net income for the period is a decrease in the amount of stockholders' equity (retained earnings) in the business.

**Ex. 1–15**

| <b>Amber</b>                                                                   |                          |
|--------------------------------------------------------------------------------|--------------------------|
| Stockholders' equity at end of year (\$1,730,000 – \$1,150,000).....           | <b>\$ 580,000</b>        |
| Deduct stockholders' equity at beginning of year (\$1,220,000 – \$990,000).... | <b><u>(230,000)</u></b>  |
| Net income (increase in stockholders' equity).....                             | <b><u>\$ 350,000</u></b> |
| <b>Blue</b>                                                                    |                          |
| Increase in stockholders' equity (as determined for Amber).....                | <b>\$ 350,000</b>        |
| Add dividends.....                                                             | <b><u>60,000</u></b>     |
| Net income.....                                                                | <b><u>\$ 410,000</u></b> |
| <b>Coral</b>                                                                   |                          |
| Increase in stockholders' equity (as determined for Amber).....                | <b>\$ 350,000</b>        |
| Deduct additional issuance of common stock.....                                | <b><u>(140,000)</u></b>  |
| Net income.....                                                                | <b><u>\$ 210,000</u></b> |
| <b>Daffodil</b>                                                                |                          |
| Increase in stockholders' equity (as determined for Amber).....                | <b>\$ 350,000</b>        |
| Deduct additional issuance of common stock.....                                | <b><u>(140,000)</u></b>  |
|                                                                                | <b>\$ 210,000</b>        |
| Add dividends.....                                                             | <b><u>60,000</u></b>     |
| Net income.....                                                                | <b><u>\$ 270,000</u></b> |

**Ex. 1–16**

**Balance sheet items: 1, 2, 3, 5, 7, 8, 10**

**Ex. 1–17**

**Income statement items: 4, 6, 9**

## Ex. 1–18

a.

| Organic Products Company<br>Statement of Stockholders' Equity<br>For the Month Ended June 30, 20Y9 |                 |                      |             |
|----------------------------------------------------------------------------------------------------|-----------------|----------------------|-------------|
|                                                                                                    | Common<br>Stock | Retained<br>Earnings | Total       |
| Balances, June 1, 20Y9                                                                             | \$180,000       | \$1,630,000          | \$1,810,000 |
| Issued common stock                                                                                | 50,000          |                      | 50,000      |
| Net income for June                                                                                |                 | 115,000              | 115,000     |
| Dividends                                                                                          |                 | (25,000)             | (25,000)    |
| Balances, June 30, 20Y9                                                                            | \$230,000       | \$1,720,000          | \$1,950,000 |
|                                                                                                    |                 |                      |             |

- b. The statement of stockholders' equity is prepared before the June 30, 20Y9, balance sheet because common stock and retained earnings as of June 30, 20Y9, are needed for the June 30, 20Y9, balance sheet.

## Ex. 1–19

| Imaging Services<br>Income Statement<br>For the Month Ended March 31, 20Y5 |           |            |
|----------------------------------------------------------------------------|-----------|------------|
| Fees earned                                                                |           | \$ 482,000 |
| Expenses:                                                                  |           |            |
| Wages expense                                                              | \$300,000 |            |
| Rent expense                                                               | 41,500    |            |
| Supplies expense                                                           | 3,600     |            |
| Miscellaneous expense                                                      | 1,900     |            |
| Total expenses                                                             |           | (347,000)  |
| Net income                                                                 |           | \$ 135,000 |
|                                                                            |           |            |

**Ex. 1–20**

In each case, solve for a single unknown, using the following equation:

$$\text{Stockholders' Equity (beginning)} + \text{Additional Common Stock Issued} - \text{Dividends} + \text{Revenues} - \text{Expenses} = \text{Stockholders' Equity (ending)}$$

**Freeman**

|                                                                      |                   |
|----------------------------------------------------------------------|-------------------|
| Stockholders' equity at end of year (\$1,260,000 – \$330,000).....   | \$ 930,000        |
| Stockholders' equity at beginning of year (\$900,000 – \$360,000)... | <u>(540,000)</u>  |
| Increase in stockholders' equity.....                                | \$ 390,000        |
| Deduct increase due to net income (\$570,000 – \$240,000).....       | <u>(330,000)</u>  |
|                                                                      | \$ 60,000         |
| Add dividends.....                                                   | <u>75,000</u>     |
| Additional common stock issued..... (a)                              | <u>\$ 135,000</u> |

**Heyward**

|                                                                      |                   |
|----------------------------------------------------------------------|-------------------|
| Stockholders' equity at end of year (\$675,000 – \$220,000).....     | \$ 455,000        |
| Stockholders' equity at beginning of year (\$490,000 – \$260,000)... | <u>(230,000)</u>  |
| Increase in stockholders' equity.....                                | \$ 225,000        |
| Add dividends.....                                                   | <u>32,000</u>     |
|                                                                      | \$ 257,000        |
| Deduct additional common stock issued.....                           | <u>(150,000)</u>  |
| Increase due to net income.....                                      | \$ 107,000        |
| Add expenses.....                                                    | <u>128,000</u>    |
| Revenue..... (b)                                                     | <u>\$ 235,000</u> |

**Jones**

|                                                                                  |                   |
|----------------------------------------------------------------------------------|-------------------|
| Stockholders' equity at end of year (\$100,000 – \$80,000).....                  | \$ 20,000         |
| Stockholders' equity at beginning of year (\$115,000 – \$81,000).....            | <u>(34,000)</u>   |
| Decrease in stockholders' equity.....                                            | \$(14,000)        |
| Decrease in stockholders' equity due to net loss<br>(\$115,000 – \$122,500)..... | <u>7,500</u>      |
|                                                                                  | \$ (6,500)        |
| Deduct common stock issued.....                                                  | <u>(10,000)</u>   |
| Dividends..... (c)                                                               | <u>\$(16,500)</u> |

**Ramirez**

|                                                                  |                  |
|------------------------------------------------------------------|------------------|
| Stockholders' equity at end of year (\$270,000 – \$136,000)..... | \$134,000        |
| Add decrease due to net loss (\$115,000 – \$128,000).....        | <u>13,000</u>    |
|                                                                  | \$147,000        |
| Add dividends.....                                               | <u>39,000</u>    |
| Stockholders' equity at beginning of year.....                   | \$186,000        |
| Deduct additional investment.....                                | <u>(55,000)</u>  |
|                                                                  | \$131,000        |
| Add liabilities at beginning of year.....                        | <u>120,000</u>   |
| Assets at beginning of year..... (d)                             | <u>\$251,000</u> |

## Ex. 1-21

a.

| Ebony Interiors<br>Balance Sheet<br>February 28, 20Y3 |           |             |
|-------------------------------------------------------|-----------|-------------|
| <b>Assets</b>                                         |           |             |
| Cash                                                  |           | \$ 320,000  |
| Accounts receivable                                   |           | 800,000     |
| Supplies                                              |           | 30,000      |
| Total assets                                          |           | \$1,150,000 |
| <b>Liabilities</b>                                    |           |             |
| Accounts payable                                      |           | \$ 310,000  |
| <b>Stockholders' Equity</b>                           |           |             |
| Common stock                                          | \$200,000 |             |
| Retained earnings                                     | 640,000*  |             |
| Total stockholders' equity                            |           | 840,000     |
| Total liabilities and stockholders' equity            |           | \$1,150,000 |

\* \$640,000 = \$320,000 + \$800,000 + \$30,000 – \$310,000 – \$200,000

| Ebony Interiors<br>Balance Sheet<br>March 31, 20Y3 |           |             |
|----------------------------------------------------|-----------|-------------|
| <b>Assets</b>                                      |           |             |
| Cash                                               |           | \$ 380,000  |
| Accounts receivable                                |           | 960,000     |
| Supplies                                           |           | 35,000      |
| Total assets                                       |           | \$1,375,000 |
| <b>Liabilities</b>                                 |           |             |
| Accounts payable                                   |           | \$ 400,000  |
| <b>Stockholders' Equity</b>                        |           |             |
| Common stock                                       | \$200,000 |             |
| Retained earnings                                  | 775,000*  |             |
| Total stockholders' equity                         |           | 975,000     |
| Total liabilities and stockholders' equity         |           | \$1,375,000 |

\* \$775,000 = \$380,000 + \$960,000 + \$35,000 – \$400,000 – \$200,000

|                                        |                   |
|----------------------------------------|-------------------|
| b. Stockholders' equity, March 31..... | \$ 975,000        |
| Stockholders' equity, February 28..... | (840,000)         |
| Net income.....                        | <u>\$ 135,000</u> |

**Ex. 1–21 (Concluded)**

|                                        |                   |
|----------------------------------------|-------------------|
| c. Stockholders' equity, March 31..... | \$ 975,000        |
| Stockholders' equity, February 28..... | <u>(840,000)</u>  |
| Increase in stockholders' equity.....  | \$ 135,000        |
| Add dividends.....                     | <u>50,000</u>     |
| Net income.....                        | <u>\$ 185,000</u> |

**Ex. 1–22**

- a. Balance sheet: 1, 2, 3, 4, 6, 7, 8, 9, 10, 11, 13  
Income statement: 5, 12, 14, 15
- b. Yes, an item can appear on more than one financial statement. For example, cash appears on both the balance sheet and statement of cash flows. However, the same item cannot appear on both the income statement and balance sheet.
- c. Yes, the accounting equation is relevant to all companies, including Exxon Mobil Corporation. The accounting equation is the basis for all accounting systems.

**Ex. 1–23**

1. (c) financing activity
2. (a) operating activity
3. (b) investing activity
4. (c) financing activity

**Ex. 1–24**

| Parker Consulting Group<br>Statement of Cash Flows<br>For the Year Ended January 31, 20Y4 |             |            |
|-------------------------------------------------------------------------------------------|-------------|------------|
| Cash flows from (used for) operating activities:                                          |             |            |
| Cash received from customers                                                              | \$1,200,000 |            |
| Cash paid for operating expenses                                                          | (800,000)   |            |
| Net cash flows from operating activities                                                  |             | \$ 400,000 |
| Cash flows from (used for) investing activities:                                          |             |            |
| Cash paid for purchase of land                                                            |             | (300,000)  |
| Cash flows from (used for) financing activities:                                          |             |            |
| Cash received from issuing common stock                                                   | \$ 90,000   |            |
| Cash paid as dividends                                                                    | (36,000)    |            |
| Net cash flows from financing activities                                                  |             | 54,000     |
| Net increase in cash                                                                      |             | \$ 154,000 |
| Cash balance, February 1, 20Y3                                                            |             | 66,000     |
| Cash balance, January 31, 20Y4                                                            |             | \$ 220,000 |

**Ex. 1–25**

- a. 1. All financial statements should contain the name of the business in their heading. The statement of stockholders' equity is incorrectly headed as "Omar Farah" rather than We-Sell Realty. The heading of the balance sheet needs to include the name of the business.
2. The income statement covers a period of time and should be labeled "For the Month Ended August 31, 20Y7."
3. The year in the heading for the statement of stockholders' equity should be 20Y7 rather than 20Y6.
4. The balance sheet should be labeled "August 31, 20Y7," rather than "For the Month Ended August 31, 20Y7."
5. On the income statement, the miscellaneous expense amount should be listed as the last expense.
6. On the income statement, the total expenses are subtracted from the sales commissions, resulting in an incorrect net income amount of \$25,000. The correct net income should be \$24,150. This also affects the statement of stockholders' equity and the amount of retained earnings that appears on the balance sheet.
7. On the statement of stockholders' equity, there is no column for common stock. Also, the statement is for the "month" rather than for the "year" ended August 31, 20Y7.
8. Accounts payable should be listed as a liability on the balance sheet.
9. Accounts receivable and supplies should be listed as assets on the balance sheet.
10. The balance sheet assets should equal the sum of the liabilities and stockholders' equity.

**Ex. 1–25 (Concluded)**

**b. Corrected financial statements appear as follows:**

| <b>We-Sell Realty<br/>Income Statement<br/>For the Month Ended August 31, 20Y7</b> |                 |                   |
|------------------------------------------------------------------------------------|-----------------|-------------------|
| <b>Sales commissions</b>                                                           |                 | <b>\$ 140,000</b> |
| <b>Expenses:</b>                                                                   |                 |                   |
| Office salaries expense                                                            | <b>\$87,000</b> |                   |
| Rent expense                                                                       | <b>18,000</b>   |                   |
| Automobile expense                                                                 | <b>7,500</b>    |                   |
| Supplies expense                                                                   | <b>1,150</b>    |                   |
| Miscellaneous expense                                                              | <b>2,200</b>    |                   |
| <b>Total expenses</b>                                                              |                 | <b>(115,850)</b>  |
| <b>Net income</b>                                                                  |                 | <b>\$ 24,150</b>  |

| <b>We-Sell Realty<br/>Statement of Stockholders' Equity<br/>For the Month Ended August 31, 20Y7</b> |                         |                              |                  |
|-----------------------------------------------------------------------------------------------------|-------------------------|------------------------------|------------------|
|                                                                                                     | <b>Common<br/>Stock</b> | <b>Retained<br/>Earnings</b> | <b>Total</b>     |
| <b>Balances, August 1, 20Y7</b>                                                                     | <b>\$ 0</b>             | <b>\$ 0</b>                  | <b>\$ 0</b>      |
| <b>Issued common stock</b>                                                                          | <b>15,000</b>           |                              | <b>15,000</b>    |
| <b>Net income for August</b>                                                                        |                         | <b>24,150</b>                | <b>24,150</b>    |
| <b>Dividends</b>                                                                                    |                         | <b>(10,000)</b>              | <b>(10,000)</b>  |
| <b>Balances, August 31, 20Y7</b>                                                                    | <b>\$15,000</b>         | <b>\$ 14,150</b>             | <b>\$ 29,150</b> |

| <b>We-Sell Realty<br/>Balance Sheet<br/>August 31, 20Y7</b> |                 |                 |
|-------------------------------------------------------------|-----------------|-----------------|
| <b>Assets</b>                                               |                 |                 |
| Cash                                                        |                 | <b>\$ 8,900</b> |
| Accounts receivable                                         |                 | <b>38,600</b>   |
| Supplies                                                    |                 | <b>4,000</b>    |
| <b>Total assets</b>                                         |                 | <b>\$51,500</b> |
| <b>Liabilities</b>                                          |                 |                 |
| Accounts payable                                            |                 | <b>\$22,350</b> |
| <b>Stockholders' Equity</b>                                 |                 |                 |
| Common stock                                                | <b>\$15,000</b> |                 |
| Retained earnings                                           | <b>14,150</b>   |                 |
| <b>Total stockholders' equity</b>                           |                 | <b>29,150</b>   |
| <b>Total liabilities and stockholders' equity</b>           |                 | <b>\$51,500</b> |

