

Solutions Manual for Horngrens Accounting 13th Nobles

Chapter 1

Accounting and the Business Environment

Review Questions

1. Accounting is the information system that measures business activities, processes the information into reports, and communicates the results to decision makers. Accounting is the language of business.
2. Financial accounting provides information for external decision makers, such as outside investors, lenders, customers, and the federal government. Managerial accounting focuses on information for internal decision makers, such as the company's managers and employees.
3. Individuals use accounting information to help them manage their money, evaluate a new job, and better decide whether they can afford to make a new purchase. Business owners use accounting information to set goals, measure progress toward those goals, and make adjustments when needed. Investors use accounting information to help them decide whether or not a company is a good investment and once they have invested, they use a company's financial statements to analyze how their investment is performing. Creditors use accounting information to decide whether to lend money to a business and to evaluate a company's ability to make the loan payments. Taxing authorities use accounting information to calculate the amount of income tax that a company has to pay.
4. Certified Public Accountants (CPAs) are licensed professional accountants who serve the general public. They work for public accounting firms, businesses, government, or educational institutions. A Chartered Global Management Accountant (CGMA) is an accountant who has advanced knowledge in finance, operations, strategy, and management. Certified Management Accountants (CMAs) specialize in accounting and financial management knowledge. They work for a single company. Certified Financial Planners (CFPs) work with individuals to help them budget, plan for retirement, save for education, and manage their finances.
5. The FASB oversees the creation and governance of accounting standards. They work with governmental regulatory agencies, congressionally created groups, and private groups.
6. The guidelines for accounting information are called GAAP. It is the main U.S. accounting rule book and is currently created and governed by the FASB. Investors and lenders must have information that is relevant and has faithful representation in order to make decisions and GAAP provides the framework for this financial reporting.
7. A sole proprietorship has a single owner, terminates upon the owner's death or choice, the owner has personal liability for the business's debts, and it is not a separate tax entity. A partnership has two or more owners, terminates at partner's choice or death, the partners have personal liability, and it is not a separate tax entity. A corporation is a separate legal entity, has one or more owners, has indefinite life, the stockholders are not personally liable for the business's debts, and it is a separate tax entity. A limited-liability company has one or more members and each is only liable for his or her own actions, has an indefinite life, and is not a separate tax entity.

8. The land should be recorded at \$5,000. The cost principle states that assets should be recorded at their historical cost.
9. The going concern assumption assumes that the entity will remain in business for the foreseeable future and long enough to use existing resources for their intended purpose.
10. The faithful representation concept states that accounting information should be complete, neutral, and free from material error.
11. The monetary unit assumption states that items on the financial statements should be measured in terms of a monetary unit.
12. The IASB is the organization that develops and creates IFRS which are a set of global accounting standards that would be used around the world.
13. $\text{Assets} = \text{Liabilities} + \text{Equity}$. Assets are economic resources that are expected to benefit the business in the future. They are things of value that a business owns or has control of. Liabilities are debts that are owed to creditors. They are one source of claims against assets. Equity is the other source of claims against assets. Equity is the owner's claims against assets and is the amount of assets that is left over after the company has paid its liabilities. It represents the net worth of the business.
14. Equity increases with owner contributions and revenues. Equity decreases with expenses and owner withdrawals.
15. $\text{Revenues} - \text{Expenses} = \text{Net Income}$. Revenues are earnings resulting from delivering goods or services to customers. Expenses are the cost of selling goods or service.
16. Step 1: Identify the accounts and the account type. Step 2: Decide if each account increases or decreases. Step 3: Determine if the accounting equation is in balance.
17. Income Statement – Shows the difference between an entity's revenues and expenses and reports the net income or net loss for a specific period.
Statement of Owner's Equity – Shows the changes in owner's capital for a specific period including owner contributions, net income (loss) and owner withdrawals
Balance Sheet – Shows the assets, liabilities, and owner's equity of the business as of a specific date.
Statement of Cash Flows – Shows a business's cash receipts and cash payments for a specific period.
18. $\text{Return on Assets} = \text{Net income} / \text{Average total assets}$. ROA measures how profitably a company uses its assets.

Short Exercises

S-F:1-1

- | | |
|-------|-------|
| a. FA | e. MA |
| b. FA | f. FA |
| c. FA | g. MA |
| d. MA | h. FA |

S-F:1-2

The Financial Accounting Standards Board governs the majority of guidelines, called Generally Accepted Accounting Principles (GAAP), that the CPA will use to prepare financial statements for Wholly Shirts.

S-F:1-3

Chloe's needs will best be met by organizing a corporation since a corporation has an unlimited life and is a separate tax entity. In addition, the owners (stockholders) have limited liability. Chloe could also consider a limited liability company (LLC) as an option. A LLC meets two of the three criteria. It has an unlimited life and limited liability for the owner. However, a LLC is not a separate tax entity.

S-F:1-4

Advantages:

1. Easy to organize.
2. Unification of ownership and management.
3. Less government regulation.
4. Owner has more control over business.

Disadvantages:

1. The owner pays taxes on the entity's earnings since it is not a separate tax entity.
2. No continuous life or transferability of ownership.
3. Unlimited liability of owner for business's debts.

S-F:1-5

- a. The economic entity assumption
- b. The cost principle.
- c. The monetary unit assumption.
- d. The going concern assumption.

S-F:1-6**Requirement 1**

Thompson Handyman Services has equity of \$9,350.

Assets	=	Liabilities	+	Equity
\$18,400	=	\$9,050	+	?
\$18,400	=	\$9,050	+	\$9,350

Requirement 2

Thompson Handyman Services has liabilities of \$17,200.

Assets	=	Liabilities	+	Equity
\$18,400 + \$4,300	=	?	+	\$9,350 – \$3,850
\$22,700	=	\$17,200	+	\$5,500

S-F:1-7**Requirement 1**

ASSETS	=	LIABILITIES	+	EQUITY						
			+	Roland, Capital	–	Roland, Withdrawals	+	Revenues	–	Expenses
\$45,800	=	\$17,220	+	\$27,460	–	\$6,500	+	\$8,850	–	?
\$45,800	=	\$17,220	+	\$27,460	–	\$6,500	+	\$8,850	–	\$1,230

Requirement 2

Roland's Overhead Doors reported net income of \$7,620. Net Income = Revenues (\$8,850) – Expenses (\$1,230)

S-F:1-8

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| a. L | f. E |
| b. A | g. A |
| c. E | h. E |
| d. A | i. A |
| e. E | j. E |

S-F:1-9

- Increase asset (Cash); Increase equity (Service Revenue)
- Decrease asset (Cash); Decrease equity (Salaries Expense)
- Increase asset (Cash); Increase Equity (Martin, Capital)
- Increase asset (Accounts Receivable); Increase equity (Service Revenue)
- Increase liability (Accounts Payable); Decrease equity (Utility Expense)
- Decrease asset (Cash); Decrease equity (Martin, Withdrawals)

S-F:1-10

- Increase asset (Cash); Increase equity (Gibson, Capital)
- Increase asset (Equipment); Increase liability (Accounts Payable)
- Increase asset (Office Supplies); Decrease asset (Cash)
- Increase asset (Cash); Increase equity (Service Revenue)
- Decrease asset (Cash); Decrease equity (Wages Expense)
- Decrease asset (Cash); Decrease equity (Gibson, Withdrawals)
- Increase asset (Accounts Receivable); Increase equity (Service Revenue)
- Decrease asset (Cash); Decrease equity (Rent Expense)
- Increase liability (Accounts Payable); Decrease equity (Utilities Expense)

S-F:1-11

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|---------|-------|
| a. B | f. I |
| b. B, C | g. B |
| c. B | h. OE |
| d. B | i. B |
| e. I | j. I |

S-F:1-12

CENTERPIECE ARRANGEMENTS
Income Statement
Year Ended December 31, 2024

Revenue:		
Service Revenue		\$ 70,000
Expenses:		
Salaries Expense	\$ 46,000	
Rent Expense	16,000	
Insurance Expense	4,500	
Utilities Expense	1,400	
Total Expenses		<u>67,900</u>
Net Income		<u><u>\$ 2,100</u></u>

S-F:1-13

CENTERPIECE ARRANGEMENTS	
Statement of Owner's Equity	
Year Ended December 31, 2024	
Right, Capital, January 1, 2024	\$ 9,000
Owner contribution	5,100
Net income for the year	2,100
	<u>16,200</u>
Owner withdrawal	(4,800)
Right, Capital, December 31, 2024	<u><u>\$ 11,400</u></u>

S-F:1-14

CENTERPIECE ARRANGEMENTS			
Balance Sheet			
December 31, 2024			
Assets		Liabilities	
Cash	\$ 7,200	Accounts Payable	\$ 17,600
Accounts Receivable	8,000		
Office Supplies	1,700	Owner's Equity	
Equipment	12,100	Right, Capital	11,400
Total Assets	<u>\$ 29,000</u>	Total Liabilities and Owner's Equity	<u>\$ 29,000</u>

S-F:1-15

POLK STREET HOMES
Statement of Cash Flows
Month Ended July 31, 2024

Cash flows from operating activities:

Receipts:

Collections from customers \$ 25,000

Payments:

To employees \$ (1,500)

To suppliers (2,500) (4,000)

Net cash provided by operating activities 21,000

Cash flows from investing activities:

Purchase of equipment (25,000)

Net cash used by investing activities (25,000)

Cash flows from financing activities:

Owner contribution 13,000

Owner withdrawal (4,000)

Net cash provided by financing activities 9,000

Net increase in cash 5,000

Cash balance, July 1, 2024 14,000

Cash balance, July 31, 2024 \$ 19,000

S-F:1-16

<u>Return on assets</u>	=	Net income / Average total assets
	=	\$50,880 / ((\$362,000 + \$486,000) / 2)
	=	\$50,880 / \$424,000
	=	12%

Exercises

E-F:1-17

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| b. I | f. I |
| c. E | g. I |
| d. E | h. E |

E-F:1-18

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| 1. d | 6. f |
| 2. e | 7. b |
| 3. g | 8. c |
| 4. a | 9. j |
| 5. i | 10. h |

E-F:1-19

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|------|-------|
| 1. e | 7. d |
| 2. a | 8. c |
| 3. i | 9. g |
| 4. f | 10. h |
| 5. j | 11. k |
| 6. b | |

E-F:1-20

	Assets	Liabilities	Equity
Hair Styles	\$ 72,000	\$ 36,000	\$ 36,000
Style Cuts	90,000	42,000	48,000
Your Basket	101,000	68,000	33,000

E-F:1-21

	a.	b.	c.
Owner's equity, May 31, 2024 (\$122,000 – \$66,000)	\$ 56,000	\$ 56,000	\$ 56,000
Owner contribution	10,000	0	12,500
Net income for the month	77,000	90,000	104,500
	143,000	146,000	173,000
Owner withdrawal	0	(3,000)	(30,000)
Owner's equity, June 30, 2024 (\$287,000 – \$144,000)	\$ 143,000	\$ 143,000	\$ 143,000

E-F:1-22**Requirement 1**

	Assets	=	Liabilities	+	Equity
Beginning of 2024	\$19,000	=	\$14,000	+	?
	\$19,000	=	\$14,000	+	\$5,000
End of 2024	\$12,000	=	\$9,000	+	?
	\$12,000	=	\$9,000	+	\$3,000

Owner's equity decreased in 2024 by \$2,000 (\$5,000 – \$3,000).

Requirement 2

- Increase through owner's contributions.
- Increase through net income.
- Decrease through owner's withdrawals.
- Decrease through net loss.

E-F:1-23**Requirement 1**

Revenues	–	Expenses	=	Net Income
\$30,000	–	\$15,000	=	\$15,000

Requirement 2

Flowing Rivers Spa's equity increased by \$15,000 (\$29,000 - \$14,000) or the amount of the net income.

	Assets	=	Liabilities	+	Equity
Beginning of 2024	\$28,000	=	\$14,000	+	?
	\$28,000	=	\$14,000	+	\$14,000
Ending of 2024	\$43,000	=	\$14,000	+	?
	\$43,000	=	\$14,000	+	\$29,000

E-F:1-24**Requirement 1**

	Assets	–	Liabilities	=	Equity
Beginning of 2024	\$67,000	–	\$11,000	=	\$56,000
Ending of 2024	\$46,000	–	\$34,000	=	\$12,000

Owner's Equity:

Capital, Jan. 1, 2024	\$ 56,000
Plus: Owner contributions	11,000
Plus: Revenues	205,000
Less: Expenses	(252,000)
Less: Owner withdrawals	(8,000)
Capital, Dec. 31, 2024	<u>\$ 12,000</u>

Requirement 2

Felix Company suffered (or reported) a net loss of (\$36,000).

Revenue	–	Expenses	=	Net Income (Loss)
\$205,000	–	\$241,000	=	(\$36,000)

E-F:1-25

Student responses will vary. Examples include:

- Cash purchase of office supplies.
- Cash withdrawal by owner.
- Paid cash on accounts payable.
- Received cash for services provided.
- Borrowed cash from the bank.

E-F:1-26

- Increase asset (Cash); Increase equity (Vivian, Capital)
- Increase asset (Accounts Receivable); Increase equity (Rental Revenue)
- Increase asset (Office Furniture); Increase liability (Accounts Payable)
- Increase asset (Cash); Decrease asset (Accounts Receivable)
- Decrease asset (Cash); Decrease liability (Accounts Payable)
- Increase asset (Cash); Increase equity (Rental Revenue)
- Decrease asset (Cash); Decrease equity (Rent Expense)
- Decrease asset (Cash); Increase asset (Office Supplies).