# PROBLEMS

## Prob. 1-1A

| 1.   | Assets |        |             | = Liabilities + |          |       | Stockholders' Equity |       |              |        |           |       |             |        |              |       |                  |       |                  |       |           |       |            |     |
|------|--------|--------|-------------|-----------------|----------|-------|----------------------|-------|--------------|--------|-----------|-------|-------------|--------|--------------|-------|------------------|-------|------------------|-------|-----------|-------|------------|-----|
|      | Cash   | +      | Accts. Rec. | +               | Supplies | =     | Accts. Payable       | +     | Common Stock | -      | Dividends | +     | Fees Earned | -      | Rent Expense | -     | Salaries Expense | -     | Supplies Expense | -     | Auto Exp. | -     | Misc. Exp. |     |
| a.   | +      | 75,000 |             |                 |          |       |                      |       |              |        |           |       |             |        |              |       |                  |       |                  |       |           |       |            |     |
| b.   |        |        |             |                 | +        | 2,200 | +                    | 2,200 |              | 75,000 |           |       |             |        |              |       |                  |       |                  |       |           |       |            |     |
| Bal. | 75,000 |        |             |                 | 2,200    |       | 2,200                |       | 75,000       |        |           |       | +           | 19,500 |              |       |                  |       |                  |       |           |       |            |     |
| c.   | +      | 19,500 |             |                 |          |       |                      |       |              |        |           |       | 19,500      |        |              |       |                  |       |                  |       |           |       |            |     |
| Bal. | 94,500 |        |             |                 | 2,200    |       | 2,200                |       | 75,000       |        |           |       |             |        | -            | 8,000 |                  |       |                  |       |           |       |            |     |
| d.   | -      | 8,000  |             |                 |          |       |                      |       |              |        |           |       | 19,500      |        | -            | 8,000 |                  |       |                  |       |           |       |            |     |
| Bal. | 86,500 |        |             |                 | 2,200    |       | 2,200                |       | 75,000       |        |           |       |             |        |              |       |                  |       |                  |       |           |       |            |     |
| e.   | -      | 1,850  |             |                 |          |       | -                    | 1,850 |              |        |           |       | 19,500      |        | -            | 8,000 |                  |       |                  |       |           |       |            |     |
| Bal. | 84,650 |        |             |                 | 2,200    |       | 350                  |       | 75,000       |        |           |       | +           | 6,000  |              |       |                  |       |                  |       |           |       |            |     |
| f.   |        |        | +           | 6,000           |          |       |                      |       |              |        |           |       | 25,500      |        | -            | 8,000 |                  |       |                  |       |           |       |            |     |
| Bal. | 84,650 |        | 6,000       |                 | 2,200    |       | 350                  |       | 75,000       |        |           |       |             |        |              |       |                  |       |                  |       | -         | 1,500 | -          | 800 |
| g.   | -      | 2,300  |             |                 |          |       |                      |       |              |        |           |       | 25,500      |        | -            | 8,000 |                  |       |                  |       | -         | 1,500 | -          | 800 |
| Bal. | 82,350 |        | 6,000       |                 | 2,200    |       | 350                  |       | 75,000       |        |           |       |             |        |              |       | -                | 5,500 |                  |       |           |       |            |     |
| h.   | -      | 5,500  |             |                 |          |       |                      |       |              |        |           |       | 25,500      |        | -            | 8,000 |                  |       |                  |       | -         | 1,500 | -          | 800 |
| Bal. | 76,850 |        | 6,000       |                 | 2,200    |       | 350                  |       | 75,000       |        |           |       |             |        |              |       |                  |       | -                | 1,650 |           |       |            |     |
| i.   |        |        |             |                 | -        | 1,650 |                      |       |              |        |           |       | 25,500      |        | -            | 8,000 |                  |       |                  |       |           |       |            |     |
| Bal. | 76,850 |        | 6,000       |                 | 550      |       | 350                  |       | 75,000       |        |           |       |             |        |              |       |                  |       |                  |       |           |       |            |     |
| j.   | -      | 4,000  |             |                 |          |       |                      |       |              |        |           |       | 25,500      |        | -            | 8,000 |                  |       |                  |       | -         | 1,500 | -          | 800 |
| Bal. | 72,850 |        | 6,000       |                 | 550      |       | 350                  |       | 75,000       |        | -         | 4,000 |             |        |              |       |                  |       |                  |       |           |       |            |     |
|      |        |        |             |                 |          |       |                      |       |              |        |           |       | 25,500      |        | -            | 8,000 |                  |       |                  |       | -         | 1,500 | -          | 800 |

- Stockholders' equity is the right of stockholders (owners) to the assets of the business. These rights are increased by issuing common stock and revenues and decreased by dividends and expenses.
- \$8,050 (\$25,500 - \$8,000 - \$5,500 - \$1,650 - \$1,500 - \$800)
- June's transactions increased stockholders' equity by \$79,050, which is the common stock of \$75,000 that was issued plus June's net income of \$8,050 less dividends of \$4,000.

## Prob. 1–2A

| Preferred Travel Agency<br>Income Statement<br>For the Year Ended December 31, 20Y5 |           |             |
|-------------------------------------------------------------------------------------|-----------|-------------|
| Fees earned                                                                         |           | \$1,075,000 |
| Expenses:                                                                           |           |             |
| Wages expense                                                                       | \$615,000 |             |
| Rent expense                                                                        | 170,000   |             |
| Utilities expense                                                                   | 51,500    |             |
| Supplies expense                                                                    | 16,000    |             |
| Miscellaneous expense                                                               | 22,500    |             |
| Total expenses                                                                      |           | (875,000)   |
| Net income                                                                          |           | \$ 200,000  |

| Preferred Travel Agency<br>Statement of Stockholders' Equity<br>For the Year Ended December 31, 20Y5 |                 |                      |             |
|------------------------------------------------------------------------------------------------------|-----------------|----------------------|-------------|
|                                                                                                      | Common<br>Stock | Retained<br>Earnings | Total       |
| Balances, January 1, 20Y5                                                                            | \$100,000       | \$ 873,000           | \$ 973,000  |
| Issued common stock                                                                                  | 60,000          |                      | 60,000      |
| Net income for the year                                                                              |                 | 200,000              | 200,000     |
| Dividends                                                                                            |                 | (25,000)             | (25,000)    |
| Balances, December 31, 20Y5                                                                          | \$160,000       | \$1,048,000          | \$1,208,000 |

| Preferred Travel Agency<br>Balance Sheet<br>December 31, 20Y5 |            |             |
|---------------------------------------------------------------|------------|-------------|
| <b>Assets</b>                                                 |            |             |
| Cash                                                          |            | \$ 65,500   |
| Accounts receivable                                           |            | 90,000      |
| Supplies                                                      |            | 4,500       |
| Land                                                          |            | 1,100,000   |
| Total assets                                                  |            | \$1,260,000 |
| <b>Liabilities</b>                                            |            |             |
| Accounts payable                                              |            | \$ 52,000   |
| <b>Stockholders' Equity</b>                                   |            |             |
| Common stock                                                  | \$ 160,000 |             |
| Retained earnings                                             | 1,048,000  |             |
| Total stockholders' equity                                    |            | 1,208,000   |
| Total liabilities and stockholders' equity                    |            | \$1,260,000 |

**Prob. 1–2A (Concluded)**

4. Ending common stock and retained earnings appear on both the statement of stockholders' equity and the balance sheet. For Preferred Travel Agency, the December 31, 20Y5, common stock of \$160,000 and retained earnings of \$1,048,000 appear on the statement of stockholders' equity and balance sheet.

**Prob. 1–3A**

1.

| Reliance Financial Services       |          |            |
|-----------------------------------|----------|------------|
| Income Statement                  |          |            |
| For the Month Ended July 31, 20Y2 |          |            |
| Fees earned                       |          | \$ 144,500 |
| Expenses:                         |          |            |
| Salaries expense                  | \$55,000 |            |
| Rent expense                      | 33,000   |            |
| Auto expense                      | 16,000   |            |
| Supplies expense                  | 4,500    |            |
| Miscellaneous expense             | 4,800    |            |
| Total expenses                    |          | (113,300)  |
| Net income                        |          | \$ 31,200  |
|                                   |          |            |

2.

| Reliance Financial Services<br>Statement of Stockholders' Equity<br>For the Month Ended July 31, 20Y2 |                 |                      |           |
|-------------------------------------------------------------------------------------------------------|-----------------|----------------------|-----------|
|                                                                                                       | Common<br>Stock | Retained<br>Earnings | Total     |
| Balances, July 1, 20Y2                                                                                | \$ 0            | \$ 0                 | \$ 0      |
| Issued common stock                                                                                   | 50,000          |                      | 50,000    |
| Net income for July                                                                                   |                 | 31,200               | 31,200    |
| Dividends                                                                                             |                 | (15,000)             | (15,000)  |
| Balances, July 31, 20Y2                                                                               | \$50,000        | \$ 16,200            | \$ 66,200 |
|                                                                                                       |                 |                      |           |

Prob. 1–3A (Concluded)

| <b>Reliance Financial Services</b><br><b>Balance Sheet</b><br><b>July 31, 20Y2</b> |          |                 |
|------------------------------------------------------------------------------------|----------|-----------------|
| <b>Assets</b>                                                                      |          |                 |
| Cash                                                                               |          | \$32,600        |
| Accounts receivable                                                                |          | 34,500          |
| Supplies                                                                           |          | 2,500           |
| <b>Total assets</b>                                                                |          | <b>\$69,600</b> |
| <b>Liabilities</b>                                                                 |          |                 |
| Accounts payable                                                                   |          | \$ 3,400        |
| <b>Stockholders' Equity</b>                                                        |          |                 |
| Common stock                                                                       | \$50,000 |                 |
| Retained earnings                                                                  | 16,200   |                 |
| <b>Total stockholders' equity</b>                                                  |          | <b>66,200</b>   |
| <b>Total liabilities and stockholders' equity</b>                                  |          | <b>\$69,600</b> |

4. Optional

| <b>Reliance Financial Services</b><br><b>Statement of Cash Flows</b><br><b>For the Month Ended July 31, 20Y2</b> |            |                   |
|------------------------------------------------------------------------------------------------------------------|------------|-------------------|
| <b>Cash flows from (used for) operating activities:</b>                                                          |            |                   |
| Cash received from customers                                                                                     | \$ 110,000 |                   |
| Cash paid for expenses and to creditors*                                                                         | (112,400)  |                   |
| <b>Net cash flows used for operating activities</b>                                                              |            | <b>\$ (2,400)</b> |
| <b>Cash flows from (used for) investing activities</b>                                                           |            | <b>0</b>          |
| <b>Cash flows from (used for) financing activities:</b>                                                          |            |                   |
| Cash received from issuing common stock                                                                          | \$ 50,000  |                   |
| Cash paid as dividends                                                                                           | (15,000)   |                   |
| <b>Net cash flows from financing activities</b>                                                                  |            | <b>35,000</b>     |
| <b>Net increase in cash</b>                                                                                      |            | <b>\$32,600</b>   |
| Cash balance, July 1, 20Y2                                                                                       |            | 0                 |
| <b>Cash balance, July 31, 20Y2</b>                                                                               |            | <b>\$32,600</b>   |

\* \$3,600 + \$33,000 + \$20,800 + \$55,000; these amounts are taken from the Cash column shown in the problem.

Prob. 1-4A

| 1.   | Assets   |            | = | Liabilities +  |                | Stockholders' Equity |               |                 |             |             |                 |              |  |
|------|----------|------------|---|----------------|----------------|----------------------|---------------|-----------------|-------------|-------------|-----------------|--------------|--|
|      | Cash     | + Supplies | = | Accts. Payable | + Common Stock | - Dividends          | + Sales Comm. | - Salaries Exp. | - Rent Exp. | - Auto Exp. | - Supplies Exp. | - Misc. Exp. |  |
| a.   | + 35,000 |            |   |                | + 35,000       |                      |               |                 |             |             |                 |              |  |
| b.   |          | + 2,750    |   | + 2,750        |                |                      |               |                 |             |             |                 |              |  |
| Bal. | 35,000   | 2,750      |   | 2,750          | 35,000         |                      |               |                 |             |             |                 |              |  |
| c.   | - 1,800  |            |   | - 1,800        |                |                      |               |                 |             |             |                 |              |  |
| Bal. | 33,200   | 2,750      |   | 950            | 35,000         |                      |               |                 |             |             |                 |              |  |
| d.   | + 52,800 |            |   |                |                |                      | + 52,800      |                 |             |             |                 |              |  |
| Bal. | 86,000   | 2,750      |   | 950            | 35,000         |                      | 52,800        |                 | - 4,500     |             |                 |              |  |
| e.   | - 4,500  |            |   |                |                |                      |               |                 | - 4,500     |             |                 |              |  |
| Bal. | 81,500   | 2,750      |   | 950            | 35,000         |                      | 52,800        |                 | - 4,500     |             |                 |              |  |
| f.   | - 3,000  |            |   |                |                | - 3,000              |               |                 |             |             |                 |              |  |
| Bal. | 78,500   | 2,750      |   | 950            | 35,000         | - 3,000              | 52,800        |                 | - 4,500     |             |                 |              |  |
| g.   | - 2,300  |            |   |                |                |                      |               |                 |             | - 1,100     |                 | - 1,200      |  |
| Bal. | 76,200   | 2,750      |   | 950            | 35,000         | - 3,000              | 52,800        | - 5,250         | - 4,500     | - 1,100     |                 | - 1,200      |  |
| h.   | - 5,250  |            |   |                |                |                      |               | - 5,250         |             |             |                 |              |  |
| Bal. | 70,950   | 2,750      |   | 950            | 35,000         | - 3,000              | 52,800        | - 5,250         | - 4,500     | - 1,100     |                 | - 1,200      |  |
| i.   |          | - 1,000    |   |                |                |                      |               |                 |             |             | - 1,000         |              |  |
| Bal. | 70,950   | 1,750      |   | 950            | 35,000         | - 3,000              | 52,800        | - 5,250         | - 4,500     | - 1,100     | - 1,000         | - 1,200      |  |

Prob. 1–4A (Concluded)