E-F:1-27

- a. Increase asset (Cash); Increase equity (Sam, Capital)
- b. Increase asset (Land); Decrease asset (Cash)
- c. Decrease asset (Cash); Decrease liability (Accounts Payable)
- d. Increase asset (Equipment); Increase liability (Notes Payable)
- e. Increase asset (Accounts Receivable); Increase equity (Service Revenue)
- f. Increase liability (Salaries Payable); Decrease equity (Salaries Expense)
- g. Increase asset (Cash); Decrease asset (Accounts Receivable)
- h. Increase asset (Cash); Increase liability (Notes Payable)
- i. Decrease asset (Cash); Decrease equity (Sam, Withdrawals)
- j. Increase liability (Accounts Payable); Decrease equity (Utility Expense)

E-F:1-28

Transaction Descriptions:

- 1. Cash contribution by owner
- 2. Earned revenue on account
- 3. Purchased equipment on account
- 4. Collected cash on account
- 5. Cash purchase of equipment
- 6. Paid cash on account
- 7. Earned revenue and received cash
- 8. Paid cash for salaries

E-F:1-29

ASSETS					=	LIABILITIES	+	EQUITY											
Date	Cash	+	Medical Supplies	+	Land	=	Accounts Payable	+	Stamper, Capital	–	Stamper, Withdrawals	+	Service Revenue	–	Salaries Expense	–	Rent Expense	–	Utilities Expense
July 6	+68,000								+68,000										
Bal.	\$68,000					=			+ \$68,000										
9	–56,000				+56,000	=													
Bal.	\$12,000				+ \$56,000	=			+ \$68,000										
12		+	+1,500			=	+1,500												
Bal.	\$12,000	+	\$1,500	+	\$56,000	=	\$1,500	+	\$68,000										
15																			
Bal.	\$12,000	+	\$1,500	+	\$56,000	=	\$1,500	+	\$68,000										
20	–2,900					=									–1,300		–1,500		–100
Bal.	\$ 9,100	+	\$1,500	+	\$56,000	=	\$1,500	+	\$68,000						– \$1,300		– \$1,500		– \$100
31	+13,000					=							+13,000						
Bal.	\$22,100	+	\$1,500	+	\$56,000	=	\$1,500	+	\$68,000			+	\$13,000	–	\$1,300	–	\$1,500	–	\$100
31	–1,050					=	–1,050												
Bal.	\$21,050	+	\$1,500	+	\$56,000	=	\$ 450	+	\$68,000			+	\$13,000	–	\$1,300	–	\$1,500	–	\$100

E-F:1-30

Requirement 1

- a. Income statement
- b. Statement of owner's equity
- c. Balance sheet
- d. Statement of cash flows

Requirement 2

Yes, the financial statements should be prepared in the order listed above in Requirement 1.

Requirement 3

Income Statement:

- a. The header includes the name of the business, the title of the statement, and the time period. An income statement always represents a period of time, for example, a month or a year.
- b. The revenue accounts are always listed first and then subtotaled if necessary.
- c. Each expense account is listed separately from largest to smallest and then subtotaled if necessary.
- d. Net income is calculated as total revenues minus total expenses.

Statement of Owner's Equity:

- a. The header includes the name of the business, the title of the statement, and the time period. A statement of owner's equity always represents a period of time, for example, a month or a year.
- b. The beginning capital is listed first and will always be the ending capital from the previous time period.
- c. The owner contributions and net income are added to the beginning capital.
- d. The owner withdrawals are subtracted from capital. If there had been a net loss, this would also be subtracted.

Balance Sheet:

- a. The header includes the name of the business and the title of the statement but the date is different. The balance sheet shows the date as a specific date and not a period of time.
- b. Each asset account is listed separately and then totaled. Cash is always listed first.
- c. Liabilities are listed separately and then totaled. Liabilities that are to be paid first are listed first.
- d. The owner's equity section includes the ending capital from the statement of owner's equity.
- e. The balance sheet must always balance: $\text{Assets} = \text{Liabilities} + \text{Equity}$.

Statement of Cash Flows:

- a. The header includes the name of the business, the title of the statement, and the time period. A statement of cash flows always represents a period of time, for example, a month or a year.
- b. Each dollar amount is calculated by evaluating the cash column on the transaction detail.
- c. Operating activities involve cash receipts for services provided and cash payments for expenses paid.
- d. Investing activities include the purchase and sale of land and equipment for cash.
- e. Financing activities include cash from owner contributions and payment of cash for owner withdrawals.
- f. The ending cash balance must match the cash balance on the balance sheet.

E-F:1-31
Requirement 1

WILSON TOWING SERVICE		
Income Statement		
Month Ended June 30, 2024		
Revenue:		
Service Revenue		\$ 15,000
Expenses:		
Salaries Expense	\$ 2,400	
Rent Expense	900	
Total Expenses		3,300
Net Income		<u>\$ 11,700</u>

Requirement 2

The income statement reports revenues and expenses for a period of time.

E-F:1-32
Requirement 1

WILSON TOWING SERVICE	
Statement of Owner's Equity	
Month Ended June 30, 2024	
Wilson, Capital, June 1, 2024	\$ 3,250
Owner contribution	11,000
Net income for the month	11,700
	<u>25,950</u>
Owner withdrawal	(3,500)
Wilson, Capital, June 30, 2024	<u>\$ 22,450</u>

Requirement 2

The statement of owner's equity reports the changes in owner's capital during a time period.

E-F:1-33
Requirement 1

WILSON TOWING SERVICE				
Balance Sheet				
June 30, 2024				
Assets		Liabilities		
Cash	\$ 1,400	Accounts Payable	\$	8,000
Accounts Receivable	9,000	Notes Payable		<u>6,800</u>
Office Supplies	1,000	Total Liabilities		14,800
Equipment	25,850	Owner's Equity		
		Wilson, Capital		<u>22,450</u>
		Total Liabilities and Owner's		
Total Assets	<u>\$ 37,250</u>	Equity		<u>\$ 37,250</u>

Requirement 2

The balance sheet reports an entity's assets, liabilities, and owner's equity as of a specific date.

E-F:1-34

DAMON DESIGN STUDIO			
Income Statement			
Year Ended December 31, 2024			
Revenue:			
Service Revenue			\$ 154,600
Expenses:			
Salaries Expense	\$ 65,000		
Rent Expense	23,000		
Utilities Expense	7,200		
Miscellaneous Expense	3,800		
Property Tax Expense	<u>2,200</u>		
Total Expenses			<u>101,200</u>
Net Income			<u>\$ 53,400</u>

E-F:1-35

DAMON DESIGN STUDIO	
Statement of Owner's Equity	
Year Ended December 31, 2024	
Damon, Capital, January 1, 2024	\$ 39,000
Owner contribution	13,000
Net income for the year	53,400
	<u>105,400</u>
Owner withdrawal	(57,000)
Damon, Capital, December 31, 2024	<u>\$ 48,400</u>

E-F:1-36

DAMON DESIGN STUDIO			
Balance Sheet			
December 31, 2024			
Assets		Liabilities	
Cash	\$ 3,200	Accounts Payable	\$ 3,600
Accounts Receivable	9,300	Notes Payable	14,000
Office Supplies	5,100	Total Liabilities	<u>17,600</u>
Office Furniture	48,400	Owner's Equity	
	<u> </u>	Damon, Capital	<u>48,400</u>
		Total Liabilities and Owner's	
Total Assets	<u>\$ 66,000</u>	Equity	<u>\$ 66,000</u>

E-F:1-37

- | | |
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| a. F + | f. I – |
| b. O – | g. O – |
| c. X | h. X |
| d. F – | i. O – |
| e. O + | j. X |

E-F:1-38

MORNING BEAN FOOD EQUIPMENT COMPANY

Statement of Cash Flows

Month Ended January 31, 2024

Cash flows from operating activities:

Receipts:

Collections from customers	\$ 8,500	
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Payments:

To employees	\$ (1,300)	
To suppliers	(2,050)	(3,350)

Net cash provided by operating activities		5,150
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Cash flows from investing activities:

Purchase of land	(19,000)	
Net cash used by investing activities		(19,000)

Cash flows from financing activities:

Owner contribution	5,000	
Owner withdrawal	(500)	
Net cash provided by financing activities		4,500

Net decrease in cash		(9,350)
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Cash balance, January 1, 2024		11,800
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Cash balance, January 31, 2024		\$ 2,450
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E-F:1-39

Average total assets = (Beginning total assets + ending total assets) / 2

Beginning total assets = \$34,000 + \$23,000 + \$160,000 + \$2,200 + \$24,000 + \$4,800 = \$248,000

Ending total assets = \$134,200 + \$44,000 + \$160,000 + \$19,800 + \$42,000 + \$2,000 = \$402,000

Average total assets = (\$248,000 + \$402,000) / 2 = \$325,000

ROA = Net income / Average total assets

ROA = \$58,500 / \$325,000 = 0.18 = 18%

E-F:1-40

- a. Decreases. The increase in assets (office furniture) increases the denominator in the equation and therefore decreases the ratio.
- b. Increases. The increase in rental revenue increases net income in the numerator of the equation, therefore increases the ratio.
- c. Does not change. The decrease in assets (cash) and increase in assets (office supplies) in the denominator of the equation causes no change.
- d. Decreases. The increase in assets (cash) increases the denominator in the equation and therefore decreases the ratio.
- e. Increases. The decrease in assets (cash) decreases the denominator in the equation and therefore increases the ratio.
- f. Does not change. The increase in assets (cash) and decrease in assets (accounts receivable) in the denominator of the equation causes no change.

Problems (Group A)

P-F:1-41A

	ASSETS					=	LIABILITIES			+	EQUITY								
	Cash	+	Accounts Receivable	+	Office Supplies	+	Land	=	Accounts Payable	+	McKinney, Capital	–	McKinney, Withdrawals	+	Service Revenue	–	Rent Expense	–	Advertising Expense
Bal.	\$1,900	+	\$3,200			+	\$15,000	=	\$5,000	+	\$11,900				+	\$3,200			
(a)	+17,000										+17,000								
Bal.	\$18,900	+	\$3,200			+	\$15,000	=	\$5,000	+	\$28,900					\$3,200			
(b)	+800															+800			
Bal.	\$19,700	+	\$3,200			+	\$15,000	=	\$5,000	+	\$28,900					\$4,000			
(c)	–5,000								–5,000										
Bal.	\$14,700	+	\$3,200			+	\$15,000	=	\$0	+	\$28,900			+	\$4,000				
(d)					+1,200				+1,200										
Bal.	\$14,700	+	\$3,200	+	\$1,200	+	\$15,000	=	\$1,200	+	\$28,900			+	\$4,000				
(e)	+2,000		–2,000																
Bal.	\$16,700	+	\$1,200	+	\$1,200	+	\$15,000	=	\$1,200	+	\$28,900			+	\$4,000				
(f)	–1,600												–1,600						
Bal.	\$15,100	+	\$1,200	+	\$1,200	+	\$15,000	=	\$1,200	+	\$28,900	–	\$1,600	+	\$4,000				
(g)			+4,500												+4,500				
Bal.	\$15,100	+	\$5,700	+	\$1,200	+	\$15,000	=	\$1,200	+	\$28,900	–	\$1,600	+	\$8,500				
(h)	–1,500																–1,000		–500
Bal.	\$13,600	+	\$5,700	+	\$1,200	+	\$15,000	=	\$1,200	+	\$28,900	–	\$1,600	+	\$8,500	–	\$1,000	–	\$500

P-F:1-42A

	ASSETS				=	LIABILITIES		+	EQUITY												
	Cash	+	Accounts Receivable	+	Office Supplies	=	Accounts Payable	+	Thomas, Capital	-	Thomas, Withdrawals	+	Service Revenue	-	Rent Expense	-	Utilities Expense	-	Wages Expense	-	Advertising Expense
1	+19,000								+19,000												
2	+3,800												+3,800								
Bal.	\$22,800					=		+	\$19,000			+	\$3,800								
5	-200				+200																
Bal.	\$22,600			+	\$200	=		+	\$19,000			+	\$3,800								
9			+4,500										+4,500								
Bal.	\$22,600	+	\$4,500	+	\$200	=		+	\$19,000			+	\$8,300								
10							+200										-200				
Bal.	\$22,600	+	\$4,500	+	\$200	=	\$200	+	\$19,000			+	\$8,300				\$200				
15	-250																				-250
Bal.	\$22,350	+	\$4,500	+	\$200	=	\$200	+	\$19,000			+	\$8,300				\$200			-	\$250
20	-200						-200														
Bal.	\$22,150	+	\$4,500	+	\$200	=	\$ 0	+	\$19,000			+	\$8,300				\$200			-	\$250
25	+4,500		-4,500																		
Bal.	\$26,650	+	\$ 0	+	\$200	=		+	\$19,000			+	\$8,300				\$200			-	\$250
28	-1,600														-1,600						
Bal.	\$25,050			+	\$200	=		+	\$19,000			+	\$8,300	-	\$1,600	-	\$200			-	\$250
28	-1,450																		-1,450		
Bal.	\$23,600			+	\$200	=		+	\$19,000			+	\$8,300	-	\$1,600	-	\$200	-	\$1,450	-	\$250
30	+1,400												+1,400								
Bal.	\$25,000			+	\$200	=		+	\$19,000			+	\$9,700	-	\$1,600	-	\$200	-	\$1,450	-	\$250
31	-3,500										-3,500										
Bal.	\$21,500	+	\$ 0	+	\$200	=	\$ 0	+	\$19,000	-	\$3,500	+	\$9,700	-	\$1,600	-	\$200	-	\$1,450	-	\$250

P-F:1-43A**Requirement 1**

HOMETOWN DÉCOR COMPANY
Income Statement
Year Ended December 31, 2024

Revenue:		
Service Revenue		\$ 225,000
Expenses:		
Salaries Expense	\$ 67,000	
Advertising Expense	17,000	
Rent Expense	14,000	
Interest Expense	6,800	
Property Tax Expense	2,800	
Insurance Expense	1,700	
Total Expenses		<u>109,300</u>
Net Income		<u>\$ 115,700</u>

Requirement 2

HOMETOWN DÉCOR COMPANY
Statement of Owner's Equity
Year Ended December 31, 2024

Hunt, Capital, December 31, 2023	\$ 56,000
Owner contribution	28,000
Net income for the year	<u>115,700</u>
	199,700
Owner withdrawal	<u>(36,000)</u>
Hunt, Capital, December 31, 2024	<u>\$ 163,700</u>

P-F:1-43A, cont.
Requirement 3

HOMETOWN DÉCOR COMPANY
Balance Sheet
December 31, 2024

Assets		Liabilities	
Cash	\$ 2,800	Accounts Payable	\$ 14,000
Accounts Receivable	800	Notes Payable	33,000
Office Supplies	8,000	Salaries Payable	<u>1,300</u>
Land	13,000	Total Liabilities	48,300
Building	170,400		
Equipment	17,000	Owner's Equity	
		Hunt, Capital	<u>163,700</u>
		Total Liabilities and Owner's	
Total Assets	<u>\$ 212,000</u>	Equity	<u>\$ 212,000</u>

P-F:1-44A**Part a.**

PICTURE PERFECT PHOTOGRAPHY**Income Statement****Year Ended December 31, 2024**

Revenue:

Service Revenue \$ 75,000

Expenses:

Salaries Expense \$ 25,000

Insurance Expense 6,000

Advertising Expense 4,000

Total Expenses 35,000

Net Income \$ 40,000

Part b.

PICTURE PERFECT PHOTOGRAPHY**Statement of Owner's Equity****Year Ended December 31, 2024**

Williamson, Capital, December 31, 2023 \$ 16,000

Owner contribution 28,000

Net income for the year 40,000

84,000

Owner withdrawal (8,000)

Williamson, Capital, December 31, 2024 \$ 76,000

Part c.

PICTURE PERFECT PHOTOGRAPHY**Balance Sheet****December 31, 2024**

Assets

Cash \$ 42,000

Accounts Receivable 13,000

Equipment 46,000

Total Assets \$101,000

Liabilities

Accounts Payable \$ 11,000

Notes Payable 14,000

Total Liabilities 25,000

Owner's Equity

Williamson, Capital 76,000

Total Liabilities and Owner's

Equity \$101,000

OUTDOOR LIFE LANDSCAPING

Balance Sheet

November 30, 2024

Assets		Liabilities	
Cash	\$ 4,600	Accounts Payable	\$ 2,700
Accounts Receivable	2,000	Notes Payable	<u>24,600</u>
Office Supplies	600	Total Liabilities	27,300
Land	34,100	Owner's Equity	
Office Furniture	<u>5,800</u>	Tarrant, Capital	<u>19,800</u>
Total assets	<u>\$ 47,100</u>	Total Liabilities and Owner's Equity	<u>\$ 47,100</u>

P-F:1-46A
Requirement 1

ASSETS						=	LIABILITIES			+	EQUITY								
	Cash	+	Accounts Receivable	+	Office Supplies	+	Furniture	=	Accounts Payable	+	Shonton, Capital	–	Shonton, Withdrawals	+	Service Revenue	–	Rent Expense	–	Utilities Expense
5	+75,000										+75,000								
6	–300				+300														
Bal.	\$74,700			+	\$300			=		+	\$75,000								
7							+9,500		+9,500										
Bal.	\$74,700			+	\$300	+	\$9,500	=	\$9,500	+	\$75,000								
10	+4,000														+4,000				
Bal.	\$78,700			+	\$300	+	\$9,500	=	\$9,500	+	\$75,000			+	\$4,000				
11	–190																		–190
Bal.	\$78,510			+	\$300	+	\$9,500	=	\$9,500	+	\$75,000			+	\$4,000		–	\$190	
12			+20,000												+20,000				
Bal.	\$78,510	+	\$20,000	+	\$300	+	\$9,500	=	\$9,500	+	\$75,000			+	\$24,000		–	\$190	
18	–750																–750		
Bal.	\$77,760	+	\$20,000	+	\$300	+	\$9,500	=	\$9,500	+	\$75,000			+	\$24,000	–	\$750	–	\$190
25	+20,000		–20,000																
Bal.	\$97,760		\$ 0	+	\$300	+	\$9,500	=	\$9,500	+	\$75,000			+	\$24,000	–	\$750	–	\$190
27	–9,500								–9,500										
Bal.	\$88,260			+	\$300	+	\$9,500	=	\$ 0	+	\$75,000			+	\$24,000	–	\$750	–	\$190
30	–3,500												–3,500						
Bal.	\$84,760	+	\$ 0	+	\$300	+	\$9,500	=	\$ 0	+	\$75,000	–	\$3,500	+	\$24,000	–	\$750	–	\$190

P-F:1-46A, cont.
Requirement 2a

ALLEN SHONTON, CPA
Income Statement
Month Ended April 30, 2024

Revenue:		
Service Revenue		\$ 24,000
Expenses:		
Rent Expense	\$ 750	
Utilities Expense	190	
Total Expenses		<u>940</u>
Net Income		<u><u>\$ 23,060</u></u>

Requirement 2b

ALLEN SHONTON, CPA
Statement of Owner's Equity
Month Ended April 30, 2024

Shonton, Capital, April 1, 2024	\$ 0
Owner contribution	75,000
Net income for the month	<u>23,060</u>
	98,060
Owner withdrawal	<u>(3,500)</u>
Shonton, Capital, April 30, 2024	<u><u>\$ 94,560</u></u>

Requirement 2c

ALLEN SHONTON, CPA
Balance Sheet
April 30, 2024

Assets		Liabilities	
Cash	\$ 84,760		
Office Supplies	300		
Furniture	9,500	Owner's Equity	
		Shonton, Capital	<u>94,560</u>
		Total Liabilities and Owner's	
Total Assets	<u><u>\$ 94,560</u></u>	Equity	<u><u>\$ 94,560</u></u>

P-F:1-47A
Requirement 1

ASSETS					=	LIABILITIES		+	EQUITY										
	Cash	+	Accounts Receivable	+	Office Supplies	+	Computer	=	Accounts Payable	+	Pachelo, Capital	-	Pachelo, Withdrawals	+	Service Revenue	-	Utilities Expense	-	Miscellaneous Expense
3	+73,000										+73,000								
5	-700				+700														
Bal.	\$72,300			+	\$700			=		+	\$73,000								
7							+5,000		+5,000										
Bal.	\$72,300			+	\$700	+	\$5,000	=	\$5,000	+	\$73,000								
9	+2,800														+2,800				
Bal.	\$75,100			+	\$700	+	\$5,000	=	\$5,000	+	\$73,000			+	\$2,800				
15									+400										-400
Bal.	\$75,100			+	\$700	+	\$5,000	=	\$5,400	+	\$73,000			+	\$2,800	-		-	\$400
23			+10,000												+10,000				
Bal.	\$75,100	+	\$10,000	+	\$700	+	\$5,000	=	\$5,400	+	\$73,000			+	\$12,800	-		-	\$400
28	-400								-400										
Bal.	\$74,700	+	\$10,000	+	\$700	+	\$5,000	=	\$5,000	+	\$73,000			+	\$12,800	-		-	\$400
30	-1,200																-1,200		
Bal.	\$73,500	+	\$10,000	+	\$700	+	\$5,000	=	\$5,000	+	\$73,000			+	\$12,800	-	\$1,200	-	\$400
31	+3,300		-3,300																
Bal.	\$76,800	+	\$6,700	+	\$700	+	\$5,000	=	\$5,000	+	\$73,000			+	\$12,800	-	\$1,200	-	\$400
31	-5,500												-5,500						
Bal.	\$71,300	+	\$6,700	+	\$700	+	\$5,000	=	\$5,000	+	\$73,000	-	\$5,500	+	\$12,800	-	\$1,200	-	\$400

P-F:1-47A, cont.
Requirement 2a

ANNETTE PACHELO, ATTORNEY
Income Statement
Month Ended March 31, 2024

Revenue:		
Service Revenue		\$ 12,800
Expenses:		
Utilities Expense	\$ 1,200	
Miscellaneous Expense	400	
Total Expenses		<u>1,600</u>
Net Income		<u><u>\$ 11,200</u></u>

Requirement 2b

ANNETTE PACHELO, ATTORNEY
Statement of Owner's Equity
Month Ended March 31, 2024

Pachelo, Capital, March 1, 2024	\$ 0
Owner contribution	73,000
Net income for the month	<u>11,200</u>
	84,200
Owner withdrawal	<u>(5,500)</u>
Pachelo, Capital, March 31, 2024	<u><u>\$ 78,700</u></u>

Requirement 2c

ANNETTE PACHELO, ATTORNEY
Balance Sheet
March 31, 2024

Assets		Liabilities	
Cash	\$ 71,300	Accounts Payable	\$ 5,000
Accounts Receivable	6,700		
Office Supplies	700	Owner's Equity	
Computer	<u>5,000</u>	Pachelo, Capital	<u>78,700</u>
		Total Liabilities and Owner's	
Total Assets	<u><u>\$ 83,700</u></u>	Equity	<u><u>\$ 83,700</u></u>

P-F:1-47A, cont.
Requirement 2d

ANNETTE PACHELO, ATTORNEY
Statement of Cash Flows
Month Ended March 31, 2024

Cash flows from operating activities:

Receipts:

Collections from customers \$ 6,100

Payments:

To suppliers (2,300)

Net cash provided by operating activities 3,800

Cash flows from investing activities: 0

Cash flows from financing activities

Owner contribution \$ 73,000

Owner withdrawal (5,500)

Net cash provided by financing activities 67,500

Net increase in cash 71,300

Cash balance, March 1, 2024 0

Cash balance, March 31, 2024 \$ 71,300

Requirement 3

Average total assets = (Beginning total assets + ending total assets) / 2

Average total assets = (\$0 + \$83,700 / 2 = \$41,850

ROA = Net income / Average total assets

ROA = \$11,200 / \$41,850 = 0.27 = 27% (rounded)

Problems Group B

P-F:1-48B

	ASSETS						=	LIABILITIES			+	EQUITY							
	Cash	+	Accounts Receivable	+	Office Supplies	+	Land	=	Accounts Payable	+	McIntyre, Capital	–	McIntyre, Withdrawals	+	Service Revenue	–	Rent Expense	–	Advertising Expense
Bal.	\$2,600	+	\$2,500	+		+	\$16,000	=	\$5,000	+	\$13,600			+	2,500				
(a)	+14,000										+14,000								
Bal.	\$16,600	+	\$2,500			+	\$16,000	=	\$5,000	+	\$27,600			+	2,500				
(b)	+1,600														+1,600				
Bal.	\$18,200	+	\$2,500			+	\$16,000	=	\$5,000	+	\$27,600			+	\$4,100				
(c)	–5,000								–5,000										
Bal.	\$13,200	+	\$2,500			+	\$16,000	=	\$0	+	\$27,600			+	\$4,100				
(d)					+1,200				+1,200										
Bal.	\$13,200	+	\$2,500	+	\$1,200	+	\$16,000	=	\$1,200	+	\$27,600			+	\$4,100				
(e)	+2,300		–2,300																
Bal.	\$15,500	+	\$200	+	\$1,200	+	\$16,000	=	\$1,200	+	\$27,600			+	\$4,100				
(f)	–1,500												–1,500						
Bal.	\$14,000	+	\$200	+	\$1,200	+	\$16,000	=	\$1,200	+	\$27,600	–	\$1,500	+	\$4,100				
(g)			+4,000												+4,000				
Bal.	\$14,000	+	\$4,200	+	\$1,200	+	\$16,000	=	\$1,200	+	\$27,600	–	\$1,500	+	\$8,100				
(h)	–1,350																–900		–450
Bal.	\$12,650	+	\$4,200	+	\$1,200	+	\$16,000	=	\$1,200	+	\$27,600	–	\$1,500	+	\$8,100	–	\$900	–	\$450

P-F:1-49B

	ASSETS				=	LIABILITIES		+	EQUITY												
	Cash	+	Accounts Receivable	+	Office Supplies	=	Accounts Payable	+	Thomas, Capital	–	Thomas, Withdrawals	+	Service Revenue	–	Rent Expense	–	Utilities Expense	–	Wages Expense	–	Advertising Expense
1	+19,000								+19,000												
2	+3,800												+3,800								
Bal.	\$22,800					=		+	\$19,000			+	\$3,800								
5	–300				+300																
Bal.	\$22,500			+	\$300	=		+	\$19,000			+	\$3,800								
9			+4,500										+4,500								
Bal.	\$22,500	+	\$4,500	+	\$300	=		+	\$19,000			+	\$8,300								
10							+150										–150				
Bal.	\$22,500	+	\$4,500	+	\$300	=	\$150	+	\$19,000			+	\$8,300			–	\$150				
15	–350																			–350	
Bal.	\$22,150	+	\$4,500	+	\$300	=	\$150	+	\$19,000			+	\$8,300			–	\$150			–	\$350
20	–150						–150														
Bal.	\$22,000	+	\$4,500	+	\$300	=	\$ 0	+	\$19,000			+	\$8,300			–	\$150			–	\$350
25	+4,500		–4,500																		
Bal.	\$26,500	+	\$ 0	+	\$300	=		+	\$19,000			+	\$8,300			–	\$150			–	\$350
28	–2,600														–2,600						
Bal.	\$23,900			+	\$300	=		+	\$19,000			+	\$8,300	–	\$2,600	–	\$150			–	\$350
28	–1,200																	–1,200			
Bal.	\$22,700			+	\$300	=		+	\$19,000			+	\$8,300	–	\$2,600	–	\$150	–	\$1,200	–	\$350
30	+1,600												+1,600								
Bal.	\$24,300			+	\$300	=		+	\$19,000			+	\$9,900	–	\$2,600	–	\$150	–	\$1,200	–	\$350
31	–3,000									–3,000											
Bal.	\$21,300	+	\$ 0	+	\$300	=	\$ 0	+	\$19,000	–	\$3,000	+	\$9,900	–	\$2,600	–	\$150	–	\$1,200	–	\$350

P-F:1-50B**Requirement 1**

PEMBROKE BOOKKEEPING COMPANY

Income Statement

Year Ended December 31, 2024

Revenues:		
Service Revenue		\$ 192,000
Expenses:		
Salaries Expense	\$ 64,000	
Advertising Expense	12,000	
Rent Expense	7,000	
Interest Expense	6,600	
Property Tax Expense	3,100	
Insurance Expense	1,700	
Total Expenses		94,400
Net Income		<u>\$ 97,600</u>

Requirement 2

PEMBROKE BOOKKEEPING COMPANY

Statement of Owner's Equity

Year Ended December 31, 2024

Pembroke, Capital, December 31, 2023	\$ 51,000
Owner contribution	29,000
Net income for the year	97,600
	<u>177,600</u>
Owner withdrawal	(28,000)
Pembroke, Capital, December 31, 2024	<u>\$ 149,600</u>

Requirement 3

PEMBROKE BOOKKEEPING COMPANY

Balance Sheet

December 31, 2024

Assets		Liabilities	
Cash	\$ 2,800	Accounts Payable	\$ 7,000
Accounts Receivable	1,200	Notes Payable	31,000
Office Supplies	12,000	Salaries Payable	800
Land	10,000	Total Liabilities	<u>38,800</u>
Building	147,400	Owner's Equity	
Equipment	<u>15,000</u>	Pembroke, Capital	<u>149,600</u>
Total Assets	<u>\$ 188,400</u>	Total Liabilities and Owner's Equity	<u>\$ 188,400</u>

P-F:1-51B
Requirement a

PRETTY PICTURES			
Income Statement			
Year Ended December 31, 2024			
Revenues:			
Service Revenue			\$ 115,000
Expenses:			
Salaries Expense	\$ 30,000		
Insurance Expense	6,000		
Advertising Expense	4,500		
Total Expenses			<u>40,500</u>
Net Income			<u>\$ 74,500</u>

Requirement b

PRETTY PICTURES	
Statement of Owner's Equity	
Year Ended December 31, 2024	
Lemon, Capital, December 31, 2023	\$ 20,000
Owner contribution	28,000
Net income for the year	<u>74,500</u>
	122,500
Owner withdrawal	<u>(13,000)</u>
Lemon, Capital, December 31, 2024	<u>\$ 109,500</u>

Requirement c

PRETTY PICTURES			
Balance Sheet			
December 31, 2024			
Assets		Liabilities	
Cash	\$ 42,000	Accounts Payable	\$ 13,000
Accounts Receivable	5,000	Notes Payable	<u>10,000</u>
Equipment	85,500	Total Liabilities	23,000
		Owner's Equity	
		Lemon, Capital	<u>109,500</u>
Total Assets	<u>\$ 132,500</u>	Total Liabilities And Owner's Equity	<u>\$ 132,500</u>