2.

| <b>Western Realty</b><br><b>Income Statement</b><br><b>For the Month Ended August 31, 20Y9</b> |         |           |
|------------------------------------------------------------------------------------------------|---------|-----------|
| Sales commissions                                                                              |         | \$ 52,800 |
| Expenses:                                                                                      |         |           |
| Salaries expense                                                                               | \$5,250 |           |
| Rent expense                                                                                   | 4,500   |           |
| Automobile expense                                                                             | 1,100   |           |
| Supplies expense                                                                               | 1,000   |           |
| Miscellaneous expense                                                                          | 1,200   |           |
| Total expenses                                                                                 |         | (13,050)  |
| Net income                                                                                     |         | \$ 39,750 |

| <b>Western Realty</b><br><b>Statement of Stockholders' Equity</b><br><b>For the Month Ended August 31, 20Y9</b> |                 |                      |          |
|-----------------------------------------------------------------------------------------------------------------|-----------------|----------------------|----------|
|                                                                                                                 | Common<br>Stock | Retained<br>Earnings | Total    |
| Balances, August 1, 20Y9                                                                                        | \$ 0            | \$ 0                 | \$ 0     |
| Issued common stock                                                                                             | 35,000          |                      | 35,000   |
| Net income for August                                                                                           |                 | 39,750               | 39,750   |
| Dividends                                                                                                       |                 | (3,000)              | (3,000)  |
| Balances, August 31, 20Y9                                                                                       | \$35,000        | \$36,750             | \$71,750 |

| <b>Western Realty</b><br><b>Balance Sheet</b><br><b>August 31, 20Y9</b> |          |          |
|-------------------------------------------------------------------------|----------|----------|
| <b>Assets</b>                                                           |          |          |
| Cash                                                                    |          | \$70,950 |
| Supplies                                                                |          | 1,750    |
| Total assets                                                            |          | \$72,700 |
| <b>Liabilities</b>                                                      |          |          |
| Accounts payable                                                        |          | \$ 950   |
| <b>Stockholders' Equity</b>                                             |          |          |
| Common stock                                                            | \$35,000 |          |
| Retained earnings                                                       | 36,750   |          |
| Total stockholders' equity                                              |          | 71,750   |
| Total liabilities and stockholders' equity                              |          | \$72,700 |

**Prob. 1–5A**

|    |               |   |                        |   |          |   |                                           |   |                     |   |                   |   |                      |
|----|---------------|---|------------------------|---|----------|---|-------------------------------------------|---|---------------------|---|-------------------|---|----------------------|
| 1. | <u>Assets</u> |   |                        |   |          | = | <u>Liabilities + Stockholders' Equity</u> |   |                     |   |                   |   |                      |
|    | Cash          | + | Accounts<br>Receivable | + | Supplies | + | Land                                      | = | Accounts<br>Payable | + | Common<br>Stock   | + | Retained<br>Earnings |
|    | \$45,000      | + | \$93,000               | + | \$7,000  | + | \$75,000                                  | = | \$40,000            | + | \$60,000          | + | Retained<br>Earnings |
|    |               |   |                        |   |          |   | \$220,000                                 | = | \$100,000           | + | Retained Earnings |   |                      |
|    |               |   |                        |   |          |   | \$120,000                                 | = | Retained Earnings   |   |                   |   |                      |

Prob. 1–5A (Continued)

| 2.   | Assets   |   |                |   |          | = | Liabilities + Stockholders' Equity |   |                   |   |                 |   |                      |          |           |
|------|----------|---|----------------|---|----------|---|------------------------------------|---|-------------------|---|-----------------|---|----------------------|----------|-----------|
|      | Cash     | + | Accts.<br>Rec. | + | Supplies | + | Land                               | = | Accts.<br>Payable | + | Common<br>Stock | + | Retained<br>Earnings | –        | Dividends |
| Bal. | 45,000   |   | 93,000         |   | 7,000    |   | 75,000                             |   | 40,000            |   | 60,000          |   | 120,000              |          |           |
| a.   | + 35,000 |   |                |   |          |   |                                    |   |                   |   | + 35,000        |   |                      |          |           |
| Bal. | 80,000   |   | 93,000         |   | 7,000    |   | 75,000                             |   | 40,000            |   | 95,000          |   | 120,000              |          |           |
| b.   | – 50,000 |   |                |   |          |   | + 50,000                           |   |                   |   |                 |   |                      |          |           |
| Bal. | 30,000   |   | 93,000         |   | 7,000    |   | 125,000                            |   | 40,000            |   | 95,000          |   | 120,000              |          |           |
| c.   | + 32,125 |   |                |   |          |   |                                    |   |                   |   |                 |   |                      |          |           |
| Bal. | 62,125   |   | 93,000         |   | 7,000    |   | 125,000                            |   | 40,000            |   | 95,000          |   | 120,000              |          |           |
| d.   | – 6,000  |   |                |   |          |   |                                    |   |                   |   |                 |   |                      |          |           |
| Bal. | 56,125   |   | 93,000         |   | 7,000    |   | 125,000                            |   | 40,000            |   | 95,000          |   | 120,000              |          |           |
| e.   |          |   |                |   | + 2,500  |   |                                    |   | + 2,500           |   |                 |   |                      |          |           |
| Bal. | 56,125   |   | 93,000         |   | 9,500    |   | 125,000                            |   | 42,500            |   | 95,000          |   | 120,000              |          |           |
| f.   | – 22,800 |   |                |   |          |   |                                    |   | – 22,800          |   |                 |   |                      |          |           |
| Bal. | 33,325   |   | 93,000         |   | 9,500    |   | 125,000                            |   | 19,700            |   | 95,000          |   | 120,000              |          |           |
| g.   |          |   | + 84,750       |   |          |   |                                    |   |                   |   |                 |   |                      |          |           |
| Bal. | 33,325   |   | 177,750        |   | 9,500    |   | 125,000                            |   | 19,700            |   | 95,000          |   | 120,000              |          |           |
| h.   |          |   |                |   |          |   |                                    |   | + 29,500          |   |                 |   |                      |          |           |
| Bal. | 33,325   |   | 177,750        |   | 9,500    |   | 125,000                            |   | 49,200            |   | 95,000          |   | 120,000              |          |           |
| i.   | – 14,000 |   |                |   |          |   |                                    |   |                   |   |                 |   |                      |          |           |
| Bal. | 19,325   |   | 177,750        |   | 9,500    |   | 125,000                            |   | 49,200            |   | 95,000          |   | 120,000              |          |           |
| j.   | + 88,000 |   | – 88,000       |   |          |   |                                    |   |                   |   |                 |   |                      |          |           |
| Bal. | 107,325  |   | 89,750         |   | 9,500    |   | 125,000                            |   | 49,200            |   | 95,000          |   | 120,000              |          |           |
| k.   |          |   |                |   | – 3,600  |   |                                    |   |                   |   |                 |   |                      |          |           |
| Bal. | 107,325  |   | 89,750         |   | 5,900    |   | 125,000                            |   | 49,200            |   | 95,000          |   | 120,000              |          |           |
| l.   | – 12,000 |   |                |   |          |   |                                    |   |                   |   |                 |   |                      | – 12,000 |           |
| Bal. | 95,325   |   | 89,750         |   | 5,900    |   | 125,000                            |   | 49,200            |   | 95,000          |   | 120,000              | – 12,000 |           |

## Prob. 1–5A (Continued)

| Stockholders' Equity (Continued) |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
|----------------------------------|----------|---------|----------|--------|-------|-------|------|-------|----------|-------|-------|-------|-----------|-------|-------|-------|
|                                  | Dry      |         | Dry      |        | Wages |       | Rent |       | Supplies |       | Truck |       | Utilities |       | Misc. |       |
| +                                | Cleaning | -       | Cleaning | -      | Exp.  | -     | Exp. | -     | Exp.     | -     | Exp.  | -     | Exp.      | -     | Exp.  |       |
| Bal.                             |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| a.                               |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| b.                               |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| c.                               | +        | 32,125  |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 32,125  |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| d.                               |          |         |          |        |       |       | -    | 6,000 |          |       |       |       |           |       |       |       |
| Bal.                             |          | 32,125  |          |        |       |       | -    | 6,000 |          |       |       |       |           |       |       |       |
| e.                               |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 32,125  |          |        |       |       | -    | 6,000 |          |       |       |       |           |       |       |       |
| f.                               |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 32,125  |          |        |       |       | -    | 6,000 |          |       |       |       |           |       |       |       |
| g.                               | +        | 84,750  |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 116,875 |          |        |       |       | -    | 6,000 |          |       |       |       |           |       |       |       |
| h.                               |          |         | -        | 29,500 |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 116,875 | -        | 29,500 |       |       | -    | 6,000 |          |       |       |       |           |       |       |       |
| i.                               |          |         |          |        | -     | 7,500 |      |       |          | -     | 2,500 | -     | 1,300     | -     | 2,700 |       |
| Bal.                             |          | 116,875 | -        | 29,500 | -     | 7,500 | -    | 6,000 |          | -     | 2,500 | -     | 1,300     | -     | 2,700 |       |
| j.                               |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 116,875 | -        | 29,500 | -     | 7,500 | -    | 6,000 |          | -     | 2,500 | -     | 1,300     | -     | 2,700 |       |
| k.                               |          |         |          |        |       |       |      |       | -        | 3,600 |       |       |           |       |       |       |
| Bal.                             |          | 116,875 | -        | 29,500 | -     | 7,500 | -    | 6,000 | -        | 3,600 | -     | 2,500 | -         | 1,300 | -     | 2,700 |
| l.                               |          |         |          |        |       |       |      |       |          |       |       |       |           |       |       |       |
| Bal.                             |          | 116,875 | -        | 29,500 | -     | 7,500 | -    | 6,000 | -        | 3,600 | -     | 2,500 | -         | 1,300 | -     | 2,700 |

Prob. 1–5A (Continued)

| <b>D'Lite Dry Cleaners</b><br><b>Income Statement</b><br><b>For the Month Ended July 31, 20Y4</b> |          |           |
|---------------------------------------------------------------------------------------------------|----------|-----------|
| Dry cleaning revenue                                                                              |          | \$116,875 |
| Expenses:                                                                                         |          |           |
| Dry cleaning expense                                                                              | \$29,500 |           |
| Wages expense                                                                                     | 7,500    |           |
| Rent expense                                                                                      | 6,000    |           |
| Supplies expense                                                                                  | 3,600    |           |
| Truck expense                                                                                     | 2,500    |           |
| Utilities expense                                                                                 | 1,300    |           |
| Miscellaneous expense                                                                             | 2,700    |           |
| Total expenses                                                                                    |          | (53,100)  |
| Net income                                                                                        |          | \$ 63,775 |

| <b>D'Lite Dry Cleaners</b><br><b>Statement of Stockholders' Equity</b><br><b>For the Month Ended July 31, 20Y4</b> |                 |                      |           |
|--------------------------------------------------------------------------------------------------------------------|-----------------|----------------------|-----------|
|                                                                                                                    | Common<br>Stock | Retained<br>Earnings | Total     |
| Balances, July 1, 20Y4                                                                                             | \$60,000        | \$120,000            | \$180,000 |
| Issued common stock                                                                                                | 35,000          |                      | 35,000    |
| Net income for July                                                                                                |                 | 63,775               | 63,775    |
| Dividends                                                                                                          |                 | (12,000)             | (12,000)  |
| Balances, July 31, 20Y4                                                                                            | \$95,000        | \$171,775            | \$266,775 |

| <b>D'Lite Dry Cleaners</b><br><b>Balance Sheet</b><br><b>July 31, 20Y4</b> |           |           |
|----------------------------------------------------------------------------|-----------|-----------|
| <b>Assets</b>                                                              |           |           |
| Cash                                                                       |           | \$ 95,325 |
| Accounts receivable                                                        |           | 89,750    |
| Supplies                                                                   |           | 5,900     |
| Land                                                                       |           | 125,000   |
| Total assets                                                               |           | \$315,975 |
| <b>Liabilities</b>                                                         |           |           |
| Accounts payable                                                           |           | \$ 49,200 |
| <b>Stockholders' Equity</b>                                                |           |           |
| Common stock                                                               | \$ 95,000 |           |
| Retained earnings                                                          | 171,775   |           |
| Total stockholders' equity                                                 |           | 266,775   |
| Total liabilities and stockholders' equity                                 |           | \$315,975 |

## Prob. 1–5A (Concluded)

## 4. Optional

| D'Lite Dry Cleaners<br>Statement of Cash Flows<br>For the Month Ended July 31, 20Y4 |           |           |
|-------------------------------------------------------------------------------------|-----------|-----------|
| Cash flows from (used for) operating activities:                                    |           |           |
| Cash received from customers*                                                       | \$120,125 |           |
| Cash paid for expenses and to creditors**                                           | (42,800)  |           |
| Net cash flows from operating activities                                            |           | \$ 77,325 |
| Cash flows from (used for) investing activities:                                    |           |           |
| Cash paid for acquisition of land                                                   |           | (50,000)  |
| Cash flows from (used for) financing activities:                                    |           |           |
| Cash received from issuing common stock                                             | \$ 35,000 |           |
| Cash paid as dividends                                                              | (12,000)  |           |
| Net cash flows from financing activities                                            |           | 23,000    |
| Net increase in cash                                                                |           | \$ 50,325 |
| Cash balance, July 1, 20Y4                                                          |           | 45,000    |
| Cash balance, July 31, 20Y4                                                         |           | \$ 95,325 |

\* \$32,125 + \$88,000; these amounts are taken from the Cash column of the spreadsheet in Part 2.

\*\* \$6,000 + \$22,800 + \$14,000; these amounts are taken from the Cash column of the spreadsheet in Part 2.