P-F:1-52B

JUNIPER LANDSCAPING**Balance Sheet****July 31, 2024**

Assets		Liabilities	
Cash	\$ 5,300	Accounts Payable	\$ 2,700
Accounts Receivable	1,800	Notes Payable	<u>24,700</u>
Office Supplies	800	Total Liabilities	27,400
Land	34,500		
Office Furniture	6,300	Owner's Equity	
		Simmon, Capital	<u>21,300</u>
		Total Liabilities and Owner's	
Total Assets	<u>\$ 48,700</u>	Equity	<u>\$ 48,700</u>

P-F:1-53B
Requirement 1

	ASSETS					=	LIABILITIES			+	EQUITY								
	Cash	+	Accounts Receivable	+	Office Supplies	+	Office Furniture	=	Accounts Payable	+	Sharp, Capital	-	Sharp, Withdrawals	+	Service Revenue	-	Rent Expense	-	Utilities Expense
5	+45,000										+45,000								
Bal.	\$45,000							=		+	\$45,000								
6	-300				+300														
Bal.	\$44,700			+	\$300			=		+	\$45,000								
7							+6,500		+6,500										
Bal.	\$44,700			+	\$300	+	\$6,500	=	\$6,500	+	\$45,000								
10	+3,300														+3,300				
Bal.	\$48,000			+	\$300	+	\$6,500	=	\$6,500	+	\$45,000			+	\$3,300				
11	-340																	-340	
Bal.	\$47,660			+	\$300	+	\$6,500	=	\$6,500	+	\$45,000			+	\$3,300			-	\$340
12			+16,000												+16,000				
Bal.	\$47,660	+	\$16,000	+	\$300	+	\$6,500	=	\$6,500	+	\$45,000			+	\$19,300			-	\$340
18	-1,800																-1,800		
Bal.	\$45,860	+	\$16,000	+	\$300	+	\$6,500	=	\$6,500	+	\$45,000			+	\$19,300	-	\$1,800	-	\$340
25	+16,000		-16,000																
Bal.	\$61,860		\$ 0	+	\$300	+	\$6,500	=	\$6,500	+	\$45,000			+	\$19,300	-	\$1,800	-	\$340
27	-6,500								-6,500										
Bal.	\$55,360		\$ 0	+	\$300	+	\$6,500	=	\$ 0	+	\$45,000			+	\$19,300	-	\$1,800	-	\$340
31	-3,800												-3,800						
Bal.	\$51,560	+	\$ 0	+	\$300	+	\$6,500	=	\$ 0	+	\$45,000	-	\$3,800	+	\$19,300	-	\$1,800	-	\$340

P-F:1-53B, cont.
Requirement 2a

AMOS SHARP, CPA
Income Statement
Month Ended October 31, 2024

Revenues:		
Service Revenue		\$ 19,300
Expenses:		
Rent Expense	\$ 1,800	
Utilities Expense	340	
Total Expenses		<u>2,140</u>
Net Income		<u>\$ 17,160</u>

Requirement 2b

AMOS SHARP, CPA
Statement of Owner's Equity
Month Ended October 31, 2024

Sharp, Capital, October 1, 2024	\$ 0
Owner contribution	45,000
Net income for the month	<u>17,160</u>
	62,160
Owner withdrawal	<u>(3,800)</u>
Sharp, Capital, October 31, 2024	<u>\$ 58,360</u>

Requirement 2c

AMOS SHARP, CPA
Balance Sheet
October 31, 2024

Assets		Liabilities	
Cash	\$ 51,560		
Office Supplies	300		
Office Furniture	6,500	Owner's Equity	
	<u> </u>	Sharp, Capital	<u>58,360</u>
Total Assets	<u>\$ 58,360</u>	Total Liabilities and Owner's Equity	<u>\$ 58,360</u>

P-F:1-54B
Requirement 1

	ASSETS				=	LIABILITIES		+	EQUITY										
	Cash	+	Accounts Receivable	+	Office Supplies	+	Computer	=	Accounts Payable	+	Perry, Capital	-	Perry, Withdrawals	+	Service Revenue	-	Utility Expense	-	Misc. Expense
3	+89,000										+89,000								
5	-600				+600														
Bal.	\$88,400				\$600	+		=		+	\$89,000								
7							+8,000		+8,000										
Bal.	\$88,400			+	\$600	+	\$8,000	=	\$8,000	+	\$89,000								
9	+2,900														+2,900				
Bal.	\$91,300			+	\$600	+	\$8,000	=	\$8,000	+	\$89,000			+	\$2,900				
15									+300										-300
Bal.	\$91,300			+	\$600	+	\$8,000	=	\$8,300	+	\$89,000			+	\$2,900	-		-	\$300
23			+8,000												+8,000				
Bal.	\$91,300	+	\$8,000	+	\$600	+	\$8,000	=	\$8,300	+	\$89,000			+	\$10,900	-		-	\$300
28	-300								-300										
Bal.	\$91,000	+	\$8,000	+	\$600	+	\$8,000	=	\$8,000	+	\$89,000			+	\$10,900	-		-	\$300
30	-900																-900		
Bal.	\$90,100	+	\$8,000	+	\$600	+	\$8,000	=	\$8,000	+	\$89,000			+	\$10,900	-	\$900	-	\$300
31	+2,800		-2,800																
Bal.	\$92,900	+	\$5,200	+	\$600	+	\$8,000	=	\$8,000	+	\$89,000			+	\$10,900	-	\$900	-	\$300
31	-3,000												-3,000						
Bal.	\$89,900	+	\$5,200	+	\$600	+	\$8,000	=	\$8,000	+	\$89,000	-	\$3,000	+	\$10,900	-	\$900	-	\$300

P-F:1-54B, cont.
Requirement 2a

ABBY PERRY, ATTORNEY			
Income Statement			
Month Ended December 31, 2024			
Revenues:			
Service Revenue			\$ 10,900
Expenses:			
Utility Expense	\$ 900		
Miscellaneous Expense	300		
Total Expenses			1,200
Net Income			<u>\$ 9,700</u>

Requirement 2b

ABBY PERRY, ATTORNEY	
Statement of Owner's Equity	
Month Ended December 31, 2024	
Perry, Capital, December 1, 2024	\$ 0
Owner contribution	89,000
Net income for the month	9,700
	<u>98,700</u>
Owner withdrawal	(3,000)
Perry, Capital, December 31, 2024	<u>\$ 95,700</u>

Requirement 2c

ABBY PERRY, ATTORNEY			
Balance Sheet			
December 31, 2024			
Assets		Liabilities	
Cash	\$ 89,900	Accounts Payable	\$ 8,000
Accounts Receivable	5,200		
Office Supplies	600	Owner's Equity	
Computer	8,000	Perry, Capital	95,700
Total Assets	<u>\$ 103,700</u>	Total Liabilities and Owner's Equity	<u>\$ 103,700</u>

P-F:1-54B, cont.
Requirement 2d

ABBY PERRY, ATTORNEY
Statement of Cash Flows
Month Ended December 31, 2024

Cash flows from operating activities:

Receipts:

Collections from customers \$ 5,700

Payments:

To suppliers (1,800)

Net cash provided by operating activities 3,900

Cash flows from investing activities: 0

Cash flows from financing activities

Owner contribution \$ 89,000

Owner withdrawal (3,000)

Net cash provided by financing activities 86,000

Net increase in cash 89,900

Cash balance, December 1, 2024 0

Cash balance, December 31, 2024 \$ 89,900

Requirement 3

Average total assets = (Beginning total assets + ending total assets) / 2

Average total assets = (\$0 + \$103,700) / 2 = \$51,850

ROA = Net income / Average total assets

ROA = \$9,700 / \$51,850 = 0.19 = 19% (rounded)

Using Excel

The student templates for *Using Excel* are available online in MyLab Accounting in the Multimedia Library or at <http://www.pearsonhighered.com/Horngren>. The solution to *Using Excel* is located in MyLab Accounting in the Instructor Resource Center or at <http://www.pearsonhighered.com/Horngren>.

Continuing Problem

P-F:1-55, Requirement 1

	ASSETS				=	LIABILITIES				+	EQUITY																	
	Cash	+	Accounts Receivable	+	Office Supplies	+	Canoes	=	Accounts Payable	+	Utilities Payable	+	Telephone Payable	+	Wilson, Capital	-	Wilson, Withdrawals	+	Canoe Rental Revenue	-	Rent Expense	-	Utilities Expense	-	Wages Expense	-	Telephone Expense	
1	+16,000														+16,000													
2	-1,200																				-1,200							
Bal.	\$14,800							=							+	\$16,000				-	\$1,200							
3							+4,800		+4,800																			
Bal.	\$14,800						\$4,800	=	\$4,800						+	\$16,000				-	\$1,200							
4					+750				+750																			
Bal.	\$14,800				\$750		\$4,800	=	\$5,550						+	\$16,000				-	\$1,200							
7	+1,400																		+1,400									
Bal.	\$16,200				\$750		\$4,800	=	\$5,550						+	\$16,000			+	\$1,400	-	\$1,200						
13	-1,500																								-1,500			
Bal.	\$14,700				\$750		\$4,800	=	\$5,550						+	\$16,000			+	\$1,400	-	\$1,200				-	\$1,500	
15	-50																-50											
Bal.	\$14,650				\$750		\$4,800	=	\$5,550						+	\$16,000	-	\$50	+	\$1,400	-	\$1,200				-	\$1,500	
16											+150												-150					
Bal.	\$14,650				\$750		\$4,800	=	\$5,550		\$150				+	\$16,000	-	\$50	+	\$1,400	-	\$1,200	-	\$150	-	\$1,500		
20												+175														-175		
Bal.	\$14,650				\$750		\$4,800	=	\$5,550		\$150		\$175		+	\$16,000	-	\$50	+	\$1,400	-	\$1,200	-	\$150	-	\$1,500	-	\$175
22			+3,000																+3,000									
Bal.	\$14,650	+	\$3,000		\$750		\$4,800	=	\$5,550		\$150		\$175		+	\$16,000	-	\$50	+	\$4,400	-	\$1,200	-	\$150	-	\$1,500	-	\$175
26	-1,000								-1,000																			
Bal.	\$13,650	+	\$3,000		\$750		\$4,800	=	\$4,550		\$150		\$175		+	\$16,000	-	\$50	+	\$4,400	-	\$1,200	-	\$150	-	\$1,500	-	\$175
28	+750		-750																									
Bal.	\$14,400	+	\$2,250		\$750		\$4,800	=	\$4,550		\$150		\$175		+	\$16,000	-	\$50	+	\$4,400	-	\$1,200	-	\$150	-	\$1,500	-	\$175
30	-100																-100											
Bal.	\$14,300	+	\$2,250		\$750		\$4,800	=	\$4,550		\$150		\$175		+	\$16,000	-	\$150	+	\$4,400	-	\$1,200	-	\$150	-	\$1,500	-	\$175

P-F:1-55, cont.
Requirement 2

CANYON CANOE COMPANY			
Income Statement			
Month Ended November 30, 2024			
Revenue:			
Canoe Rental Revenue			\$ 4,400
Expenses:			
Wages Expense	\$ 1,500		
Rent Expense	1,200		
Telephone Expense	175		
Utilities Expense	150		
Total Expense			3,025
Net Income			<u>\$ 1,375</u>

Requirement 3

CANYON CANOE COMPANY			
Statement of Owner's Equity			
Month Ended November 30, 2024			
Wilson, Capital, November 1, 2024			\$ 0
Owner contribution			16,000
Net income for the month			1,375
			<u>17,375</u>
Owner withdrawal			(150)
Wilson, Capital, November 30, 2024			<u>\$ 17,225</u>

Requirement 4

CANYON CANOE COMPANY					
Balance Sheet					
November 30, 2024					
	Assets		Liabilities		
Cash	\$ 14,300	Accounts Payable		\$ 4,550	
Accounts Receivable	2,250	Utilities Payable		150	
Office Supplies	750	Telephone Payable		175	
Canoes	4,800	Total Liabilities		<u>4,875</u>	
			Owner's Equity		
		Wilson, Capital		<u>17,225</u>	
		Total Liabilities and Owner's			
Total Assets	<u>\$ 22,100</u>	Equity		<u>\$ 22,100</u>	

P-F:1-55, cont.

Requirement 5

Average total assets = $(\$0 + \$22,100) / 2 = \$11,050$

Return on assets = Net income / Average total assets = $\$1,375 / \$11,050 = 0.124 = 12.4\%$

Critical Thinking

Tying It All Together Case F:1-1 Requirement 1

Starbucks Corporation would report the cost of internet service as an expense on its income statement. Most likely, the expense would be included in Store Operating Expenses.

Requirement 2

When Starbucks receives a bill from its internet service provider, Starbucks would record the following:

Increase Accounts Payable

Increase Store Operating Expenses

This would cause liabilities to increase and equity to decrease.

Requirement 3

When Starbucks pays the bill, Starbucks would record the following:

Decrease Cash

Decrease Accounts Payable

This would cause assets to decrease and liabilities to decrease.

Requirement 4

An increase in the cost of internet service in the coming year would cause expenses to increase. If revenue did not change, this would cause net income to decrease. Starbucks might overcome this impact by charging customers for using the internet service, thereby offsetting the increase in expenses with additional revenue. This change, though, might discourage customers from visiting Starbucks when other competitors might offer free internet service. Another alternative would be to increase the prices of the products sold to cover the increased cost of internet service.

Decision Case F:1-1

Requirement 1

Greg's Tunes has more assets.

Sal's \$23,000, Greg's \$25,000 ($\$10,000 + \$6,000 + \$9,000$)

Requirement 2

Greg's Tunes owes more to creditors.

Sal's \$2,000 ($\$23,000 - (\$8,000 + \$35,000 - \$22,000)$), Greg's \$10,000

Requirement 3

Sal's Silly Songs has more owner's equity.

Sal's \$21,000 ($\$8,000 + \$35,000 - \$22,000$) Greg's \$15,000 ($\$6,000 + \$9,000$)

Requirement 4

Greg's Tunes earned more revenue.

Sal's \$35,000, Greg's \$53,000 ($\$9,000 + \$44,000$)

Requirement 5

Sal's Silly Songs is more profitable.

Sal's \$13,000 ($\$35,000 - \$22,000$), Greg's \$9,000

Requirement 6

This question is opinion based. More profit is good, which means Sal's has the advantage. Greg's also owes more to creditors which is risky. Sal's has much more equity, which minimizes risk.

Requirement 7

Sal's looks financially better, because Sal earned more net income on less total revenue. Sal also owes less to creditors and has more equity.

Ethical Issues F:1-1

Requirement 1

The chief financial officer (CFO) of Philip Morris would be torn between addressing the fact that the payments are related to illnesses caused by the company's products, or alternatively, omitting or concealing this fact. The ethical course of action for the CFO is to be open, honest and forthcoming about the reasons for the payments.

Requirement 2

Negative consequences of not telling the truth are as follows: If users of the financial statements feel they are only getting part of the truth, or that the reports are distorting the information, this will damage the credibility of the company, and damage the company's reputation.

Negative consequences of telling the truth include painting so bleak a picture of the effects of smoking that investors will view Philip Morris as too risky and stop buying the company's stock. Another negative consequence would be to create the impression that the company is engaged in unethical behavior by selling a product that damages people's health.

Fraud Case F:1-1
Requirement 1

The proposed action would increase net income by increasing revenues. It would distort the balance sheet by understating liabilities and overstating equity.

Requirement 2

By making the company's financial situation look better than it actually was, the company's creditors would likely be more willing to extend credit to the company, and offer the credit at a lower interest rate.

Financial Statement Case F:1-1
Requirement 1

\$1,556 (in millions)

Requirement 2

\$41,290 (in millions) at February 2, 2019; \$40,303 (in millions) at February 3, 2018

Requirement 3

Target Corporation adopted Accounting Standards Update (ASU) No. 2014-09—*Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-02—*Leases (Topic 842)*. This required the company to adjust its financial statements for year ending on February 3, 2018.

Requirement 4

Assets	=	Liabilities	+	Equity
\$41,290	=	(\$15,014 + \$14,979)	+	\$11,297
\$41,290	=	\$29,993	+	\$11,297

(shown in millions)

Requirement 5

\$75,356 (in millions) for year ended February 2, 2019. This is an increase of \$2,642 (in millions) over fiscal year 2017. (\$75,356 – \$72,714)

Requirement 6

\$2,937 (in millions) in 2018

\$2,914 (in millions) in 2017

Target's net income increased by \$23 (million) from fiscal 2017 to fiscal 2018 (\$2,937 – \$2,914).

Financial Statement Case F:1-1, cont.
Requirement 7

All amounts in millions.

Average total assets = $(\$40,303 + \$41,290) / 2 = \$40,797$ (rounded)

Return on assets = $\$2,937 / \$40,797 = 0.0719 = 7.2\%$ (rounded)

Requirement 8

Target Corporation's return on assets (7.2%) was one (1) percentage point higher than Kohl's Corporation (6.2%).

Chapter 1

Introduction to Managerial Accounting

Review Questions

1. The primary purpose of managerial accounting is to provide information to help managers plan, direct, control, and make decisions.
2. Financial accounting and managerial accounting differ on the following 6 dimensions: (1) primary users, (2) purpose of information, (3) focus and time dimension of the information, (4) rules and restrictions, (5) scope of information, and (6) behavioral.
3. Line positions are directly involved in providing goods or services to customers. Staff positions support line positions.
4. Planning means choosing goals and deciding how to achieve them. Directing involves running the day-to-day operations of a business. Controlling is the process of monitoring operations and keeping the company on track.
5. The four IMA standards of ethical practice and a description of each follow.
 - I. Competence.
 - Maintain an appropriate level of professional leadership and expertise by enhancing knowledge and skills.
 - Perform professional duties in accordance with relevant laws, regulations, and technical standards.
 - Provide decision support information and recommendations that are accurate, clear, concise, and timely.
 - Recognise and help manage risk.
 - II. Confidentiality.
 - Keep information confidential except when disclosure is authorized or legally required.
 - Inform all relevant parties regarding appropriate use of confidential information. Monitor to ensure compliance.
 - Refrain from using confidential information for unethical or illegal advantage.
 - III. Integrity.
 - Mitigate actual conflicts of interest. Regularly communicate with business associates to avoid apparent conflicts of interest. Advise all parties of any potential conflicts.
 - Refrain from engaging in any conduct that would prejudice carrying out duties ethically.
 - Abstain from engaging in or supporting any activity that might discredit the profession.
 - Contribute to a positive ethical culture and place integrity of the profession above personal interest.

5, cont.

IV. Credibility.

- Communicate information fairly and objectively.
- Provide all relevant information that could reasonably be expected to influence an intended user's understanding of the reports, analyses, or recommendations.
- Report any delays or deficiencies in information, timeliness, processing, or internal controls in conformance with organization policy and/or applicable law.
- Communicate any professional limitations or other constraints that would preclude responsible judgment or successful performance of an activity.

6. Service companies sell time, skills, and knowledge. Examples of service companies include phone service companies, banks, cleaning service companies, accounting firms, law firms, medical physicians, and online auction services.
7. Merchandising companies resell products they buy from suppliers. Merchandisers keep an inventory of products, and managers are accountable for the purchasing, storage, and sale of the products. Examples of merchandising companies include toy stores, grocery stores, and clothing stores.
8. Merchandising companies resell products they previously bought from suppliers, whereas manufacturing companies use labor, equipment, supplies, and facilities to convert raw materials into new finished products. In contrast to merchandising companies, manufacturing companies have a broad range of production activities that require tracking costs on three kinds of inventory.
9. The three inventory accounts used by manufacturing companies are Raw Materials Inventory, Work-in-Process Inventory, and Finished Goods Inventory.

Raw Materials Inventory includes materials used to manufacture a product. Work-in-Process Inventory includes goods that have been started in the manufacturing process but are not yet complete. Finished Goods Inventory includes completed goods that have not yet been sold.

10. A direct cost is a cost that can be easily and cost-effectively traced to a cost object (which is anything for which managers want a separate measurement of cost). An indirect cost is a cost that cannot be easily or cost-effectively traced to a cost object.
11. The three manufacturing costs for a manufacturing company are direct materials, direct labor, and manufacturing overhead. Direct materials are materials that become a physical part of a finished product and whose costs are easily traceable to the finished product. Direct labor is the labor cost of the employees who convert materials into finished products. Manufacturing overhead includes all manufacturing costs except direct materials and direct labor, such as indirect materials, indirect labor, factory depreciation, factory rent, and factory property taxes.

12. Examples of manufacturing overhead include costs of indirect materials, indirect labor, repair and maintenance in factory, factory utilities, factory rent, factory insurance, factory property taxes, manufacturing plant managers' salaries, and depreciation on manufacturing buildings and equipment.
13. Prime costs are direct materials plus direct labor. Conversion costs are direct labor plus manufacturing overhead. Note that direct labor is classified as both a prime cost and a conversion cost.
14. Product costs are the cost of purchasing or making a product. These costs are recorded as an asset and not expensed until the product is sold. Product costs include direct materials, direct labor, and manufacturing overhead.
15. Period costs are non-manufacturing costs that are expensed in the same accounting period in which they are incurred, whereas product costs are recorded as an asset and not expensed until the accounting period in which the product is sold.
16. Cost of Goods Manufactured is calculated as $\text{Beginning Work-in-Process Inventory} + \text{Total Manufacturing Costs Incurred during the Year} - \text{Ending Work-in-Process Inventory}$. $\text{Total Manufacturing Costs Incurred during the Year} = \text{Direct Materials Used} + \text{Direct Labor} + \text{Manufacturing Overhead}$.
17. For a manufacturing company, the activity in the Finished Goods Inventory account provides the information for determining Cost of Goods Sold. A manufacturing company calculates Cost of Goods Sold as $\text{Beginning Finished Goods Inventory} + \text{Cost of Goods Manufactured} - \text{Ending Finished Good Inventory}$. In addition, a manufacturing company must track costs from Raw Materials Inventory and Work-in-Process Inventory in order to compute Cost of Goods Manufactured used in the previous equation.

For a merchandising company, the activity in the Merchandise Inventory account provides the information for determining Cost of Goods Sold. A merchandising company calculates Cost of Goods Sold as $\text{Beginning Merchandise Inventory} + \text{Purchases and Freight In} - \text{Ending Merchandise Inventory}$.
18. A manufacturing company calculates unit product cost as $\text{Cost of Goods Manufactured} / \text{Total number of units produced}$.
19. A service company calculates unit cost per service as $\text{Total operating costs} / \text{Total number of services provided}$.
20. A merchandising company calculates unit cost per item as $\text{Total cost of goods sold} / \text{Total number of items sold}$.

Short Exercises

S-M:1-1

- a. FA
- b. MA
- c. MA
- d. FA
- e. FA

S-M:1-2

- a. Confidentiality
- b. Integrity
- c. Competence (skipping the session); Integrity (company-paid conference)
- d. Competence
- e. Credibility; Integrity

S-M:1-3

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

S-M:1-4

Glue for frames	\$ 250
Plant depreciation	7,500
Plant foreman's salary	3,500
Plant janitor's wages	1,300
Oil for manufacturing equipment	150
Total manufacturing overhead	<u>\$ 12,700</u>

S-M:1-5

- a. Period cost
- b. Product cost
- c. Product cost
- d. Period cost
- e. Product cost
- f. Period cost
- g. Product cost
- h. Product cost
- i. Period cost

S-M:1-6

Beginning merchandise inventory		\$ 8,600
Purchases	\$ 47,000	
Freight in	<u>2,400</u>	<u>49,400</u>
Cost of goods available for sale		58,000
Ending merchandise inventory		<u>(5,500)</u>
Cost of goods sold		<u><u>\$ 52,500</u></u>

S-M:1-7

	<u>Solu- tions:</u>	<u>Calculations:</u>
(a)	\$13,200	\$63,200 [b, below] – \$50,000
(b)	\$63,200	\$61,000 + \$2,200
(c)	\$28,000	\$40,000 – \$12,000
(d)	\$200,800	\$86,800 [f, below] + 114,000
(e)	\$60,000	\$89,000 – \$29,000
(f)	\$86,800	\$89,000 – \$2,200
(g)	\$30,000	\$114,000 – \$84,000

Order of calculations:

Smith, Inc.: (b), (a), (c)

Allen, Inc.: (e), (f), (d), and (g)

S-M:1-8

Beginning Direct Materials		\$ 4,100
Purchases of Direct Materials	\$ 6,300	
Freight In	<u>400</u>	<u>6,700</u>
Direct Materials Available for Use		10,800
Ending Direct Materials		<u>(1,300)</u>
Direct Materials Used		<u><u>\$ 9,500</u></u>

S-M:1-9

Beginning Work-in-Process Inventory		\$ 1,000
Direct Materials Used	\$ 12,000	
Direct Labor	9,000	
Manufacturing Overhead	<u>21,000</u>	
Total Manufacturing Costs Incurred during the Year		<u>42,000</u>
Total Manufacturing Costs to Account For		43,000
Ending Work-in-Process Inventory		<u>(5,000)</u>
Cost of Goods Manufactured		<u><u>\$ 38,000</u></u>

S-M:1-10

Beginning Finished Goods Inventory	\$ 30,000
Cost of Goods Manufactured	<u>165,000</u>
Cost of Goods Available for Sale	195,000
Ending Finished Goods Inventory	<u>(10,000)</u>
Cost of Goods Sold	<u><u>\$ 185,000</u></u>

S-M:1-11

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

S-M:1-12

$$\begin{aligned}
 \text{Cost of one haircut} &= \text{Total operating costs} / \text{Total number of haircuts} \\
 &= [\$950 + \$548 + \$190 + \$60] / 190 \text{ haircuts} \\
 &= \$1,748 / 190 \text{ haircuts} \\
 &= \$9.20 \text{ per haircut}
 \end{aligned}$$

Exercises

E-M:1-13

- a. Financial
- b. Creditors and Stockholders
- c. Controlling
- d. Managers
- e. Financial
- f. Managerial
- g. Planning

E-M:1-14

Students' responses will vary. Illustrative answers follow.

Requirement 1

A new employee who has engaged in this behavior is unlikely to become a valued and trusted employee. This type of behavior is unethical, and Sue Peters should consider beginning the process to terminate the employee. Any company policies with respect to discipline and termination should be followed.

As controller, Sue Peters probably hired Dale, and she is also responsible for the lack of controls that permitted a new employee to commit this theft. She will need to supervise Dale and subsequent bookkeepers more carefully.

Requirement 2

Being a new employee, Sue Peters may want to discuss the situation with her immediate supervisor or the company's president if appropriate. Unless Sue can obtain additional information, she may want to indicate to Dale that this behavior will not be tolerated in the future. Sue should establish better controls and closer supervision.

E-M:1-15

Cost	Product					Period	
	DM	DL	MOH	Prime	Conversion	Selling	Admin
a. Metal used for rims	X			X			
b. Sales salaries						X	
c. Rent on factory			X		X		
d. Wages of assembly workers		X		X	X		
e. Salary of production supervisor			X		X		
f. Depreciation on office equipment							X
g. Salary of CEO							X
h. Delivery expense						X	

E-M:1-16

Company A is a manufacturing company. Company B is a service company. Company C is a merchandising company.

E-M:1-17

Company A (all amounts in millions):

Net Sales Revenue	\$ 48
Cost of Goods Sold	<u>23</u>
Gross Profit	25
Selling and Administrative Expenses:	
Selling Expenses	\$ 4
Administrative Expenses	<u>7</u>
Total Selling and Administrative Expenses	11
Operating Income	<u><u>\$ 14</u></u>

Company B (all amounts in millions):

Service Revenue	\$ 65
Expenses:	
Wages Expense	\$ 12
Rent Expense	<u>12</u>
Total Expenses	24
Operating Income	<u><u>\$ 41</u></u>

Company C (all amounts in millions):

Net Sales Revenue	\$ 75
Cost of Goods Sold	<u>25</u>
Gross Profit	50
Selling and Administrative Expenses:	
Selling Expenses	\$ 8
Administrative Expenses	<u>4</u>
Total Selling and Administrative Expenses	12
Operating Income	<u><u>\$ 38</u></u>

E-M:1-18

Company A (all amounts in millions):

Cash	\$ 6
Accounts Receivable	14
Raw Materials Inventory	6
Work-in-Process Inventory	9
Finished Goods Inventory	<u>10</u>
Total current assets	<u>\$ 45</u>

Company B (all amounts in millions):

Cash	\$ 34
Accounts Receivable	<u>8</u>
Total current assets	<u>\$ 42</u>

Company C (all amounts in millions):

Cash	\$ 25
Accounts Receivable	19
Merchandise Inventory	<u>12</u>
Total current assets	<u>\$ 56</u>

E-M:1-19

(a)

Total Manufacturing Costs to Account For	\$ 55,400
Total Manufacturing Costs Incurred during the Year	<u>(45,200)</u>
Beginning Work-in-Process Inventory	<u>\$ 10,200</u>

(b)

Total Manufacturing Costs Incurred during the Year	\$ 45,200
Direct Materials Used	(14,400)
Direct Labor	<u>(10,300)</u>
Manufacturing Overhead	<u>\$ 20,500</u>

(c)

Total Manufacturing Costs to Account For	\$ 55,400
Cost of Goods Manufactured	<u>(50,500)</u>
Ending Work-in-Process Inventory	<u>\$ 4,900</u>

(d)

Direct Materials Used	\$ 35,900
Direct Labor	20,100
Manufacturing Overhead	<u>10,000</u>
Total Manufacturing Costs Incurred during the Year	<u>\$ 66,000</u>

(e)

Beginning Work-in-Process Inventory	\$ 40,800
Total Manufacturing Costs Incurred during the Year [d, above]	<u>66,000</u>
Total Manufacturing Costs to Account For	<u>\$ 106,800</u>

(f)

Total Manufacturing Costs to Account For [e, above]	\$ 106,800
Ending Work-in-Process Inventory	<u>(25,500)</u>
Cost of Goods Manufactured	<u>\$ 81,300</u>

E-M:1-19, cont.