**Prob. 1–6A**

- a. Fees earned, \$750,000 ( $\$275,000 + \$475,000$ )
- b. Supplies expense, \$30,000 ( $\$475,000 - \$300,000 - \$100,000 - \$20,000 - \$25,000$ )
- c. The common stock, \$375,000; the amount shown on the balance sheet
- d. Net income for April, \$275,000 from the income statement
- e. \$150,000 ( $\$275,000 - \$125,000$ )
- f. Total stockholders' equity, \$525,000 ( $\$375,000 + \$150,000$ )
- g. Total assets, \$625,000 ( $\$462,500 + \$12,500 + \$150,000$ )
- h. Retained earnings, \$150,000; same as (e)
- i. Total stockholders' equity, \$525,000 ( $\$375,000 + \$150,000$ ); same as (f)
- j. Total liabilities and stockholders' equity, \$625,000 ( $\$100,000 + \$525,000$ )
- k. Cash received from customers, \$750,000 ( $\$387,500 + \$362,500$ ); this is the same as fees earned (a) since there are no accounts receivable.
- l. Net cash flows from operating activities, \$362,500 ( $\$750,000 - \$387,500$ )
- m. Cash paid for land, (\$150,000)
- n. Cash received from issuing common stock, \$375,000
- o. Cash dividends, (\$125,000)
- p. Net cash flows from financing activities, \$250,000 ( $\$375,000 - \$125,000$ )
- q. Net increase in cash, \$462,500 ( $\$362,500 - \$150,000 + \$250,000$ )
- r. Cash as of April 30, 20Y0, \$462,500; same as (q) since Wolverine Realty was organized on April 1, 20Y0; also cash balance on the balance sheet.

Prob. 1-1B

| 1.   | Assets   |   |             | = Liabilities + |          |   | Stockholders' Equity |   |              |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
|------|----------|---|-------------|-----------------|----------|---|----------------------|---|--------------|---|-----------|---|-------------|---|--------------|---|------------------|---|------------------|---|-----------|------------|
|      | Cash     | + | Accts. Rec. | +               | Supplies | = | Accts. Payable       | + | Common Stock | - | Dividends | + | Fees Earned | - | Rent Expense | - | Salaries Expense | - | Supplies Expense | - | Auto Exp. | Misc. Exp. |
| a.   | + 50,000 |   |             |                 |          |   |                      |   | + 50,000     |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
| b.   |          |   |             |                 | + 4,000  |   | + 4,000              |   |              |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
| Bal. | 50,000   |   |             |                 | 4,000    |   | 4,000                |   | 50,000       |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
| c.   | - 2,300  |   |             |                 |          |   | - 2,300              |   |              |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
| Bal. | 47,700   |   |             |                 | 4,000    |   | 1,700                |   | 50,000       |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
| d.   | + 13,800 |   |             |                 |          |   |                      |   |              |   |           |   | + 13,800    |   |              |   |                  |   |                  |   |           |            |
| Bal. | 61,500   |   |             |                 | 4,000    |   | 1,700                |   | 50,000       |   |           |   | 13,800      |   | - 5,000      |   |                  |   |                  |   |           |            |
| e.   | - 5,000  |   |             |                 |          |   |                      |   |              |   |           |   |             |   | - 5,000      |   |                  |   |                  |   |           |            |
| Bal. | 56,500   |   |             |                 | 4,000    |   | 1,700                |   | 50,000       |   |           |   | 13,800      |   | - 5,000      |   |                  |   |                  |   |           |            |
| f.   | - 1,450  |   |             |                 |          |   |                      |   |              |   |           |   |             |   |              |   |                  |   |                  |   |           |            |
| Bal. | 55,050   |   |             |                 | 4,000    |   | 1,700                |   | 50,000       |   |           |   | 13,800      |   | - 5,000      |   |                  |   |                  |   | - 1,150   | - 300      |
| g.   | - 2,500  |   |             |                 |          |   |                      |   |              |   |           |   |             |   |              |   | - 2,500          |   |                  |   | - 1,150   | - 300      |
| Bal. | 52,550   |   |             |                 | 4,000    |   | 1,700                |   | 50,000       |   |           |   | 13,800      |   | - 5,000      |   | - 2,500          |   |                  |   | - 1,150   | - 300      |
| h.   |          |   |             |                 | - 1,300  |   |                      |   |              |   |           |   |             |   |              |   |                  |   | - 1,300          |   |           |            |
| Bal. | 52,550   |   |             |                 | 2,700    |   | 1,700                |   | 50,000       |   |           |   | 13,800      |   | - 5,000      |   | - 2,500          |   | - 1,300          |   | - 1,150   | - 300      |
| i.   |          |   | + 12,500    |                 |          |   |                      |   |              |   |           |   | + 12,500    |   |              |   |                  |   |                  |   |           |            |
| Bal. | 52,550   |   | 12,500      |                 | 2,700    |   | 1,700                |   | 50,000       |   |           |   | 26,300      |   | - 5,000      |   | - 2,500          |   | - 1,300          |   | - 1,150   | - 300      |
| j.   | - 3,900  |   |             |                 |          |   |                      |   |              |   | - 3,900   |   |             |   |              |   |                  |   |                  |   |           |            |
| Bal. | 48,650   |   | 12,500      |                 | 2,700    |   | 1,700                |   | 50,000       |   | - 3,900   |   | 26,300      |   | - 5,000      |   | - 2,500          |   | - 1,300          |   | - 1,150   | - 300      |

2. Stockholders' equity is the right of stockholders (owners) to the assets of the business. These rights are increased by issuing common stock and revenues and decreased by dividends and expenses.

3. \$16,050 (\$26,300 - \$5,000 - \$2,500 - \$1,300 - \$1,150 - \$300)

4. March's transactions increased stockholders' equity by \$62,150, which is the common stock that was issued of \$50,000 plus the excess of March's net income of \$16,050 over dividends of \$3,900.

Prob. 1–2B

| <b>Ocean Cruiser<br/>Income Statement<br/>For the Year Ended February 28, 20Y7</b> |             |              |
|------------------------------------------------------------------------------------|-------------|--------------|
| Fees earned                                                                        |             | \$ 2,500,000 |
| Expenses:                                                                          |             |              |
| Wages expense                                                                      | \$1,325,000 |              |
| Rent expense                                                                       | 215,000     |              |
| Utilities expense                                                                  | 55,000      |              |
| Advertising expense                                                                | 49,200      |              |
| Supplies expense                                                                   | 23,800      |              |
| Miscellaneous expense                                                              | 32,000      |              |
| Total expenses                                                                     |             | (1,700,000)  |
| Net income                                                                         |             | \$ 800,000   |

| <b>Ocean Cruiser<br/>Statement of Stockholders' Equity<br/>For the Year Ended February 28, 20Y7</b> |                 |                      |             |
|-----------------------------------------------------------------------------------------------------|-----------------|----------------------|-------------|
|                                                                                                     | Common<br>Stock | Retained<br>Earnings | Total       |
| Balances, March 1, 20Y6                                                                             | \$75,000        | \$ 300,000           | \$ 375,000  |
| Issued common stock                                                                                 | 20,000          |                      | 20,000      |
| Net income for the year                                                                             |                 | 800,000              | 800,000     |
| Dividends                                                                                           |                 | (150,000)            | (150,000)   |
| Balances, February 28, 20Y7                                                                         | \$95,000        | \$ 950,000           | \$1,045,000 |

| <b>Ocean Cruiser<br/>Balance Sheet<br/>February 28, 20Y7</b> |           |             |
|--------------------------------------------------------------|-----------|-------------|
| <b>Assets</b>                                                |           |             |
| Cash                                                         |           | \$ 137,000  |
| Accounts receivable                                          |           | 240,000     |
| Supplies                                                     |           | 8,000       |
| Land                                                         |           | 750,000     |
| Total assets                                                 |           | \$1,135,000 |
| <b>Liabilities</b>                                           |           |             |
| Accounts payable                                             |           | \$ 90,000   |
| <b>Stockholders' Equity</b>                                  |           |             |
| Common stock                                                 | \$ 95,000 |             |
| Retained earnings                                            | 950,000   |             |
| Total stockholders' equity                                   |           | 1,045,000   |
| Total liabilities and stockholders' equity                   |           | \$1,135,000 |

4. Net income (or net loss) appears on both the income statement and the statement of stockholders' equity. For Ocean Cruiser, net income for the year of \$800,000 appears on the income statement and statement of stockholders' equity.

## Prob. 1–3B

| Bronco Consulting<br>Income Statement<br>For the Month Ended August 31, 20Y1 |          |            |
|------------------------------------------------------------------------------|----------|------------|
| Fees earned                                                                  |          | \$ 125,000 |
| Expenses:                                                                    |          |            |
| Salaries expense                                                             | \$58,000 |            |
| Rent expense                                                                 | 27,000   |            |
| Auto expense                                                                 | 15,500   |            |
| Supplies expense                                                             | 6,100    |            |
| Miscellaneous expense                                                        | 7,500    |            |
| Total expenses                                                               |          | (114,100)  |
| Net income                                                                   |          | \$ 10,900  |

| Bronco Consulting<br>Statement of Stockholders' Equity<br>For the Month Ended August 31, 20Y1 |                 |                      |          |
|-----------------------------------------------------------------------------------------------|-----------------|----------------------|----------|
|                                                                                               | Common<br>Stock | Retained<br>Earnings | Total    |
| Balances, August 1, 20Y1                                                                      | \$ 0            | \$ 0                 | \$ 0     |
| Issued common stock                                                                           | 75,000          |                      | 75,000   |
| Net income for August                                                                         |                 | 10,900               | 10,900   |
| Dividends                                                                                     |                 | (5,000)              | (5,000)  |
| Balances, August 31, 20Y1                                                                     | \$75,000        | \$ 5,900             | \$80,900 |

| Bronco Consulting<br>Balance Sheet<br>August 31, 20Y1 |          |          |
|-------------------------------------------------------|----------|----------|
| <b>Assets</b>                                         |          |          |
| Cash                                                  |          | \$48,000 |
| Accounts receivable                                   |          | 33,000   |
| Supplies                                              |          | 2,900    |
| Total assets                                          |          | \$83,900 |
| <b>Liabilities</b>                                    |          |          |
| Accounts payable                                      |          | \$ 3,000 |
| <b>Stockholders' Equity</b>                           |          |          |
| Common stock                                          | \$75,000 |          |
| Retained earnings                                     | 5,900    |          |
| Total stockholders' equity                            |          | 80,900   |
| Total liabilities and stockholders' equity            |          | \$83,900 |

## Prob. 1–3B (Concluded)

## 4. Optional

| <b>Bronco Consulting</b><br><b>Statement of Cash Flows</b><br><b>For the Month Ended August 31, 20Y1</b> |           |                   |
|----------------------------------------------------------------------------------------------------------|-----------|-------------------|
| <b>Cash flows from (used for) operating activities:</b>                                                  |           |                   |
| Cash received from customers                                                                             | \$ 92,000 |                   |
| Cash paid for expenses and to creditors*                                                                 | (114,000) |                   |
| Net cash flows used for operating activities                                                             |           | <b>\$(22,000)</b> |
| Cash flows from (used for) investing activities                                                          |           | <b>0</b>          |
| Cash flows from (used for) financing activities:                                                         |           |                   |
| Cash received from issuing common stock                                                                  | \$ 75,000 |                   |
| Cash paid as dividends                                                                                   | (5,000)   |                   |
| Net cash flows from financing activities                                                                 |           | <b>70,000</b>     |
| Net increase in cash                                                                                     |           | <b>\$ 48,000</b>  |
| Cash balance, August 1, 20Y1                                                                             |           | <b>0</b>          |
| Cash balance, August 31, 20Y1                                                                            |           | <b>\$ 48,000</b>  |

\* \$27,000 + \$6,000 + \$23,000 + \$58,000; these amounts are taken from the Cash column shown in the problem.

Prob. 1-4B

| 1.   | Assets   |            | = Liabilities + |                | Stockholders' Equity |               |             |                 |             |                 |            |
|------|----------|------------|-----------------|----------------|----------------------|---------------|-------------|-----------------|-------------|-----------------|------------|
|      | Cash     | + Supplies | Accts. Payable  | + Common Stock | - Dividends          | + Sales Comm. | - Rent Exp. | - Salaries Exp. | - Auto Exp. | - Supplies Exp. | Misc. Exp. |
| a.   | + 24,000 |            |                 | + 24,000       |                      |               | - 3,600     |                 |             |                 |            |
| b.   | - 3,600  |            |                 |                |                      |               | - 3,600     |                 |             |                 |            |
| Bal. | 20,400   |            |                 | 24,000         |                      |               |             |                 |             |                 |            |
| c.   | - 1,950  |            |                 |                |                      |               |             |                 | - 1,350     |                 | - 600      |
| Bal. | 18,450   |            |                 | 24,000         |                      |               | - 3,600     |                 | - 1,350     |                 | - 600      |
| d.   |          | + 1,200    | + 1,200         |                |                      |               | - 3,600     |                 | - 1,350     |                 | - 600      |
| Bal. | 18,450   | 1,200      | 1,200           | 24,000         |                      |               |             |                 |             |                 |            |
| e.   | + 19,800 |            |                 |                |                      | + 19,800      |             |                 |             |                 |            |
| Bal. | 38,250   | 1,200      | 1,200           | 24,000         |                      | 19,800        | - 3,600     |                 | - 1,350     |                 | - 600      |
| f.   | - 750    |            | - 750           |                |                      |               |             |                 |             |                 |            |
| Bal. | 37,500   | 1,200      | 450             | 24,000         |                      | 19,800        | - 3,600     |                 | - 1,350     |                 | - 600      |
| g.   | - 2,500  |            |                 |                |                      |               |             | - 2,500         |             |                 |            |
| Bal. | 35,000   | 1,200      | 450             | 24,000         |                      | 19,800        | - 3,600     | - 2,500         | - 1,350     |                 | - 600      |
| h.   | - 3,500  |            |                 |                | - 3,500              |               |             |                 |             |                 |            |
| Bal. | 31,500   | 1,200      | 450             | 24,000         | - 3,500              | 19,800        | - 3,600     | - 2,500         | - 1,350     |                 | - 600      |
| i.   |          | - 900      |                 |                |                      |               |             |                 |             | - 900           |            |
| Bal. | 31,500   | 300        | 450             | 24,000         | - 3,500              | 19,800        | - 3,600     | - 2,500         | - 1,350     | - 900           | - 600      |

Prob. 1–4B (Concluded)

2.