(g)

Total Manufacturing Costs Incurred during the Year [h, below]	\$ 6,100
Direct Labor	(1,900)
Manufacturing Overhead	<u>(900)</u>
Direct Materials Used	<u><u>\$ 3,300</u></u>

(h)

Total Manufacturing Costs to Account For	\$ 8,300
Beginning Work-in-Process Inventory	<u>(2,200)</u>
Total Manufacturing Costs Incurred During the Year	<u><u>\$ 6,100</u></u>

(i)

Total Manufacturing Costs to Account For	\$ 8,300
Ending Work-in-Process Inventory	<u>(2,600)</u>
Cost of Goods Manufactured	<u><u>\$ 5,700</u></u>

E-M:1-20
Requirement 1

WILSON CORP. Schedule of Cost of Goods Manufactured Year Ended December 31, 2024			
Beginning Work-in-Process Inventory			\$ 109,000
Direct Materials Used:			
Beginning Direct Materials	\$ 59,000		
Purchases of Direct Materials	151,000		
Direct Materials Available for Use	210,000		
Ending Direct Materials	(23,000)		
Direct Materials Used		\$ 187,000	
Direct Labor		121,000	
Manufacturing Overhead:			
Depreciation, plant building and equipment	16,000		
Insurance on plant	24,000		
Repairs and maintenance—plant	10,000		
Indirect labor	39,000		
Total Manufacturing Overhead		89,000	
Total Manufacturing Costs Incurred During the Year			397,000
Total Manufacturing Costs to Account For			506,000
Ending Work-in-Process Inventory			(62,000)
Cost of Goods Manufactured			\$ 444,000

Requirement 2

$$\begin{aligned}
 \text{Unit product cost} &= \text{Cost of goods manufactured} / \text{Total units produced} \\
 &= \$444,000 / 3,700 \text{ lamps} \\
 &= \$120 \text{ per lamp}
 \end{aligned}$$

E-M:1-21

Beginning Work-in-Process Inventory		\$ 40,000
Direct Materials Used:		
Beginning Direct Materials	\$ 27,000	
Purchases of Direct Materials	73,000	
Direct Materials Available for Use	<u>100,000</u>	
Ending Direct Materials	<u>(28,000)</u>	
Direct Materials Used		\$ 72,000
Direct Labor		88,000
Manufacturing Overhead		<u>43,000</u>
Total Manufacturing Costs Incurred During the Year		<u>203,000</u>
Total Manufacturing Costs to Account For		243,000
Ending Work-in-Process Inventory		<u>(32,000)</u>
Cost of Goods Manufactured		<u><u>\$ 211,000</u></u>

Beginning Finished Goods Inventory	\$ 18,000	
Cost of Goods Manufactured	<u>211,000</u>	[above]
Cost of Goods Available for Sale	229,000	
Ending Finished Goods Inventory	<u>(25,000)</u>	
Cost of Goods Sold	<u><u>\$ 204,000</u></u>	

E-M:1-22

- a. JIT
- b. TQM
- c. ERP
- d. E-Commerce

E-M:1-23

a.	People
b.	Planet
c.	Planet
d.	Profit

E16-24**Requirement 1**

Grooming Revenue		\$ 16,300
Expenses:		
Wages Expense	\$ 4,061	
Grooming Supplies Expense	1,675	
Building Rent Expense	900	
Utilities Expense	305	
Depreciation Expense—Equipment	55	
Total Expenses		<u>6,996</u>
Operating Income		<u><u>\$ 9,304</u></u>

Requirement 2

$$\begin{aligned}
 \text{Cost of Service to Groom One Dog} &= \text{Total operating expenses} / \text{Total number of dogs groomed} \\
 &= \$6,996 / 660 \text{ dogs} \\
 &= \$10.60 \text{ per dog}
 \end{aligned}$$

E-M:1-25**Requirement 1**

Net Sales Revenue		\$ 151,800
Cost of Goods Sold:		
Beginning Merchandise Inventory	\$ 7,920	
Purchases	85,800	
Cost of Goods Available for Sale	93,720	
Ending Merchandise Inventory	(11,748)	
Cost of Goods Sold		81,972
Gross Profit		69,828
Selling and Administrative Expenses		47,058
Operating Income		\$ 22,770

Requirement 2

$$\begin{aligned}\text{Unit cost for one brush} &= \text{Cost of goods sold} / \text{Total units sold} \\ &= \$81,972 / 6,600 \text{ brushes} \\ &= \$12.42 \text{ per brush}\end{aligned}$$

Problems (Group A)

P-M:1-26A

Students' responses will vary. Illustrative answers follow.

Requirement 1

- a. If the goods have been received, postponing recording of the purchases understates liabilities. This is unethical and inconsistent with the IMA standards even if the suppliers agree to delay billing.
- b. The software has not been sold. Therefore, it would be inconsistent with the IMA standards to record it as sales.
- c. Delaying year-end closing incorrectly records next year's sales in this year's sales. This is unethical and inconsistent with the IMA standards.
- d. The appropriate allowance for bad debts is a difficult judgment. The decision should not be driven by the desire to meet a profit goal. It should be based on the likelihood that the company will not collect the debts. We cannot determine this without more information. However, since the company emphasizes earnings growth, which can lead to sales to customers with weaker credit records, reducing the allowance seems questionable. It is not clear whether this strategy is inconsistent with the IMA standards.
- e. If the maintenance is postponed, there is no transaction to record. This strategy is beyond the responsibility of the controller, so it does not violate IMA standards.

Requirement 2

The inconsistencies noted for Smart Software, Inc. particularly impact the financial statement information provided by financial accounting to external users, such as creditors and stockholders. They will be led to believe the operating performance (profitability) of the company is better than it really is. This misrepresentation may result in the investors holding the stock when they may have sold it with the correct information. Similarly, creditors may grant credit to the company with the false income information when they may not grant credit with the correct income information.

Requirement 3

The controller should resist attempts to implement a, b, and c and should gather more information about d. If the President ignores Wallace, then Wallace needs to consider if she wants to work for a company that engages in unethical behavior. Accountants should not be associated with any unethical behavior, and Wallace should resign.

P-M:1-27A**Requirement 1**

Period costs are non-manufacturing costs that are expensed in the accounting period in which they are incurred.

Product costs are all costs of purchasing or making a product. These costs are recorded as an asset (inventory) on the balance sheet until the asset is sold. The cost is then transferred to an expense account (Cost of Goods Sold) on the income statement. Product costs include direct materials, direct labor, and manufacturing overhead.

On the income statement, Cost of Goods Sold (product cost) is subtracted from Net Sales Revenue to determine gross profit. The period costs are then subtracted to determine operating income.

Requirement 2

Cost:	Period Cost	Product Cost		
		Direct Materials	Direct Labor	Manufacturing Overhead
Shaft and handle of weed trimmer		X		
Motor of weed trimmer		X		
Factory labor for workers assembling weed trimmers			X	
Nylon thread used by the weed trimmer (not traced to the product)				X
Glue to hold housing together				X
Plant janitorial wages				X
Depreciation on factory equipment				X
Rent on plant				X
Sales commissions	X			
Administrative salaries	X			
Plant utilities				X
Shipping costs to deliver finished weed trimmers to customers	X			

P-M:1-28A**Requirement 1**

Service companies sell services rather than products. They sell time, skills, and knowledge. Merchandising companies resell products previously bought from suppliers. Manufacturing companies use labor, equipment, supplies, and facilities to convert raw materials into new finished products.

Requirement 2

Company A is a merchandising company. Company B is a manufacturing company. The company types can be determined by the account names in the ledger.

Requirement 3

Company A:

Beginning Merchandise Inventory	\$ 10,600
Purchases (net)	154,500
Cost of Goods Available for Sale	<u>165,100</u>
Ending Merchandise Inventory	<u>(13,100)</u>
Cost of Goods Sold	<u><u>\$ 152,000</u></u>

Company B:

Beginning Finished Goods Inventory	\$ 15,000
Cost of Goods Manufactured	214,500
Cost of Goods Available for Sale	<u>229,500</u>
Ending Finished Goods Inventory	<u>(11,700)</u>
Cost of Goods Sold	<u><u>\$ 217,800</u></u>

P-M:1-29A
Requirement 1

GOURMET BONES
Schedule of Cost of Goods Manufactured
Year Ended December 31, 2024

Beginning Work-in-Process Inventory		\$	0
Direct Materials Used:			
Beginning Direct Materials	\$ 13,500		
Purchases of Direct Materials	36,000		
Direct Materials Available for Use	<u>49,500</u>		
Ending Direct Materials	<u>(7,500)</u>		
Direct Materials Used		\$ 42,000	
Direct Labor		23,000	
Manufacturing Overhead:			
Plant janitorial services	700		
Utilities for plant	1,300		
Rent on plant	<u>17,000</u>		
Total Manufacturing Overhead		<u>19,000</u>	
Total Manufacturing Costs Incurred during the Year			<u>84,000</u>
Total Manufacturing Costs to Account For			84,000
Ending Work-in-Process Inventory			<u>(3,500)</u>
Cost of Goods Manufactured			<u><u>\$ 80,500</u></u>

P-M:1-29A, cont.
Requirement 2

GOURMET BONES
Income Statement
Year Ended December 31, 2024

Net Sales Revenue		\$ 107,000
Cost of Goods Sold:		
Beginning Finished Goods Inventory	\$ 0	
Cost of Goods Manufactured*	80,500	
Cost of Goods Available for Sale	<u>80,500</u>	
Ending Finished Goods Inventory	<u>(5,200)</u>	
Cost of Goods Sold		<u>75,300</u>
Gross Profit		31,700
Selling and Administrative Expenses:		
Sales Salaries Expense	6,000	
Delivery Expense	1,300	
Customer Service Hotline Expense	<u>1,200</u>	
Total Selling and Administrative Expenses		<u>8,500</u>
Operating Income (Loss)		<u><u>\$ 23,200</u></u>

* From the Schedule of Cost of Goods Manufactured in Requirement 1.

Requirement 3

For a manufacturing company, cost of goods sold on the income statement is based on cost of goods manufactured and the change in Finished Goods Inventory. For a merchandising company, cost of goods sold on the income statement is based on cost of merchandise purchased (including freight in) and the change in Merchandise Inventory.

Requirement 4

$$\begin{aligned}\text{Unit product cost} &= \text{Cost of goods manufactured} / \text{Total units produced} \\ &= \$80,500 / 17,900 \text{ units} \\ &= \$4.50 \text{ per unit (rounded to nearest cent)}\end{aligned}$$

ELLY MANUFACTURING COMPANY
Schedule of Cost of Goods Manufactured
Month Ended June 30, 2024

Beginning <u>Work-in-Process Inventory</u>		\$ 27,000
Direct <u>Materials Used</u> :		
Beginning Direct Materials	\$ 28,000	
Purchases of Direct Materials	56,000	
<u>Direct Materials Available for Use</u>	84,000	
Ending Direct Materials	(20,000)	
Direct <u>Materials Used</u>		64,000
Direct <u>Labor</u>		72,000
Manufacturing Overhead		44,000
Total <u>Manufacturing Costs Incurred During the Month</u>		<u>180,000</u>
Total <u>Manufacturing Costs to Account For</u>		207,000
Ending <u>Work-in-Process Inventory</u>		(25,000)
<u>Cost of Goods Manufactured</u>		<u>\$ 182,000</u>

Missing Amounts:

Beginning Direct Materials

Direct Materials Available for Use	\$ 84,000
Purchases of Direct Materials	(56,000)
Beginning Direct Materials	<u>\$ 28,000</u>

Direct Materials Used:

Direct Materials Available for Use	\$ 84,000
Ending Direct Materials	(20,000)
Direct Materials Used	<u>\$ 64,000</u>

Direct Labor:

Total Manufacturing Costs Incurred During the Month	\$ 180,000
Manufacturing Overhead	(44,000)
Direct Materials Used [calculated above]	(64,000)
Direct Labor	<u>\$ 72,000</u>

P-M:1-30A, cont.

Total Manufacturing Costs to Account For:

Beginning Work-in-Process Inventory	\$ 27,000
Total Manufacturing Costs Incurred During the Month	180,000
Total Manufacturing Costs to Account For	<u>\$ 207,000</u>

Cost of Goods Manufactured:

Total Manufacturing Costs to Account For [calculated above]	\$ 207,000
Ending Work-in-Process Inventory	<u>(25,000)</u>
Cost of Goods Manufactured	<u>\$ 182,000</u>

ELLY MANUFACTURING COMPANY

Income Statement

Month Ended June 30, 2024

Net Sales Revenue		\$ 490,000
Cost of Goods Sold:		
Beginning <u>Finished Goods Inventory</u>	\$ 110,000	
<u>Cost of Goods Manufactured</u>	<u>182,000</u>	
Cost of Goods <u>Available for Sale</u>	<u>292,000</u>	
Ending <u>Finished Goods Inventory</u>	<u>(60,000)</u>	
Cost of Goods Sold		<u>232,000</u>
Gross Profit		258,000
<u>Selling and Administrative Expenses:</u>		
Selling Expenses	98,000	
Administrative Expenses	<u>62,000</u>	
Total <u>Selling and Administrative Expenses</u>		<u>160,000</u>
<u>Operating Income</u>		<u>\$ 98,000</u>

Missing Amounts:

Net Sales Revenue:

Cost of Goods Sold	\$ 232,000
Gross Profit	<u>258,000</u>
Net Sales Revenue	<u>\$ 490,000</u>

P-M:1-30A, cont.