| Custom Realty<br>Income Statement<br>For the Month Ended April 30, 20Y8 |         |          |
|-------------------------------------------------------------------------|---------|----------|
| Sales commissions                                                       |         | \$19,800 |
| Expenses:                                                               |         |          |
| Rent expense                                                            | \$3,600 |          |
| Salaries expense                                                        | 2,500   |          |
| Automobile expense                                                      | 1,350   |          |
| Supplies expense                                                        | 900     |          |
| Miscellaneous expense                                                   | 600     |          |
| Total expenses                                                          |         | (8,950)  |
| Net income                                                              |         | \$10,850 |

| Custom Realty<br>Statement of Stockholders' Equity<br>For the Month Ended April 30, 20Y8 |                 |                      |          |
|------------------------------------------------------------------------------------------|-----------------|----------------------|----------|
|                                                                                          | Common<br>Stock | Retained<br>Earnings | Total    |
| Balances, April 1, 20Y8                                                                  | \$ 0            | \$ 0                 | \$ 0     |
| Issued common stock                                                                      | 24,000          |                      | 24,000   |
| Net income for April                                                                     |                 | 10,850               | 10,850   |
| Dividends                                                                                |                 | (3,500)              | (3,500)  |
| Balances, April 30, 20Y8                                                                 | \$24,000        | \$ 7,350             | \$31,350 |

| Custom Realty<br>Balance Sheet<br>April 30, 20Y8 |          |          |
|--------------------------------------------------|----------|----------|
| <b>Assets</b>                                    |          |          |
| Cash                                             |          | \$31,500 |
| Supplies                                         |          | 300      |
| Total assets                                     |          | \$31,800 |
| <b>Liabilities</b>                               |          |          |
| Accounts payable                                 |          | \$ 450   |
| <b>Stockholders' Equity</b>                      |          |          |
| Common stock                                     | \$24,000 |          |
| Retained earnings                                | 7,350    |          |
| Total stockholders' equity                       |          | 31,350   |
| Total liabilities and stockholders' equity       |          | \$31,800 |

**Prob. 1–5B**

|    |               |   |                     |   |          |   |             |   |                      |   |                   |   |                   |
|----|---------------|---|---------------------|---|----------|---|-------------|---|----------------------|---|-------------------|---|-------------------|
| 1. | <u>Assets</u> |   |                     |   |          | = | Liabilities | + | Stockholders' Equity |   |                   |   |                   |
|    | Cash          | + | Accounts Receivable | + | Supplies | + | Land        | = | Accounts Payable     | + | Common Stock      | + | Retained Earnings |
|    | \$39,000      | + | \$80,000            | + | \$11,000 | + | \$50,000    | = | \$31,500             | + | \$50,000          | + | Retained Earnings |
|    |               |   |                     |   |          |   | \$180,000   | = | \$81,500             | + | Retained Earnings |   |                   |
|    |               |   |                     |   |          |   | \$98,500    | = | Retained Earnings    |   |                   |   |                   |

**Prob. 1–5B (Continued)**

| 2.   | Assets   |               |            |          | = Liabilities +  | Stockholders' Equity |                     |             |
|------|----------|---------------|------------|----------|------------------|----------------------|---------------------|-------------|
|      | Cash     | + Accts. Rec. | + Supplies | + Land   | = Accts. Payable | + Common Stock       | + Retained Earnings | – Dividends |
| Bal. | 39,000   | 80,000        | 11,000     | 50,000   | 31,500           | 50,000               | 98,500              |             |
| a.   | + 21,000 |               |            |          |                  | + 21,000             |                     |             |
| Bal. | 60,000   | 80,000        | 11,000     | 50,000   | 31,500           | 71,000               | 98,500              |             |
| b.   | – 35,000 |               |            | + 35,000 |                  |                      |                     |             |
| Bal. | 25,000   | 80,000        | 11,000     | 85,000   | 31,500           | 71,000               | 98,500              |             |
| c.   | – 4,000  |               |            |          |                  |                      |                     |             |
| Bal. | 21,000   | 80,000        | 11,000     | 85,000   | 31,500           | 71,000               | 98,500              |             |
| d.   |          | + 72,000      |            |          |                  |                      |                     |             |
| Bal. | 21,000   | 152,000       | 11,000     | 85,000   | 31,500           | 71,000               | 98,500              |             |
| e.   | – 20,000 |               |            |          | – 20,000         |                      |                     |             |
| Bal. | 1,000    | 152,000       | 11,000     | 85,000   | 11,500           | 71,000               | 98,500              |             |
| f.   |          |               | + 8,000    |          | + 8,000          |                      |                     |             |
| Bal. | 1,000    | 152,000       | 19,000     | 85,000   | 19,500           | 71,000               | 98,500              |             |
| g.   | + 38,000 |               |            |          |                  |                      |                     |             |
| Bal. | 39,000   | 152,000       | 19,000     | 85,000   | 19,500           | 71,000               | 98,500              |             |
| h.   | + 77,000 | – 77,000      |            |          |                  |                      |                     |             |
| Bal. | 116,000  | 75,000        | 19,000     | 85,000   | 19,500           | 71,000               | 98,500              |             |
| i.   |          |               |            |          | + 29,450         |                      |                     |             |
| Bal. | 116,000  | 75,000        | 19,000     | 85,000   | 48,950           | 71,000               | 98,500              |             |
| j.   | – 29,200 |               |            |          |                  |                      |                     |             |
| Bal. | 86,800   | 75,000        | 19,000     | 85,000   | 48,950           | 71,000               | 98,500              |             |
| k.   |          |               | – 7,200    |          |                  |                      |                     |             |
| Bal. | 86,800   | 75,000        | 11,800     | 85,000   | 48,950           | 71,000               | 98,500              |             |
| l.   | – 5,000  |               |            |          |                  |                      |                     | – 5,000     |
| Bal. | 81,800   | 75,000        | 11,800     | 85,000   | 48,950           | 71,000               | 98,500              | – 5,000     |

## Prob. 1–5B (Continued)

| Stockholders' Equity (Continued) |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
|----------------------------------|----------|---------|----------|---|----------|---------|----------|---|---------|---------|-------|---------|-----------|---------|-------|
|                                  | Dry      |         | Dry      |   | Wages    |         | Supplies |   | Rent    |         | Truck |         | Utilities |         | Misc. |
| +                                | Cleaning | -       | Cleaning | - | Exp.     | -       | Exp.     | - | Exp.    | -       | Exp.  | -       | Exp.      | -       | Exp.  |
| Revenue                          | Exp.     |         | Exp.     |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| a.                               |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| b.                               |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| c.                               |          |         |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| Bal.                             |          |         |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| d.                               | +        | 72,000  |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 72,000  |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| e.                               |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 72,000  |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| f.                               |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 72,000  |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| g.                               | +        | 38,000  |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 110,000 |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| h.                               |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 110,000 |          |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| i.                               |          |         | - 29,450 |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 110,000 | - 29,450 |   |          |         |          |   | - 4,000 |         |       |         |           |         |       |
| j.                               |          |         |          |   | - 24,000 |         |          |   |         | - 2,100 |       | - 1,800 |           | - 1,300 |       |
| Bal.                             |          | 110,000 | - 29,450 |   | - 24,000 |         |          |   | - 4,000 | - 2,100 |       | - 1,800 |           | - 1,300 |       |
| k.                               |          |         |          |   |          | - 7,200 |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 110,000 | - 29,450 |   | - 24,000 | - 7,200 |          |   | - 4,000 | - 2,100 |       | - 1,800 |           | - 1,300 |       |
| l.                               |          |         |          |   |          |         |          |   |         |         |       |         |           |         |       |
| Bal.                             |          | 110,000 | - 29,450 |   | - 24,000 | - 7,200 |          |   | - 4,000 | - 2,100 |       | - 1,800 |           | - 1,300 |       |

Prob. 1–5B (Continued)

| <b>Bev's Dry Cleaners</b><br><b>Income Statement</b><br><b>For the Month Ended November 30, 20Y3</b> |          |           |
|------------------------------------------------------------------------------------------------------|----------|-----------|
| Dry cleaning revenue                                                                                 |          | \$110,000 |
| Expenses:                                                                                            |          |           |
| Dry cleaning expense                                                                                 | \$29,450 |           |
| Wages expense                                                                                        | 24,000   |           |
| Supplies expense                                                                                     | 7,200    |           |
| Rent expense                                                                                         | 4,000    |           |
| Truck expense                                                                                        | 2,100    |           |
| Utilities expense                                                                                    | 1,800    |           |
| Miscellaneous expense                                                                                | 1,300    |           |
| Total expenses                                                                                       |          | (69,850)  |
| Net income                                                                                           |          | \$ 40,150 |

| <b>Bev's Dry Cleaners</b><br><b>Statement of Stockholders' Equity</b><br><b>For the Month Ended November 30, 20Y3</b> |                 |                      |           |
|-----------------------------------------------------------------------------------------------------------------------|-----------------|----------------------|-----------|
|                                                                                                                       | Common<br>Stock | Retained<br>Earnings | Total     |
| Balances, November 1, 20Y3                                                                                            | \$50,000        | \$ 98,500            | \$148,500 |
| Issued common stock                                                                                                   | 21,000          |                      | 21,000    |
| Net income for November                                                                                               |                 | 40,150               | 40,150    |
| Dividends                                                                                                             |                 | (5,000)              | (5,000)   |
| Balances, November 30, 20Y3                                                                                           | \$71,000        | \$133,650            | \$204,650 |

| <b>Bev's Dry Cleaners</b><br><b>Balance Sheet</b><br><b>November 30, 20Y3</b> |           |           |
|-------------------------------------------------------------------------------|-----------|-----------|
| <b>Assets</b>                                                                 |           |           |
| Cash                                                                          |           | \$ 81,800 |
| Accounts receivable                                                           |           | 75,000    |
| Supplies                                                                      |           | 11,800    |
| Land                                                                          |           | 85,000    |
| Total assets                                                                  |           | \$253,600 |
| <b>Liabilities</b>                                                            |           |           |
| Accounts payable                                                              |           | \$ 48,950 |
| <b>Stockholders' Equity</b>                                                   |           |           |
| Common stock                                                                  | \$ 71,000 |           |
| Retained earnings                                                             | 133,650   |           |
| Total stockholders' equity                                                    |           | 204,650   |
| Total liabilities and stockholders' equity                                    |           | \$253,600 |

## Prob. 1–5B (Concluded)

## 4. Optional

| <b>Bev's Dry Cleaners</b><br><b>Statement of Cash Flows</b><br><b>For the Month Ended November 30, 20Y3</b> |           |           |
|-------------------------------------------------------------------------------------------------------------|-----------|-----------|
| <b>Cash flows from (used for) operating activities:</b>                                                     |           |           |
| Cash received from customers*                                                                               | \$115,000 |           |
| Cash paid for expenses and to creditors**                                                                   | (53,200)  |           |
| Net cash flows from operating activities                                                                    |           | \$ 61,800 |
| <b>Cash flows from (used for) investing activities:</b>                                                     |           |           |
| Cash paid for acquisition of land                                                                           |           | (35,000)  |
| <b>Cash flows from (used for) financing activities:</b>                                                     |           |           |
| Cash received from issuing common stock                                                                     | \$ 21,000 |           |
| Cash paid as dividends                                                                                      | (5,000)   |           |
| Net cash flows from financing activities                                                                    |           | 16,000    |
| Net increase in cash                                                                                        |           | \$ 42,800 |
| Cash balance, November 1, 20Y3                                                                              |           | 39,000    |
| Cash balance, November 30, 20Y3                                                                             |           | \$ 81,800 |

\* \$38,000 + \$77,000; these amounts are taken from the Cash column of the spreadsheet in Part 2.

\*\* \$4,000 + \$20,000 + \$29,200; these amounts are taken from the Cash column of the spreadsheet in Part 2.

**Prob. 1–6B**

- a. Wages expense, \$203,200 ( $\$288,000 - \$48,000 - \$17,600 - \$14,400 - \$4,800$ )
- b. Net income, \$112,000 ( $\$400,000 - \$288,000$ )
- c. Common stock, \$160,000; from statement of cash flows
- d. Net income for May, \$112,000; from (b)
- e. Dividends, \$64,000; from statement of cash flows
- f. Increase in retained earnings, \$48,000 ( $\$112,000 - \$64,000$ )
- g. Total stockholders' equity, \$208,000 ( $\$160,000 + \$48,000$ )
- h. Land, \$120,000; from statement of cash flows
- i. Total assets, \$256,000 ( $\$123,200 + \$12,800 + \$120,000$ )
- j. Common stock, \$160,000; from statement of cash flows
- k. Retained earnings, \$48,000; same as (f)
- l. Total stockholders' equity, \$208,000; same as (g)
- m. Total liabilities and stockholders' equity, \$256,000 ( $\$48,000 + \$208,000$ )
- n. Cash received from customers, \$400,000; this is the same as fees earned since there are no accounts receivable.
- o. Net cash flows from operating activities, \$147,200 ( $\$400,000 - \$252,800$ )
- p. Net cash flows from financing activities, \$96,000 ( $\$160,000 - \$64,000$ )
- q. Net increase in cash, \$123,200 ( $\$147,200 - \$120,000 + \$96,000$ )
- r. Cash as of May 31, 20Y6, \$123,200; same as (q) since Atlas Realty was organized on May 1, 20Y6; also the cash balance on the balance sheet.