Cost of Goods Manufactured:

[From the Schedule of Cost of Goods Manufactured]

Cost of Goods Available for Sale:

Beginning Finished Goods Inventory	\$ 110,000
Cost of Goods Manufactured	<u>182,000</u>
Cost of Goods Available for Sale	<u><u>\$ 292,000</u></u>

Ending Finished Goods Inventory:

Cost of Goods Available for Sale [calculated above]	\$ 292,000
Cost of Goods Sold	<u>(232,000)</u>
Ending Finished Goods Inventory	<u><u>\$ 60,000</u></u>

Administrative Expenses:

Total Selling and Administrative Expenses	\$ 160,000
Selling Expenses	<u>(98,000)</u>
Administrative Expenses	<u><u>\$ 62,000</u></u>

Operating Income:

Gross Profit	\$ 258,000
Total Selling and Administrative Expenses	<u>(160,000)</u>
Operating Income	<u><u>\$ 98,000</u></u>

P-M:1-31A
Requirement 1

Cost of direct materials purchased:

$$\begin{array}{rcccl} \text{Direct} & & \text{Beginning} & & \text{Purchases of} & & \text{Ending} \\ \text{Materials Used} & = & \text{Direct Materials} & + & \text{Direct Materials} & - & \text{Direct Materials} \end{array}$$

Solving for cost of direct materials purchased:

$$\begin{array}{rcccl} \text{Purchases of} & & \text{Direct} & & \text{Ending} & & \text{Beginning} \\ \text{Direct} & = & \text{Materials} & + & \text{Direct Materials} & - & \text{Direct Materials} \\ \text{Materials} & & \text{Used} & & & & \\ & = & \$2,000,000 & + & \$800,000 & - & \$700,000 \\ & = & \$2,100,000 & & & & \end{array}$$

Requirement 2

Cost of goods manufactured for the year:

$$\begin{array}{rcccl} \text{Cost of} & & \text{Beginning} & & \text{Total} & & \text{Ending} \\ \text{Goods} & = & \text{Work-in-Process} & + & \text{Manufacturing} & - & \text{Work-in-Process} \\ \text{Manufactured} & & \text{Inventory} & & \text{Costs Incurred} & & \text{Inventory} \\ & = & \$1,500,000 & + & \$26,300,000 & - & \$1,200,000 \\ & = & \$26,600,000 & & & & \end{array}$$

Requirement 3

Cost of goods sold for the year:

$$\begin{array}{rcccl} \text{Cost of} & & \text{Beginning} & & \text{Cost of} & & \text{Ending} \\ \text{Goods} & = & \text{Finished Goods} & + & \text{Goods} & - & \text{Finished Goods} \\ \text{Sold} & & \text{Inventory} & & \text{Manufactured} & & \text{Inventory} \\ & = & \$400,000 & + & \$26,600,000 & - & \$600,000 \\ & & & & \text{[calculated in 2]} & & \\ & = & \$26,400,000 & & & & \end{array}$$

P-M:1-32A
Requirement 1

THE WINDSHIELD DOCTORS
Income Statement
Month Ended March 31, 2024

Revenues:		
Net Service Revenue		\$ 23,000
Expenses:		
Salaries and Wages Expense	\$ 12,000	
Materials Expense	4,600	
Depreciation Expense—Truck	300	
Depreciation Expense—Building and Equipment	1,200	
Supplies Expense	300	
Utilities Expense	460	
Total Expenses		<u>18,860</u>
Operating Income		<u><u>\$ 4,140</u></u>

Requirement 2

$$\begin{aligned}\text{Unit cost} &= \text{Total operating expenses} / \text{Total windshields repaired} \\ &= \$18,860 / 500 \text{ windshields} \\ &= \$37.72 \text{ per windshield}\end{aligned}$$

Requirement 3

Yes. The actual unit cost per windshield of \$37.72 is less than \$50.

P-M:1-33A
Requirement 1

CLYDE'S PETS
Income Statement
Year Ended December 31, 2024

Net Sales Revenue		\$ 56,000
Cost of Goods Sold:		
Beginning Merchandise Inventory	\$ 15,900	
Purchases of Merchandise	25,000	
Cost of Goods Available for Sale	<u>40,900</u>	
Ending Merchandise Inventory	<u>(10,100)</u>	
Cost of Goods Sold		<u>30,800</u>
Gross Profit		25,200
Selling and Administrative Expenses:		
Utilities Expense	3,300	
Rent Expense	4,100	
Sales Commission Expense	<u>2,650</u>	
Total Selling and Administrative Expenses		<u>10,050</u>
Operating Income		<u><u>\$ 15,150</u></u>

Requirement 2

$$\begin{aligned}\text{Unit cost} &= \text{Cost of goods sold} / \text{Total units sold} \\ &= \$30,800 / 3,850 \text{ units} \\ &= \$8.00 \text{ per unit}\end{aligned}$$

Problems (Group B)

P-M:1-34B

Students' responses will vary. Illustrative answers follow.

Requirement 1

- a. If the goods have been received, postponing recording of the purchases understates liabilities. This is unethical and inconsistent with the IMA standards even if the suppliers agree to delay billing.
- b. The software has not been sold. Therefore, it would be inconsistent with the IMA standards to record it as sales.
- c. Delaying year-end closing incorrectly records next year's sales in this year's sales. This is unethical and inconsistent with the IMA standards.
- d. The appropriate allowance for bad debts is a difficult judgment. The decision should not be driven by the desire to meet a profit goal. It should be based on the likelihood that the company will not collect the debts. We cannot determine this without more information. However, since the company emphasizes earnings growth, which can lead to sales to customers with weaker credit records, reducing the allowance seems questionable. It is not clear whether this strategy is inconsistent with the IMA standards.
- e. If the maintenance is postponed, there is no transaction to record. This strategy is beyond the responsibility of the controller, so it does not violate IMA standards.

Requirement 2

The inconsistencies noted for Halo Software, Inc. particularly impact the financial statement information provided by financial accounting to external users, such as creditors and stockholders. They will be led to believe the operating performance (profitability) of the company is better than it really is. This misrepresentation may result in the investors holding the stock when they may have sold it with the correct information. Similarly, creditors may grant credit to the company with the false income information when they may not grant credit with the correct income information.

Requirement 3

The controller should resist attempts to implement a, b, and c and should gather more information about d. If the President ignores Borzi, then Borzi needs to consider if she wants to work for a company that engages in unethical behavior. Borzi should not be associated with unethical behavior and should resign.

P-M:1-35B**Requirement 1**

Period costs are non-manufacturing costs that are expensed in the accounting period in which they are incurred.

Product costs are the costs of purchasing or making a product. These costs are recorded as an asset (inventory) on the balance sheet until the asset is sold. The cost is then transferred to an expense account (Cost of Goods Sold) on the income statement. Product costs include direct materials, direct labor, and manufacturing overhead.

On the income statement, Cost of Goods Sold (product cost) is subtracted from Net Sales Revenue to determine gross profit. The period costs are then subtracted from gross profit to determine operating income.

Requirement 2

Cost:	Period Cost	Product Cost		
		Direct Materials	Direct Labor	Manufacturing Overhead
Handle and shaft of edger		X		
Motor of edger		X		
Factory labor for workers assembling edgers			X	
Lubricant used on bearings in the edger (not traced to the product)				X
Glue to hold housing together				X
Plant janitorial wages				X
Depreciation on factory equipment				X
Rent on plant				X
Sales commissions	X			
Administrative salaries	X			
Plant utilities				X
Shipping costs to deliver finished edgers to customers	X			

P-M:1-36B**Requirement 1**

Service companies sell services rather than products. They sell time, skills, and knowledge. Merchandising companies resell products previously bought from suppliers. Manufacturing companies use labor, equipment, supplies, and facilities to convert raw materials into new finished products.

Requirement 2

Company 1 is a merchandising company. Company 2 is a manufacturing company. The company type can be determined by the account names in the ledger.

Requirement 3

Company 1:

Beginning Merchandise Inventory	\$ 11,600
Purchases (net)	152,500
Cost of Goods Available for Sale	<u>164,100</u>
Ending Merchandise Inventory	<u>(12,400)</u>
Cost of Goods Sold	<u><u>\$ 151,700</u></u>

Company 2:

Beginning Finished Goods Inventory	\$ 15,400
Cost of Goods Manufactured	214,500
Cost of Goods Available for Sale	<u>229,900</u>
Ending Finished Goods Inventory	<u>(11,300)</u>
Cost of Goods Sold	<u><u>\$ 218,600</u></u>

P-M:1-37B
Requirement 1

CHEWY BONES			
Schedule of Cost of Goods Manufactured			
Year Ended December 31, 2024			
Beginning Work-in-Process Inventory		\$	0
Direct Materials Used:			
Beginning Direct Materials	\$ 13,400		
Purchases of Direct Materials	39,000		
Direct Materials Available for Use	<u>52,400</u>		
Ending Direct Materials	<u>(10,500)</u>		
Direct Materials Used		\$ 41,900	
Direct Labor		16,000	
Manufacturing Overhead:			
Plant janitorial services	900		
Utilities for plant	1,200		
Rent on plant	<u>9,000</u>		
Total Manufacturing Overhead		<u>11,100</u>	
Total Manufacturing Costs Incurred during the Year			<u>69,000</u>
Total Manufacturing Costs to Account For			69,000
Ending Work-in-Process Inventory			<u>(1,500)</u>
Cost of Goods Manufactured			<u><u>\$ 67,500</u></u>

P-M:1-37B, cont.
Requirement 2

CHEWY BONES
Income Statement
Year Ended December 31, 2024

Net Sales Revenue		\$ 115,000
Cost of Goods Sold:		
Beginning Finished Goods Inventory	\$ 0	
Cost of Goods Manufactured*	67,500	
Cost of Goods Available for Sale	67,500	
Ending Finished Goods Inventory	(5,400)	
Cost of Goods Sold		62,100
Gross Profit		52,900
Selling and Administrative Expenses:		
Sales Salaries Expense	5,100	
Delivery Expense	1,700	
Customer Service Hotline Expense	1,600	
Total Selling and Administrative Expenses		8,400
Operating Income (Loss)		\$ 44,500

* From the Schedule of Cost of Goods Manufactured in Requirement 1.

Requirement 3

For a manufacturing company, cost of goods sold on the income statement is based on cost of goods manufactured and the change in Finished Goods Inventory. For a merchandising company, cost of goods sold on the income statement is based on cost of merchandise purchased (including freight in) and the change in Merchandise Inventory.

Requirement 4

$$\begin{aligned}\text{Unit cost} &= \text{Cost of goods manufactured} / \text{Total units produced} \\ &= \$67,500 / 17,500 \text{ units} \\ &= \$3.86 \text{ per unit (rounded to the nearest cent)}\end{aligned}$$

CHARLIE MANUFACTURING COMPANY
Schedule of Cost of Goods Manufactured
Month Ended June 30, 2024

Beginning <u>Work-in-Process Inventory</u>		\$ 26,000
Direct <u>Materials Used</u> :		
Beginning Direct Materials	\$ 30,000	
Purchases of Direct Materials	51,000	
<u>Direct Materials Available for Use</u>	81,000	
Ending Direct Materials	(26,000)	
Direct <u>Materials Used</u>		\$ 55,000
Direct <u>Labor</u>		72,000
Manufacturing Overhead		50,000
Total <u>Manufacturing Costs Incurred During the Month</u>		177,000
Total <u>Manufacturing Costs to Account For</u>		203,000
Ending <u>Work-in-Process Inventory</u>		(29,000)
<u>Cost of Goods Manufactured</u>		<u>\$ 174,000</u>

Missing Amounts:

Beginning Direct Materials:

Direct Materials Available for Use	\$ 81,000
Purchases of Direct Materials	(51,000)
Beginning Direct Materials	<u>\$ 30,000</u>

Direct Materials Used:

Direct Materials Available for Use	\$ 81,000
Ending Direct Materials	(26,000)
Direct Materials Used	<u>\$ 55,000</u>

Direct Labor:

Total Manufacturing Costs Incurred During the Month	\$ 177,000
Manufacturing Overhead	(50,000)
Direct Materials Used [calculated above]	(55,000)
Direct Labor	<u>\$ 72,000</u>

P-M:1-38B, cont.

Total Manufacturing Costs to Account For:

Beginning Work-in-Process Inventory	\$ 26,000
Total Manufacturing Costs Incurred During the Month	177,000
Total Manufacturing Costs to Account For	<u>\$ 203,000</u>

Cost of Goods Manufactured:

Total Manufacturing Costs to Account For [calculated above]	\$ 203,000
Ending Work-in-Process Inventory	(29,000)
Cost of Goods Manufactured	<u>\$ 174,000</u>

CHARLIE MANUFACTURING COMPANY

Income Statement

Month Ended June 30, 2024

Net Sales Revenue	\$ 500,000
Cost of Goods Sold:	
Beginning <u>Finished Goods Inventory</u>	\$ 118,000
<u>Cost of Goods Manufactured</u>	<u>174,000</u>
Cost of Goods <u>Available for Sale</u>	<u>292,000</u>
Ending <u>Finished Goods Inventory</u>	<u>(60,000)</u>
Cost of Goods Sold	232,000
Gross Profit	268,000
<u>Selling and Administrative Expenses:</u>	
Selling Expenses	90,000
Administrative Expenses	<u>60,000</u>
Total <u>Selling and Administrative Expenses</u>	150,000
<u>Operating Income</u>	<u>\$ 118,000</u>

Missing Amounts:

Net Sales Revenue:

Cost of Goods Sold	\$ 232,000
Gross Profit	268,000
Net Sales Revenue	<u>\$ 500,000</u>

P-M:1-38B, cont.