**This Page Not Used.**

# CONTINUING PROBLEM

| 1.   |    | Assets |       |                |       |          | =   | Liabilities       |     | +               | Stockholders' Equity |           |   |                |       |
|------|----|--------|-------|----------------|-------|----------|-----|-------------------|-----|-----------------|----------------------|-----------|---|----------------|-------|
|      |    | Cash   | +     | Accts.<br>Rec. | +     | Supplies | =   | Accts.<br>Payable | +   | Common<br>Stock | -                    | Dividends | + | Fees<br>Earned |       |
| June | 1  | +      | 4,000 |                |       |          |     |                   |     | +               | 4,000                |           |   |                |       |
| June | 2  | +      | 3,500 |                |       |          |     |                   |     |                 |                      |           |   | +              | 3,500 |
| Bal. |    |        | 7,500 |                |       |          |     |                   |     | 4,000           |                      |           |   |                | 3,500 |
| June | 2  | -      | 800   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 6,700 |                |       |          |     |                   |     | 4,000           |                      |           |   |                | 3,500 |
| June | 4  |        |       |                |       | +        | 350 | +                 | 350 |                 |                      |           |   |                |       |
| Bal. |    |        | 6,700 |                |       |          | 350 |                   | 350 | 4,000           |                      |           |   |                | 3,500 |
| June | 6  | -      | 500   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 6,200 |                |       |          | 350 |                   | 350 | 4,000           |                      |           |   |                | 3,500 |
| June | 8  | -      | 675   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 5,525 |                |       |          | 350 |                   | 350 | 4,000           |                      |           |   |                | 3,500 |
| June | 12 | -      | 350   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 5,175 |                |       |          | 350 |                   | 350 | 4,000           |                      |           |   |                | 3,500 |
| June | 13 | -      | 100   |                |       |          |     | -                 | 100 |                 |                      |           |   |                |       |
| Bal. |    |        | 5,075 |                |       |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 3,500 |
| June | 16 | +      | 300   |                |       |          |     |                   |     |                 |                      |           |   | +              | 300   |
| Bal. |    |        | 5,375 |                |       |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 3,800 |
| June | 22 |        |       | +              | 1,000 |          |     |                   |     |                 |                      |           |   | +              | 1,000 |
| Bal. |    |        | 5,375 |                | 1,000 |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 4,800 |
| June | 25 | +      | 500   |                |       |          |     |                   |     |                 |                      |           |   | +              | 500   |
| Bal. |    |        | 5,875 |                | 1,000 |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 5,300 |
| June | 29 | -      | 240   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 5,635 |                | 1,000 |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 5,300 |
| June | 30 | +      | 900   |                |       |          |     |                   |     |                 |                      |           |   | +              | 900   |
| Bal. |    |        | 6,535 |                | 1,000 |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 6,200 |
| June | 30 | -      | 400   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 6,135 |                | 1,000 |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 6,200 |
| June | 30 | -      | 300   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 5,835 |                | 1,000 |          | 350 |                   | 250 | 4,000           |                      |           |   |                | 6,200 |
| June | 30 |        |       |                |       | -        | 180 |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 5,835 |                | 1,000 |          | 170 |                   | 250 | 4,000           |                      |           |   |                | 6,200 |
| June | 30 | -      | 415   |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 5,420 |                | 1,000 |          | 170 |                   | 250 | 4,000           |                      |           |   |                | 6,200 |
| June | 30 | -      | 1,000 |                |       |          |     |                   |     |                 |                      |           |   |                |       |
| Bal. |    |        | 4,420 |                | 1,000 |          | 170 |                   | 250 | 4,000           |                      |           |   |                | 6,200 |
| June | 30 | -      | 500   |                |       |          |     |                   |     |                 | -                    | 500       |   |                |       |
| Bal. |    |        | 3,920 |                | 1,000 |          | 170 |                   | 250 | 4,000           | -                    | 500       |   |                | 6,200 |

### Continuing Problem (Continued)

|      |    | Stockholders' Equity (Continued) |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
|------|----|----------------------------------|-------|------------------------|-----|------------------------|-----|--------------------------|-----|---------------|-----|-------------------|-----|------------------|-----|---------------|
|      |    | Music<br>Exp.                    |       | Office<br>Rent<br>Exp. |     | Equip.<br>Rent<br>Exp. |     | Adver-<br>tising<br>Exp. |     | Wages<br>Exp. |     | Utilities<br>Exp. |     | Supplies<br>Exp. |     | Misc.<br>Exp. |
|      | -  |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| June | 1  |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| June | 2  |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| June | 2  |                                  |       | -                      | 800 |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    |                                  |       | -                      | 800 |                        |     |                          |     |               |     |                   |     |                  |     |               |
| June | 4  |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    |                                  |       | -                      | 800 |                        |     |                          |     |               |     |                   |     |                  |     |               |
| June | 6  |                                  |       |                        |     |                        |     | -                        | 500 |               |     |                   |     |                  |     |               |
| Bal. |    |                                  |       | -                      | 800 |                        |     | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 8  |                                  |       |                        |     | -                      | 675 |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    |                                  |       | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 12 | -                                | 350   |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 350   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 13 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 350   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 16 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 350   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 22 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 350   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 25 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 350   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 29 | -                                | 240   |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 590   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 30 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 590   | -                      | 800 | -                      | 675 | -                        | 500 |               |     |                   |     |                  |     |               |
| June | 30 |                                  |       |                        |     |                        |     |                          |     | -             | 400 |                   |     |                  |     |               |
| Bal. |    | -                                | 590   | -                      | 800 | -                      | 675 | -                        | 500 | -             | 400 |                   |     |                  |     |               |
| June | 30 |                                  |       |                        |     |                        |     |                          |     |               |     | -                 | 300 |                  |     |               |
| Bal. |    | -                                | 590   | -                      | 800 | -                      | 675 | -                        | 500 | -             | 400 | -                 | 300 |                  |     |               |
| June | 30 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     | -                | 180 |               |
| Bal. |    | -                                | 590   | -                      | 800 | -                      | 675 | -                        | 500 | -             | 400 | -                 | 300 | -                | 180 |               |
| June | 30 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     | -             |
| Bal. |    | -                                | 590   | -                      | 800 | -                      | 675 | -                        | 500 | -             | 400 | -                 | 300 | -                | 180 | -             |
| June | 30 | -                                | 1,000 |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 1,590 | -                      | 800 | -                      | 675 | -                        | 500 | -             | 400 | -                 | 300 | -                | 180 | -             |
| June | 30 |                                  |       |                        |     |                        |     |                          |     |               |     |                   |     |                  |     |               |
| Bal. |    | -                                | 1,590 | -                      | 800 | -                      | 675 | -                        | 500 | -             | 400 | -                 | 300 | -                | 180 | -             |

Continuing Problem (Concluded)

| <b>PS Music</b><br><b>Income Statement</b><br><b>For the Month Ended June 30, 20Y5</b> |                |                 |
|----------------------------------------------------------------------------------------|----------------|-----------------|
| <b>Fees earned:</b>                                                                    |                | <b>\$ 6,200</b> |
| <b>Expenses:</b>                                                                       |                |                 |
| <b>Music expense</b>                                                                   | <b>\$1,590</b> |                 |
| <b>Office rent expense</b>                                                             | <b>800</b>     |                 |
| <b>Equipment rent expense</b>                                                          | <b>675</b>     |                 |
| <b>Advertising expense</b>                                                             | <b>500</b>     |                 |
| <b>Wages expense</b>                                                                   | <b>400</b>     |                 |
| <b>Utilities expense</b>                                                               | <b>300</b>     |                 |
| <b>Supplies expense</b>                                                                | <b>180</b>     |                 |
| <b>Miscellaneous expense</b>                                                           | <b>415</b>     |                 |
| <b>Total expenses</b>                                                                  |                | <b>(4,860)</b>  |
| <b>Net income</b>                                                                      |                | <b>\$ 1,340</b> |

| <b>PS Music</b><br><b>Statement of Stockholders' Equity</b><br><b>For the Month Ended June 30, 20Y5</b> |                         |                              |                |
|---------------------------------------------------------------------------------------------------------|-------------------------|------------------------------|----------------|
|                                                                                                         | <b>Common<br/>Stock</b> | <b>Retained<br/>Earnings</b> | <b>Total</b>   |
| <b>Balances, June 1, 20Y5</b>                                                                           | <b>\$ 0</b>             | <b>\$ 0</b>                  | <b>\$ 0</b>    |
| <b>Issued common stock</b>                                                                              | <b>4,000</b>            |                              | <b>4,000</b>   |
| <b>Net income</b>                                                                                       |                         | <b>1,340</b>                 | <b>1,340</b>   |
| <b>Dividends</b>                                                                                        |                         | <b>(500)</b>                 | <b>(500)</b>   |
| <b>Balances, June 30, 20Y5</b>                                                                          | <b>\$4,000</b>          | <b>\$ 840</b>                | <b>\$4,840</b> |

| <b>PS Music</b><br><b>Balance Sheet</b><br><b>June 30, 20Y5</b> |                |                |
|-----------------------------------------------------------------|----------------|----------------|
| <b>Assets</b>                                                   |                |                |
| <b>Cash</b>                                                     |                | <b>\$3,920</b> |
| <b>Accounts receivable</b>                                      |                | <b>1,000</b>   |
| <b>Supplies</b>                                                 |                | <b>170</b>     |
| <b>Total assets</b>                                             |                | <b>\$5,090</b> |
| <b>Liabilities</b>                                              |                |                |
| <b>Accounts payable</b>                                         |                | <b>\$ 250</b>  |
| <b>Stockholders' Equity</b>                                     |                |                |
| <b>Common stock</b>                                             | <b>\$4,000</b> |                |
| <b>Retained earnings</b>                                        | <b>840</b>     |                |
| <b>Total stockholders' equity</b>                               |                | <b>4,840</b>   |
| <b>Total liabilities and stockholders' equity</b>               |                | <b>\$5,090</b> |

**MAKE A DECISION****MAD 1–1**

$$\text{a. Ratio of Liabilities to Stockholders' Equity} = \frac{\text{Total Liabilities}}{\text{Total Stockholders' Equity}}$$

$$\text{Amazon: } \frac{\$282,304}{\$138,245} = 2.04$$

$$\text{Best Buy: } \frac{\$14,484}{\$3,020} = 4.80$$

- b. Amazon's ratio is 2.04, which means the total liabilities are over two times as great as the stockholders' equity. For Best Buy, the ratio is even higher at 4.80, which is almost five times greater than stockholders' equity. Thus, the margin of protection for creditors is better for Amazon than it is for Best Buy.

**MAD 1–2**

$$\text{a. Ratio of Liabilities to Stockholders' Equity} = \frac{\text{Total Liabilities}}{\text{Total Stockholders' Equity}}$$

$$\text{Year 1: } \frac{\$30,946}{\$11,833} = 2.62$$

$$\text{Year 2: } \frac{\$36,808}{\$14,440} = 2.55$$

$$\text{Year 3: } \frac{\$40,984}{\$12,827} = 3.20$$

- b. The ratio of liabilities to stockholders' equity for Target decreased from 2.62 in Year 1 to 2.55 in Year 2, but increased to 3.20 in Year 3. Thus, the protection to creditors increased slightly in Year 2, but decreased in Year 3.

**MAD 1–3**

$$\text{a. Ratio of Liabilities to Stockholders' Equity} = \frac{\text{Total Liabilities}}{\text{Total Stockholders' Equity}}$$

$$\text{Year 1: } \frac{\$154,943}{\$81,552} = 1.90$$

$$\text{Year 2: } \frac{\$164,965}{\$87,531} = 1.88$$

$$\text{Year 3: } \frac{\$152,969}{\$91,891} = 1.66$$

- b. The ratio of liabilities to stockholders' equity for Walmart decreased from 1.90 in Year 1 to 1.66 in Year 3, causing the margin of protection to creditors to increase.

**MAD 1–4**

The ratios of liabilities to stockholders' equity are summarized below for Target (MAD 1–2) and Walmart (MAD 1–3).

|         | Year 3 | Year 2 | Year 1 |
|---------|--------|--------|--------|
| Target  | 3.20   | 2.55   | 2.62   |
| Walmart | 1.66   | 1.88   | 1.90   |

Target's ratio of liabilities to stockholders' equity is more than that of Walmart for all three years. While Walmart's ratios are decreasing in all three years, Target's ratios increased from 2.62 to 3.20 during the three years. Thus, Walmart's creditors have more protection than Target's creditors.

**MAD 1–5**

a. **Ratio of Liabilities to Stockholders' Equity** = 
$$\frac{\text{Total Liabilities}}{\text{Total Stockholders' Equity}}$$

**Wendy's:** 
$$\frac{\$4,665}{\$436} = 10.7$$

**Chipotle:** 
$$\frac{\$4,356}{\$2,297} = 1.9$$

- b. The ratio of liabilities to stockholders' equity is 10.7 for Wendy's. This ratio suggests that creditors have a high risk with their investments. That is, the small level of stockholders' equity provides a low margin of protection for creditors.
- c. Chipotle's ratio of liabilities to stockholders' equity of 1.9 suggests that Chipotle does not use as much debt as Wendy's to finance its operations. Thus, Chipotle's creditors have more protection than Wendy's creditors.

## TAKE IT FURTHER

### TIF 1–1

1. The car repair is a personal expense and is Marco's personal responsibility. By using partnership funds to pay for the repair, Marco is behaving unethically because he is violating the business entity assumption. The business entity assumption treats the business as a separate entity from its owners. By taking money from the partnership for a personal expense, Marco is effectively stealing from his partners.
2. The partnership's net income will be reduced by the \$2,000 Marco has taken. This will reduce the amount of net income available to Marco's partners.
3. Marco could ask his partners for a loan from the partnership. The loan could be repaid out of his salary or from his share of the partnership income.

## TIF 1–2

1. Acceptable professional conduct requires that Colleen Fernandez supply First Federal Bank with all the relevant financial statements necessary for the bank to make an informed decision. Therefore, Colleen should provide the complete set of financial statements. These can be supplemented with a discussion of the net loss in the past year or other data explaining why granting the loan is a good investment for the bank.
2. a. Owners are generally willing to provide bankers with information about the operating and financial condition of the business, such as the following:
  - Operating Information:
    - Description of business operations
    - Results of past operations
    - Preliminary results of current operations
    - Plans for future operations
  - Financial Condition:
    - List of assets and liabilities (balance sheet)
    - Estimated current values of assets
    - Owner's personal investment in the business
    - Owner's commitment to invest additional funds in the business

Owners are normally reluctant to provide the following types of information to bankers:

- **Proprietary Operating Information.** Such information, which might hurt the business if it becomes known by competitors, might include special processes used by the business or future plans to expand operations into areas that are not currently served by a competitor.
  - **Personal Financial Information.** Owners may have little choice here because banks often require owners of small businesses to pledge their personal assets as security for a business loan. Personal financial information requested by bankers often includes the owner's net worth, salary, and other income. In addition, bankers usually request information about factors that might affect the personal financial condition of the owner. For example, a pending divorce by the owner might significantly affect the owner's personal wealth.
- b. Bankers typically want as much information as possible about the ability of the business and the owner to repay the loan with interest. Examples of such information are described above.
  - c. Both bankers and business owners share the common interest of the business doing well and being successful. If the business is successful, the bankers will receive their loan payments on time with interest, and the owners will increase their personal wealth.

**TIF 1–3**

**A sample solution based on Amazon’s Form 10-K for the fiscal year ended December 31, 2022, follows:**

- 1. Amazon.com, Inc.**
- 2. Seattle, Washington**
- 3. Andrew R. Jassy, President and Chief Executive Officer**
- 4. Amazon.com is “primarily” a merchandising company. Amazon does manufacture some electronic products such as the Kindle and Fire tablet. Amazon also provides technology services through its Amazon Web Services (AWS). However, the majority of Amazon’s revenues are generated from retail sales of consumer products.**
- 5. We seek to be Earth’s most customer-centric company. . . . We serve consumers through our online and physical stores and focus on selection, price, and convenience. . . . We offer programs that enable sellers to grow their businesses, sell their products in our stores, and fulfill orders through us. . . . We serve developers and enterprises of all sizes, including start-ups, government agencies, and academic institutions, through AWS, which offers a broad set of on-demand technology services, including compute, storage, database, analytics, and machine learning, and other services. . . . We offer programs that allow authors, independent publishers, musicians, filmmakers, Twitch streamers, skill and app developers, and others to publish and sell content. . . . We provide advertising services to sellers, vendors, publishers, authors, and others, through programs such as sponsored ads, display, and video advertising.**
- 6. Statement of cash flows, statement of operations (income statement), statement of comprehensive income (loss), balance sheet, and statement of stockholders’ equity.**

***Note to Instructor:* The statement of comprehensive income (loss) is discussed in Appendix B, Topic 2, “Reporting Unusual Items and Comprehensive Income.”**

**TIF 1–4****Example Memo**

**To: Teacher**  
**From: Student**  
**Date: Current Date**  
**Subject: Causes of Accounting Fraud**

**Business and accounting fraud typically result from either a failure of individual character or a culture of greed within an organization. Managers and accountants often face pressure to meet or exceed a company’s financial goals. At times, supervisors can place pressure on individuals to violate accounting standards to improve a company’s reported financial results. Individuals who give in to these pressures exhibit a failure of individual character. In other situations, a company may indirectly encourage employees to violate accounting rules as part of their job. This occurs in organizations that do not value ethical decision making or fair financial reporting and exhibit a culture of ethical indifference.**

**TIF 1–5**

The difference in the two bank balances, \$55,000 (\$80,000 – \$25,000), may not be pure profit from an accounting perspective. To determine the accounting profit for the six-month period, the revenues for the period would need to be matched with the related expenses. The revenues minus the expenses would indicate whether the business generated net income (profit) or a net loss for the period. Using only the difference between the two bank account balances ignores such factors as amounts due from customers (receivables), liabilities (accounts payable) that need to be paid for wages or other operating expenses, additional investments that Dr. Cousins may have made in the business during the period, or dividends paid during the period that Dr. Cousins might have taken for personal reasons unrelated to the business.

Some businesses that have few, if any, receivables or payables may use a “cash” basis of accounting. The cash basis of accounting ignores receivables and payables because they are assumed to be insignificant in amount. However, even with the cash basis of accounting, additional investments during the period and any dividends paid during the period have to be considered in determining the net income (profit) or net loss for the period.

**TIF 1–6 Excel**

| Row Labels           | Sum of Amount          |
|----------------------|------------------------|
| Asset                | \$31,417,915.20        |
| Liabilities + Equity | \$31,417,915.20        |
| <b>Grand Total</b>   | <b>\$62,835,830.40</b> |

**TIF 1–6 Tableau**

## Account Balance

| Category (group)     |                 |
|----------------------|-----------------|
| Asset                | \$31,417,915.20 |
| Liabilities + Equity | \$31,417,915.20 |

Sum of Amount broken down by  
Category (group).

# Instructor Manual

Warren/Jones/Tayler, Financial & Managerial Accounting, 17e, 2026,  
9798214040288; Chapter 1: Introduction to Accounting and Business

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## PURPOSE AND PERSPECTIVE OF THE CHAPTER

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The purpose of this chapter is to introduce students to business and accounting. For many students, Chapter 1 of *Corporate Financial Accounting* is their first taste of the business or accounting disciplines. The teaching challenge is to get students to understand and accept the importance of learning business and accounting concepts. This will make the course more than just another requirement that students must complete to graduate. Because this chapter will set the tone for the entire course and the students' business careers, avoid the temptation to rush through the material.

Chapter 1 begins with a discussion of the nature of business and accounting and the different types of businesses (service, merchandising, and manufacturing). Next, the chapter describes the role of accounting in business. The chapter then moves on to business ethics and discusses how individual character, firm culture, and laws and enforcement affect ethics as well as examples of accounting/business fraud. Opportunities in accounting professions/careers are discussed. Following this introductory information, the text explains generally accepted accounting principles (GAAP), the characteristics of financial information, and the assumptions that form the basis of GAAP. The forms of business entities (proprietorships, partnerships, corporations, and limited liability companies) are described. The four principles of financial accounting (measurement, historical cost, revenue recognition, and expense recognition) are defined. The accounting equation is introduced, and then the discussion of how business transactions affect accounts in the accounting equation begins. When transactions are analyzed, changes in assets, liabilities, and stockholders' equity are stated as "increases" or "decreases"; the terms *debit* and *credit* are not introduced until Chapter 2. The components of the accounting equation are discussed using several transactions for a business called NetSolutions. Next are examples of how to prepare the four primary financial statements using the accounting equation information and explanations of how the four financial statements are interrelated. The chapter ends with an explanation of the ratio of liabilities to stockholders' equity and how it is particularly important to creditors.

## CHAPTER OBJECTIVES

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The following objectives are addressed in this chapter:

- Obj. 1 Describe the nature of business and the role of accounting and ethics in business.
- Obj. 2 Describe generally accepted accounting principles, including the underlying assumptions and principles.
- Obj. 3 State the accounting equation and define each element of the equation.
- Obj. 4 Describe and illustrate how business transactions can be recorded in terms of the resulting change in the elements of the accounting equation.

Obj. 5 Describe the financial statements of a corporation and explain how they interrelate.

Obj. 6 Describe and illustrate the use of the ratio of liabilities to stockholders' equity in evaluating a company's financial condition.

## COMPLETE LIST OF CHAPTER ACTIVITIES AND ASSESSMENTS

The following table organizes activities and assessments by objective, so that you can see how all this content relates to objectives and make decisions about which content you would like to emphasize in your class based on your objectives. For additional guidance, refer to the Teaching Online Guide.

| Chapter Objective | Activity/Assessment        | Source (i.e., PPT slide, Workbook) |
|-------------------|----------------------------|------------------------------------|
| Obj. 1            | Knowledge Check Activity 1 | PPT Slides 5–6                     |
| Obj. 2            | Discussion Activity 1      | PPT Slides 22–23                   |
| Obj. 3            | Discussion Activity 2      | PPT Slides 25–26                   |
| Obj. 4            | Knowledge Check Activity 2 | PPT Slides 41–42                   |
| Obj. 5            | Knowledge Check Activity 3 | PPT Slides 54–55                   |

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## KEY TERMS

**Account payable:** The liability created by a purchase on account.

**Account receivable:** An asset, which is a claim against the customer created by selling merchandise or services on credit.

**Accounting:** An information system that measures, records, and reports financial information about a company that assists and supports user decision making.

**Accounting assumptions:** Assumptions that provide the framework upon which accounting standards are constructed.

**Accounting equation:** The equation that shows the relationship among assets, liabilities, and equity; expressed as  $\text{Assets} = \text{Liabilities} + \text{Equity}$ .

**Accounting principles:** Principles that provide the framework upon which accounting standards are constructed.

**Accounting standards:** The rules that determine the accounting for individual business transactions.

**Accounting Standards Codification:** An electronic database maintained by the Financial Accounting Standards Board (FASB) that contains all of the accounting standards that make up the generally accepted accounting principles (GAAP).

**Accounting Standards Updates:** Published changes to accounting standards that are the source of updates to the Accounting Standards Codification.

**Arm's-length transactions:** Transactions between two independent parties.

**Assets:** The resources owned by a business.

**Balance sheet:** A list of the assets, liabilities, and stockholders' equity as of a specific date, usually at the close of the last day of a month or a year.

**Business:** An organization in which basic resources (inputs), such as materials and labor, are assembled and processed to provide goods or services (outputs) to customers.

**Business entity assumption:** A concept of accounting that limits the economic data in the accounting system to data related directly to the activities of the business.

**Business transaction:** An economic event or condition that directly changes an entity's financial condition or directly affects its results of operations.

**Certified Public Accountants (CPAs):** Public accountants who have met a state's education, experience, and examination requirements.

**Common stock:** Certificates issued by a corporation to investors as proof of their ownership rights; an account representing the ownership rights of investors in a corporation; a class of stock issued by a corporation that bears no preference rights.

**Comparability:** A secondary characteristic of financial information; comparability includes consistent reporting, that allows users to identify similarities and differences among reported items.

**Corporation:** A business organized under state or federal statutes as a separate legal entity.

**Cost principle:** A concept of accounting that states that an asset should be recorded and maintained in the accounting records at its initial transaction price.

**Data analytics:** The science of analyzing raw data to discover patterns, identify anomalies, or gain other useful insights.

**Dividends:** Distributions of earnings to stockholders; an account representing the distribution of a corporation's earnings to stockholders.

**Earnings:** The amount by which revenues exceed expenses.

**Equity:** The rights of the owners of a business.

**Ethics:** Moral principles that guide the conduct of individuals.

**Expense recognition principle:** A principle, sometimes called the matching principle, that requires expenses to be recorded in the same period as the related revenue; a concept of accounting in which expenses are matched with the revenue generated during a period by those expenses.

**Expenses:** Amounts used to generate revenue; assets used up or services consumed in the process of generating revenues.

**Faithful representation:** A characteristic of financial reports that pertains to information accurately reflecting an entity's economic activity or condition.

**Fees earned:** Revenue from providing services.

**Financial accounting:** The branch of accounting that is concerned with recording transactions using generally accepted accounting principles (GAAP) for a business or other economic unit and with a periodic preparation of various statements from such records.

**Financial Accounting Standards Board (FASB):** The authoritative body that has the primary responsibility for developing accounting principles.

**Financial statements:** Financial reports that summarize the effects of events on a business.

**Financing activities:** Activities by which a company obtains funds to start and operate the company.

**Fiscal year:** The annual accounting period adopted by a business.

**Generally accepted accounting principles (GAAP):** A collection of accounting standards, principles, and assumptions that define how financial information should be reported.

**General-purpose financial statements:** A type of financial accounting report that is distributed to external users. The term "general purpose" refers to the wide range of decision-making needs that the reports are designed to serve.

**Going concern assumption:** An assumption that requires that financial reports be prepared assuming that the entity will continue operating in the future.

**Historical cost principle:** A concept of accounting that states that an asset should be recorded and maintained in the accounting records at its initial transaction price.

**Income statement:** A summary of the revenue and expenses for a specific period of time, such as a month or a year.

**Interest revenue:** Earnings received for interest.

**International Accounting Standards Board (IASB):** An organization that issues International Financial Reporting Standards for many countries outside the United States.

**Investing activities:** Activities by which a company acquires long-term assets for use in the operating activities of the company.

**Liabilities:** The rights of creditors that represent debts of the business.

**Limited liability company (LLC):** A business form consisting of one or more persons or entities filing an operating agreement with a state to conduct business with limited liability to the owners, yet treated as a partnership for tax purposes.

**Managerial (or management) accounting:** The branch of accounting that uses both historical and estimated data in providing internal users (management) with information relevant to decision making.

**Manufacturing business:** A type of business that changes basic inputs into products that are sold to customers.

**Measurement principle:** A principle that requires that amounts be objective and verifiable.

**Monetary unit assumption:** An accounting assumption that requires that financial reports be expressed in a single monetary unit, or currency.

**Natural business year:** A fiscal year that ends when business activities have reached the lowest point in an annual operating cycle.

**Net income (or net profit):** The amount by which revenues exceed expenses.

**Net loss:** The amount by which expenses exceed revenues.

**Operating activities:** Activities by which a company generates revenues from customers.

**Owner's equity:** The equity for a proprietorship, partnership, or a limited liability company.

**Partnership:** An unincorporated business form consisting of two or more persons conducting business as co-owners for profit.

**Prepaid expenses:** Assets created by making advanced payments for expense items, such as insurance premiums or supplies, that will be used in the business in the future.

**Private accounting:** The field of accounting whereby accountants are employed by a business firm or a not-for-profit organization.

**Profit:** The difference between the amounts received from customers for goods or services provided and the amounts paid for the inputs used to provide the goods or services.

**Proprietorship:** A business owned by one individual.

**Public accounting:** The field of accounting where accountants and their staff provide services on a fee basis.

**Public Company Accounting Oversight Board (PCAOB):** A new oversight body for the accounting profession that was established by the Sarbanes-Oxley Act.

**Ratio of liabilities to stockholders' equity:** A comprehensive leverage ratio that measures the relationship of the claims of creditors to stockholders' equity; a solvency ratio that measures how much of the company is financed by debt and equity, computed as total liabilities divided by total stockholders' equity.

**Relevant:** A characteristic of financial reports that pertains to information having the potential to impact decision making.

**Rent revenue:** Earnings from property that is leased to others for use.

**Report form:** A form of balance sheet with the "Liabilities" and "Stockholders' Equity" sections presented below the "Assets" section.

**Retained earnings:** The stockholders' equity created from business operations through revenue and expense transactions; an account representing the net income retained in a corporation.

**Retained earnings statement:** A summary of the changes in the retained earnings in a corporation that have occurred during a specific period of time, such as a month or a year.

**Revenue:** Increases in owner's equity as a result of providing services or selling goods to customers.

**Revenue recognition principle:** A concept of accounting that states that revenues are recorded when earned, which is when the services have been performed or products have been delivered to customers.

**Sales:** How revenue from the sale of merchandise is recorded; the total amount charged customers for merchandise sold, including cash sales and sales on account.

**Sarbanes-Oxley Act (SOX):** An act passed by Congress to restore public confidence and trust in the financial statements of companies.

**Securities and Exchange Commission (SEC):** An agency of the U.S. government that has authority over the accounting and financial disclosures for companies whose shares of ownership (stock) are traded and sold to the public.

**Service business:** A business providing services rather than products to customers.

**Statement of cash flows:** A summary of the cash receipts and cash payments for a specific period of time, such as a month or a year.

**Statement of stockholders' equity:** A summary of the changes in the stockholders' equity in a corporation that have occurred during a specific period of time, such as a month or a year.

**Stockholders' equity:** The ownership rights of stockholders in a corporation; the stockholders' rights to the assets in a corporation after all liabilities have been paid.

**Timeliness:** A secondary characteristic of financial information that requires distribution of financial reports in time to influence a user's decision.

**Time period assumption:** An accounting assumption that allows a company to report its economic activities on a regular basis for a specific period of time.

**Understandability:** A secondary characteristic of financial information that requires clear and concise financial reports that facilitate user interpretation and analysis.

**Verifiability:** A secondary characteristic of financial information that allows users to agree on the meaning of reported items.

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## WHAT'S NEW IN THIS CHAPTER

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See the Transition Guide for a list of improvements in this chapter from the previous edition.

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## CHAPTER OUTLINE

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The following outline organizes activities (including any existing discussion questions in PowerPoints or other supplements) and assessments by chapter (and therefore by topic), so that you can see how all the content relates to the topics covered in the text.

- I. Nature of Business and Accounting (1-1, PPT Slides 3-13, BUSPROG: Analytic, AICPA: FN-Research)
  - a. The first objective starts with a list of the three types of businesses: service, merchandising, and manufacturing. It defines each type of business and gives examples.
  - b. **Knowledge Check Activity 1:** *Which of the following businesses would be considered a service business?* (Slides 5-6)
    - Southwest Airlines would be considered a service business.
    - Walmart and Starbucks would be considered merchandising businesses, and Ford Motor Company would be a manufacturer.
  - c. Businesses engage in three types of activities: operating, investing, and financing. Exhibit 1 (PPT Slide 7) summarizes these three activities.
  - d. The role of accounting in business is discussed along with the two types of users: internal and external.
  - e. Accounting can be defined as an information system that provides reports to internal and external users about the economic activities and condition of a business as shown in Exhibit 2 (PPT Slide 9).
  - f. Internal users require information from managerial accounting, while external users require information from financial accounting. To be useful, accounting information must be relevant, timely, and trustworthy.

- g. The failure of individual character and a culture of corporate greed and ethical indifference led to accounting and business frauds as shown in Exhibit 3 (PPT Slide 11). The Sarbanes-Oxley Act (SOX) was enacted in 2002 as a countermeasure to the fraud that was being committed. One of the many regulations that SOX established was a new oversight body for the accounting profession called the Public Company Accounting Oversight Board (PCAOB).
  - h. Opportunities for accountants are increasing as regulations increase, and people are beginning to realize the importance and value of accounting information. Exhibit 4 (PPT Slides 12 and 13) provides a list of accounting career paths and salaries.
- II. Generally Accepted Accounting Principles (GAAP) (1-2, PPT Slides 14–23, BUSPROG: Analytic, AICPA: FN-Measurement)
  - a. Generally accepted accounting principles (GAAP) are used to prepare financial reports. This allows users to compare one company to another. In the United States, these principles are the responsibility of the Financial Accounting Standards Board (FASB). Companies that are publicly traded are also guided by the Securities and Exchange Commission (SEC).
  - b. The FASB works with the International Accounting Standards Board (IASB) to reduce differences between international and U.S. standards. This helps make global investment and business easier. Financial accounting and GAAP are based on assumptions regarding the monetary unit, time period, business entity, and going concern.
  - c. This chapter also introduces the four forms of business entities: sole proprietorship, partnership, corporation, and limited liability company (LLC). Exhibit 5 (PPT Slides 19 and 20) lists the types of business entities and the characteristics and advantages of each.
  - d. Financial accounting relies on principles regarding measurement, historical cost, revenue recognition, and expense recognition.
  - e. **Discussion Activity 1:** *In the following scenarios, which form of business entity do you think would be the best choice? Explain your reasons.* (Slides 22–23)
    - A group of three dentists opening a full-service dental office
    - A graphic design artist specializing in digital marketing
    - Five entrepreneurs opening a chain of hair salons
      - There are advantages and disadvantages for each type of business formation. Small businesses often select a sole proprietorship, although it does expose them to liability issues, including potential lawsuits.
      - For each of these scenarios, the answers may vary. Legal and medical professionals often select a form of partnership or LLC. An individual, such as the graphic artist, may choose to be a sole proprietor. When there are more people involved and the potential exists for shares to be issued, a corporation would be the best choice (likely for the hair salons).
      - What did you choose for each, and why? If you opened a business, which would you choose?

- f. More companies are relying on data analytics, which is the science of analyzing raw data to discover patterns, identify anomalies, or gain other useful insights. Because of accounting's role in providing useful information, accountants are increasingly using data analytics to help businesses make better decisions.
- III. The Accounting Equation (1-3, PPT Slides 24–26, BUSPROG: Analytic, AICPA: FN-Measurement)
  - a. This objective defines assets, liabilities, and stockholders' equity and uses the accounting equation ( $\text{Assets} = \text{Liabilities} + \text{Equity}$ ) to explain their relationship.
  - b. **Discussion Activity 2:** *Give an example of what a company might have as an asset and a liability. Then consider what an individual would have as an asset and a liability. (Slides 25–26)*
    - How would an asset differ from a business compared to an individual?
    - How would a liability differ from a business compared to an individual?
    - Can an individual calculate their net worth using the same accounting equation as a business?
- IV. Business Transactions and the Accounting Equation (1-4, PPT Slides 27–42, BUSPROG: Analytic, AICPA: FN-Measurement)
  - a. Using a sample company called NetSolutions, this objective demonstrates how business transactions affect a company's financial condition.
  - b. Transactions, such as depositing cash, purchasing assets, selling services, and paying bills, affect the accounting equation. This shows students that through each transaction the two sides of the accounting equation must always be equal.
  - c. **Knowledge Check Activity 2:** *Hampshire Havens buys an adjoining piece of land to expand its golf course. It pays \$89,000 in cash to acquire this land. Based on the accounting equation, what would be the effect of this transaction? (Slides 41–42)*
    - Cash would decrease by \$89,000, and Land would increase by \$89,000.
- V. Financial Statements (1-5, PPT Slides 43–55, BUSPROG: Analytic, AICPA: FN-Reporting)
  - a. This objective shows the income statement, statement of stockholders' equity, balance sheet, and statement of cash flows. Exhibit 8 (PPT Slide 44) shows the order in which the financial statements are prepared.
  - b. Using the same NetSolutions example as the previous objective, the order, preparation, and relationship among the four financial statements is demonstrated. Each statement is prepared for a specific period of time, except the balance sheet; it is prepared for a point in time.
  - c. The income statement is the first one prepared: revenue minus expenses is known as net income; if expenses are greater than revenue, the excess is a net loss. The statement of stockholders' equity reports

the changes in common stock and retained earnings; the balance sheet reports the amount of assets, liabilities, and stockholders' equity and must follow the accounting equation. The statement of cash flows has three sections: operating, investing, and financing activities. Exhibit 9 (PPT Slides 45 and 46) shows the four financial statements for NetSolutions. Exhibit 10 (PPT Slides 51 and 52) explains the interrelationships between the financial statements. The balance sheet is the connecting link between the financial statements, and this is shown in Exhibit 11 (PPT Slide 53).

- d. **Knowledge Check Activity 3:** *Which financial statement would a stockholder want to review if they are interested in the company's sales and expenses?* (Slides 54–55)
  - The income statement would list a company's sales, expenses, and net income or net loss.
- VI. Analysis for Decision Making: Ratio of Liabilities to Stockholders' Equity (1–6, PPT Slides 56–58, BUSPROG: Analytic, AICPA: FN-Measurement)
  - a. Using the financial statements prepared in the previous objective, the use of the ratio of liabilities to stockholders' equity is examined. The total liabilities amount is divided by the total stockholders' equity amount to calculate this ratio.
  - b. Because creditors have rights to a business's assets before the owner, this ratio is important to both owners and creditors. This ratio can affect how a business pays its creditors and foretells how well a business will do in poor economic conditions. As this ratio increases, the creditors and the business become more at risk. Examples of the ratio for Alphabet and Meta Platforms are shown on PPT Slides 57 and 58.

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## ADDITIONAL DISCUSSION QUESTIONS

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The following are discussion questions that do not appear in the text, PPTs, or courseware – they are for you to use as you wish. You can assign these questions several ways: in a discussion forum in your LMS; as whole-class discussions in person; or as a partner or group activity in class.

1. Discussion: Importance of Accounting (Nature of Business and Accounting, 1–1, PPT Slide 8) Duration 10 minutes.
  - a. The role of accounting is to provide information to businesses about their activities, including operating, investing, and financing. Why is “accounting” so important?
    - i. Answer: Accounting is the language of business. Without an organized system that provides information to users about the economic activities and condition of a business, there would no guarantee of a company being profitable or continuing in existence.

- b. Why do I need to know about accounting if I am not going to be an accountant?
  - i. Answer: Any business professional needs to be aware of the functions and information provided by an accounting system. Without these vital data, such as information on sales, expenses, assets, liabilities, and equity, a business cannot survive, nor can its owners be assured of its profitability. Basic financial statements, such as the income statement and balance sheet, provide useful information for all users, internal and external, regarding a business. For example, if you are a marketing manager, it is important to know the expenses of the company's product or service to ensure the items are sold at a price that will provide a profit. Every employee of a business has a responsibility to uphold the company's mission to attain and sustain profitability.
- 2. Discussion: Recording Financial Transactions (Business Transactions and the Accounting Equation, 1-4) Duration 10 minutes.
  - a. Why can't I just use a computer program to do all my accounting? Isn't that what technology is for?
    - i. Answer: Technology and software are extremely useful tools in all areas of business. Today's accounting software allows companies to record and process transactions very quickly and has lots of safeguards to protect against errors such as incorrect account numbers, math mistakes, unbalanced journal entries, and confusion in creating financial statements. However, financial and accounting systems are maintained by humans who need to provide directions and "rules" within the software programs. Accounting rules can change, and in certain areas, such as payroll processing, they vary from year to year or even more often—think of tax rate changes and employment laws. So while technology and accounting software are superb tools, it is important for trained employees to monitor the input and output carefully and to know how accounting works to use their judgment in processing data.
- 3. Discussion: Items Listed on Financial Statements (Financial Statements, 1-5, PPT Slides 47 and 49) Duration 15 minutes.
  - a. The accounting system classifies different items into categories to help group similar items together for reporting and analysis. What is the difference between revenues and assets? Give examples of these items.
    - i. Answer: Revenues are income derived from the sales of a company's products or services. These will change over time as the company grows or has seasonal activity. For example, a company such as Hershey's Food Corporation has increased sales prior to major holidays. A company's assets are resources that a company owns to provide the ability to earn revenues. For example, FedEx owns many delivery trucks and planes to earn revenues from delivering packages. Examples

- of assets include property, plant, and equipment, as well as cash, accounts receivable, and inventory.
- b. What is the difference between expenses and liabilities? Give examples of these items.
    - i. Answer: Expenses are costs incurred by a company to make a product or provide a service. Examples of expenses include rent, payroll costs, raw materials, shipping, travel, and many others. Liabilities are amounts owed by the company to another entity. Examples of liabilities include mortgages, accounts payable to vendors, bond interest payable to bondholders, etc.

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## ADDITIONAL RESOURCES

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The following are activities and assignments developed by Cengage but not included in the text, PPTs, or courseware – they are for you to use if you wish.

1. **Class Discussion Activity:** *Types of Businesses* (Reflective Thinking, Critical Thinking, 1-1, PPT Slide 4) Duration 15 minutes.
  - a. Have the class provide the names of businesses they have patronized in the past week. Include places they have shopped, eating establishments, products they use every day, and services they have used. When listing products, name the manufacturer; for iPod, for example, the manufacturer would be Apple. List these on the board or overhead.
    - i. Answer: Student answers will vary.
  - b. Have the students identify each listed business as service, manufacturing, or manufacturing. Some will cross over categories. Nike, for example, manufactures products and owns retail outlets.
    - i. Answer: Student answers will vary.
2. **Class Discussion Activity:** *Role of Ethics in Accounting and Business* (Reflective Thinking, Critical Thinking, 1-1, PPT Slide 10) Duration 20 minutes.
  - a. Lauren Smith is the controller for Sports Central, a chain of sporting goods stores. She has been asked to recommend a site for a new store. Lauren has an uncle who owns a shopping plaza in the area of town where the new store is to be located, so she decides to contact her uncle about leasing space in his plaza. Lauren also contacted several other shopping plazas and malls, but her uncle's store turned out to be the most economical place to lease. Therefore, Lauren recommended locating the new store in her uncle's shopping plaza. In making her recommendation to management, she did not disclose that her uncle owns the shopping plaza. Discuss whether or not the accountant acted ethically.
    - i. Answer: Lauren has a conflict of interest in recommending her uncle's shopping plaza as a site for the new store. After reviewing the data, management at Sports Central may agree with Lauren that her uncle's plaza is the most economical

place to lease; however, Lauren should not make that recommendation without disclosing the family relationship. By hiding the conflict of interest, Lauren appears to lack integrity.

- b. John Jones is the chief accountant for the southwest district office of Security Life Insurance Company. While preparing the fourth-quarter sales report, John overheard the company president say that he would close Security's Phoenix office if it did not meet its fourth-quarter sales quota. John's best friend from college works at the Phoenix office. Anxious to find out whether the office was in jeopardy, John immediately finished the Phoenix office's report, only to find that it showed sales 25% below the quota. Later that afternoon, the company president called John for Phoenix's sales results. John told the president that he had not finished preparing the sales report for the Phoenix office. John wanted time to compile data that might convince the president to continue operations in Phoenix, despite lagging sales. Discuss whether or not the accountant acted ethically.

- i. Answer: Management accountants must communicate all information, both good and bad, fairly and objectively. It is not ethical to mislead management by withholding available information.

3. **Writing Exercises Activity:** *Business Entity and Cost Concept* (Reflective Thinking, Measurement, 1-2, PPT Slide 18) Duration 20 minutes.

- a. Sally Vertrees purchased a personal computer for use at home. Sally owns a dental practice. She occasionally uses the computer for a task related to her dental practice; however, the computer is used primarily by Sally's children. Can the computer be recorded as an asset in the accounting records of Sally's dental office? Why or why not?

- i. Answer: This is not the proper use of the business entity assumption. Purchasing items for personal use from business funds will affect the reporting of how successful or unsuccessful a business purports to be for a financial period.

- b. Jason Thompson purchased an office building 10 years ago for \$780,000. The building was just appraised at \$1.25 million. What value should be used for the building in Jason's accounting records?

Support your answer.

- i. Answer: This is a clear example of the cost principle. Assets are recorded at cost and remain on the business books at cost until they are disposed of. Future economic conditions may change this appraised value; therefore, no adjustment is made until the asset is sold.

4. **Class Discussion and Online Activity:** *Types of Business Organizations* (Reflective Thinking, Critical Thinking, 1-2, PPT Slides 19 and 20) Duration 20 minutes.

- a. Ask students to name examples of businesses in the business entity categories of proprietorship, partnership, corporation, and limited liability corporation. Explain that they will be learning about accounting concepts related to businesses organized as corporations. Have them look online to find examples of each type.

- i. Answer: Student answers will vary. It may be a challenge to find businesses that fall under the category of limited liability

corporation. Ask students what the advantages would be for each category.

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