Cost of Goods Manufactured:

[From the Schedule of Cost of Goods Manufactured]

Cost of Goods Available for Sale:

Beginning Finished Goods Inventory	\$ 118,000
Cost of Goods Manufactured	<u>174,000</u>
Cost of Goods Available for Sale	<u><u>\$ 292,000</u></u>

Ending Finished Goods Inventory:

Cost of Goods Available for Sale [calculated above]	\$ 292,000
Cost of Goods Sold	<u>(232,000)</u>
Ending Finished Goods Inventory	<u><u>\$ 60,000</u></u>

Administrative Expenses:

Total Selling and Administrative Expenses	\$ 150,000
Selling Expenses	<u>(90,000)</u>
Administrative Expenses	<u><u>\$ 60,000</u></u>

Operating Income:

Gross Profit	\$ 268,000
Total Selling and Administrative Expenses	<u>(150,000)</u>
Operating Income	<u><u>\$ 118,000</u></u>

P-M:1-39B
Requirement 1

Cost of direct materials purchased during the year:

$$\begin{array}{rcccl} \text{Direct} & & \text{Beginning} & & \text{Purchases of} & & \text{Ending} \\ \text{Materials Used} & = & \text{Direct Materials} & + & \text{Direct Materials} & - & \text{Direct Materials} \end{array}$$

Solving for cost of direct materials purchased:

$$\begin{array}{rcccl} \text{Purchases of} & & \text{Direct} & & \text{Ending} & & \text{Beginning} \\ \text{Direct} & = & \text{Materials} & + & \text{Direct Materials} & - & \text{Direct Materials} \\ \text{Materials} & & \text{Used} & & & & \\ & = & \$2,600,000 & + & \$800,000 & - & \$700,000 \\ & = & \$2,700,000 & & & & \end{array}$$

Requirement 2

Cost of goods manufactured for the year:

$$\begin{array}{rcccl} \text{Cost of} & & \text{Beginning} & & \text{Total} & & \text{Ending} \\ \text{Goods} & = & \text{Work-in-Process} & + & \text{Manufacturing} & - & \text{Work-in-Process} \\ \text{Manufactured} & & \text{Inventory} & & \text{Costs Incurred} & & \text{Inventory} \\ & = & \$1,500,000 & + & \$21,900,000 & - & \$2,000,000 \\ & = & \$21,400,000 & & & & \end{array}$$

Requirement 3

Cost of goods sold for the year:

$$\begin{array}{rcccl} \text{Cost of} & & \text{Beginning} & & \text{Cost of} & & \text{Ending} \\ \text{Goods} & = & \text{Finished Goods} & + & \text{Goods} & - & \text{Finished Goods} \\ \text{Sold} & & \text{Inventory} & & \text{Manufactured} & & \text{Inventory} \\ & = & \$1,100,000 & + & \$21,400,000 & - & \$1,080,000 \\ & & & & \text{[calculated in 2]} & & \\ & = & \$21,420,000 & & & & \end{array}$$

P-M:1-40B
Requirement 1

THE GLASS DOCTORS
Income Statement
Month Ended July 31, 2024

Revenues:		
Net Service Revenue		\$ 25,000
Expenses:		
Salaries and Wages Expense	\$ 10,000	
Materials Expense	4,100	
Depreciation Expense—Truck	500	
Depreciation Expense—Building and Equipment	900	
Supplies Expense	450	
Utilities Expense	4,550	
Total Expenses		<u>20,500</u>
Operating Income		<u><u>\$ 4,500</u></u>

Requirement 2

$$\begin{aligned}\text{Unit cost} &= \text{Total operating expenses} / \text{Total windshields repaired} \\ &= \$20,500 / 250 \text{ windshields} \\ &= \$82.00 \text{ per windshield}\end{aligned}$$

Requirement 3

No. The actual unit cost per windshield of \$82.00 is greater than \$80.

P-M:1-41B
Requirement 1

DILLON'S PETS
Income Statement
Year Ended December 31, 2024

Net Sales Revenue		\$ 56,000
Cost of Goods Sold:		
Beginning Merchandise Inventory	\$ 16,000	
Purchases of Merchandise	25,000	
Cost of Goods Available for Sale	<u>41,000</u>	
Ending Merchandise Inventory	<u>(10,500)</u>	
Cost of Goods Sold		<u>30,500</u>
Gross Profit		25,500
Selling and Administrative Expenses:		
Utilities Expense	3,200	
Rent Expense	4,100	
Sales Commission Expense	<u>2,750</u>	
Total Selling and Administrative Expenses		<u>10,050</u>
Operating Income		<u><u>\$ 15,450</u></u>

Requirement 2

$$\begin{aligned}\text{Unit cost} &= \text{Cost of goods sold} / \text{Total units sold} \\ &= \$30,500 / 5,550 \text{ units} \\ &= \$5.50 \text{ per unit (rounded to the nearest cent)}\end{aligned}$$

Using Excel

The student templates for *Using Excel* are available online in MyLab Accounting in the Multimedia Library or at <http://www.pearsonhighered.com/Horngren>. The solution to *Using Excel* is located in MyLab Accounting in the Instructor Resource Center or at <http://www.pearsonhighered.com/Horngren>.

Continuing Problem

P-M:1-42

PIEDMONT COMPUTER COMPANY
Schedule of Cost of Goods Manufactured
Month Ended January 31, 2024

Beginning Work-in-Process Inventory		\$ 0
Direct Materials Used:		
Beginning Direct Materials	\$ 10,500	
Purchases of Direct Materials	16,000	
Direct Materials Available for Use	<u>26,500</u>	
Ending Direct Materials	<u>(9,700)</u>	
Direct Materials Used		\$ 16,800
Direct Labor		210,000
Manufacturing Overhead:		
Plant janitorial services	500	
Utilities for plant	16,000	
Rent on plant	<u>9,000</u>	
Total Manufacturing Overhead		<u>25,500</u>
Total Manufacturing Costs Incurred during the Month		<u>252,300</u>
Total Manufacturing Costs to Account For		252,300
Ending Work-in-Process Inventory		<u>(17,000)</u>
Cost of Goods Manufactured		<u><u>\$ 235,300</u></u>

Critical Thinking

Tying It All Together Case M:1–1

Requirement 1

Winnebago's finished goods inventory is such a relatively small portion of total inventory because Winnebago manufactures the RVs and then sells them to dealerships for resale to consumers. The company does not own or operate dealerships. Therefore, Winnebago has a relatively small portion of Finished Goods Inventory. As soon as RVs are complete, Winnebago will want to sell them to the dealerships. The majority of Winnebago's inventory is in Raw Materials Inventory that will be used in the manufacturing process and Work-in-Process Inventory of the RVs started but not yet completed.

Requirement 2

Average cost of goods sold = Average sales price $\times$ Cost of goods sold % = $\$96,000 \times 85\% = \$81,600$.

Average gross profit = Average sales price – Average cost of goods sold = $\$96,000 - \$81,600 = \$14,400$.

Requirement 3

Average cost of goods sold = Average sales price $\times$ Cost of goods sold % = $\$96,000 \times 82\% = \$78,720$.

Average gross profit = Average sales price – Average cost of goods sold = $\$96,000 - \$78,720 = \$17,280$. Profits would increase by \$2,880 ($\$17,280 - \$14,400$) per motor home sold.

Requirement 4

Total increase in operating income = Average increase in profits per motor home $\times$ Number of motor homes = $\$2,880 \text{ per motor home} \times 9,548 \text{ motor homes} = \$27,498,240$.

Requirement 5

Managerial accounting provides detailed information on all costs incurred by the company. Managers can use the information provided to analyze different types of costs, such as product costs and period costs, to determine where actual costs exceeded expected costs and then consider options to reduce those costs.

Decision Case M:1-1
Requirement 1

Shown in the schedule, below, the ending inventories are: Direct Materials, \$143,000; Work-in-Process Inventory, \$239,000; and Finished Goods Inventory, \$150,000.

POWERSWITCH, INC. Flow of Costs Schedule For the 1st Quarter					
Raw Materials Inventory**		Work-in-Process Inventory		Finished Goods Inventory	
Beginning DM	\$ 113,000 *	Beginning WIP Inventory	\$ 229,000 *	Beginning FG Inventory	\$ 154,000 *
+ Purchases of DM	476,000 *	+ Direct Materials Used	446,000 ^e	+ Cost of Goods Manufactured	1,186,000 ^c
		+ Direct Labor	505,000 *		
		+ Manufacturing Overhead	245,000 *		
= Direct Materials Available for Use	589,000	= Total Manufacturing Costs to Account For	1,425,000 *	= Cost of Goods Available for Sale	1,340,000 *
– Ending DM	143,000 ^f	– Ending WIP Inventory	239,000 ^d	– Ending FG Inventory	150,000 ^b
= Direct Materials Used	<u>\$ 446,000 ^e</u>	= Cost of Goods Manufactured	<u>\$ 1,186,000 ^c</u>	= Cost of Goods Sold	<u>\$ 1,190,000 ^a</u>

* Denotes amounts given in the case.

**Direct materials portion only

Calculations for amounts denoted with a superscript letters are provided on the next two pages.

Decision Case M:1-1, cont.Calculations:^a Cost of Goods Sold:

Sales	×	(1 – Gross Profit %)	=	Cost of Goods Sold
\$1,700,000	×	(1 – 30%)	=	\$1,190,000
\$1,700,000	×	70%	=	\$1,190,000

^b Ending Finished Goods Inventory:

Cost of Goods Available for Sale	–	Ending Finished Goods Inventory	=	Cost of Goods Sold
\$1,340,000	–	Ending Finished Goods Inventory	=	\$1,190,000
<i>Therefore:</i>		Ending Finished Goods Inventory	=	\$150,000

^c Cost of Goods Manufactured:

Beginning Finished Goods Inventory	+	Cost of Goods Manufactured	=	Cost of Goods Available for Sale
\$154,000	+	Cost of Goods Manufactured	=	\$1,340,000
<i>Therefore:</i>		Cost of Goods Manufactured	=	\$1,186,000

^d Ending Work-in-Process Inventory:

Total Manufacturing Costs to Account For	–	Ending Work-in-Process Inventory	=	Cost of Goods Manufactured
\$1,425,000	–	Ending Work-in-Process Inventory	=	\$1,186,000
<i>Therefore:</i>		Ending Work-in-Process Inventory	=	\$ 239,000

Decision Case M:1-1, cont.

^e Direct Materials Used:

Beginning Work-in-Process Inventory	+	Direct Materials Used	+	Direct Labor	+	Manufacturing Overhead	=	Total Manufacturing Costs to Account For
\$229,000	+	Direct Materials Used	+	\$505,000	+	\$245,000	=	\$1,425,000
<i>Therefore:</i>		Direct Materials Used					=	\$ 446,000

^f Ending Direct Materials:

Direct Materials Available for Use	–	Ending Direct Materials	=	Direct Materials Used
\$589,000	–	Ending Direct Materials	=	\$446,000
<i>Therefore:</i>		Ending Direct Materials	=	\$143,000

Requirement 2

Inventory lost in the flood:

Direct Materials	\$ 143,000
Work-in-Process Inventory	239,000
Finished Goods Inventory	<u>150,000</u>
Total Inventory	<u>\$ 532,000</u>

Ethical Issue M:1-1

Students' responses will vary. Illustrative answers follow.

- a. The ethical issue facing Becky is deciding what to do about the owner's gifts to the regional sales managers. Although small "courtesy" gifts are accepted practice in the world of sales, the regular basis and the high value of these items (especially jewelry) suggest that the owner is bribing the sales managers and other sales executives to receive a large allocation of cars.
- b. The options include:
 - (1) Do nothing,
 - (2) Discuss the matter with the owner,
 - (3) Resign if the owner will not stop the practice, or
 - (4) Inform the manufacturer.
- c. The possible consequences include:
 1. If Becky does nothing, her job and those of the other employees may remain secure for the time being. However, as controller she could be held accountable for laundering a bribe if the scheme became public. A lawsuit brought by other dealers who did not receive a fair share of available cars could name her as an involved party. If Becky is a CPA, she could also lose her CPA license.

There are also potential tax consequences to consider. Since the jewelry expenditures are being recorded as selling expenses, it is likely that this amount is being deducted on the company's tax return. The IRS limits deductions of gifts to \$25 per person per year. Since a Rolex watch far exceeds the cost of \$25, Becky's failure to disclose the true nature of the expense may make her liable for underreporting the company's tax liability.

2. If Becky discusses the matter with the owner, she might find out that there is another side to the story and in fact there is no wrongdoing or ethical dilemma. However, this seems unlikely given the facts. It also seems unlikely that the owner will end this practice since it enhances the dealership's profits. However, Becky may have some influence on Mueller if she explains the dangers of continuing the bribes. Mueller could be sued by other dealers, or the manufacturer could cancel his dealership. Such outcomes would affect all the dealership's employees, not just Mueller. If Mueller refuses to change his ways, then Becky is in an even more difficult position because she now has direct knowledge of the bribery.

Ethical Issue M:1-1, cont.

3. By resigning, Becky loses her job but protects her integrity and avoids being involved in a subsequent action against the dealership if the bribery becomes known.
 4. Perhaps an even more difficult question is whether Becky should inform the manufacturer about the bribery. If Becky has not already resigned, Mueller probably would fire her for taking this action.
- d. Accountants should never become party to, or appear to be involved in, an unethical (and possibly illegal) situation such as this. This is especially true for persons with fiduciary responsibilities like a controller. Becky should discuss her concerns with the owner. If Mueller is indeed bribing the sales representatives and refuses to stop this practice, Becky should inform the manufacturer, or she should resign.

Communication Activity M:1-1

Period costs are operating costs that are expensed in the same accounting period in which they are incurred, whereas product costs are recorded as an asset and not expensed until the accounting period in which the product is sold. Period costs are all costs not considered product costs.

Manufacturing companies track costs on three kinds of inventory. Raw Materials Inventory includes materials used to manufacture a product. Work-in-Process Inventory includes goods that have been started in the manufacturing process but are not yet complete. Finished Goods Inventory includes completed goods that have not yet been sold.

Chapter 1

Accounting and the Business Environment

Chapter 1: Overview

The chapter begins with an introduction to accounting and a brief discussion of why accounting is important. The differences between financial and managerial accounting are delineated. The text discusses how accounting information is needed by various users—individuals, businesses, investors, creditors, and taxing authorities. Reasons accounting is important to students not majoring in accounting and career paths available to accounting majors are briefly described, including a comparison of various accounting positions. The role of governing organizations such as the Financial Accounting Standards Board (FASB) and the Securities and Exchange Commission (SEC) as well as the FASB's relationships with both congressionally created and private accounting groups are explained. Generally Accepted Accounting Principles (GAAP) are introduced. The sole proprietorship, partnership, corporation, and limited liability company (LLC) forms of business are briefly described in the context of the economic entity assumption. In addition, the cost principle, going concern assumption, and monetary unit assumption are explained. The nature of International Financial Reporting Standards (IFRS) and the role of the International Accounting Standards Board (IASB) in their development are explained. The role of ethics in accounting and business is described. The U.S. government's passing of the Sarbanes-Oxley Act (SOX) and the creation of the Public Company Accounting Oversight Board (PCAOB) are presented. A Data Analytics in Accounting feature highlights the importance of data analytics skills for accountants.

The next section of the chapter introduces the accounting equation: $\text{Assets} = \text{Liabilities} + \text{Equity}$. Each element of the accounting equation is defined. Nine basic business transactions are analyzed, and their impact on the accounting equation is discussed. The financial statements—income statement, statement of owner's equity, balance sheet, and statement of cash flows—are illustrated. The interrelationship of the financial statements is emphasized.

A Tying It All Together feature poses four questions regarding a company's asset, liability, revenue, and expense accounts and the proper financial statement reporting for each. Financial statements and return on assets (ROA) are used to evaluate business performance. A Decisions feature helps students see how financial statements and ROA can be used to make real-world decisions. The Review section includes Things You Should Know which highlights the information students should have acquired from the chapter. A Check Your Understanding feature allows students to record the effects of transactions on the accounting equation, prepare financial statements, and calculate ROA. A list of Key Terms is provided. A Quick Check gives students a chance to assess their knowledge of the chapter learning objectives.

Chapter 1: Learning Objectives

- LO 1. Explain why accounting is important and list the users of accounting information
- LO 2. Describe the organizations and rules that govern accounting
- LO 3. Describe the accounting equation and define assets, liabilities, and equity
- LO 4. Use the accounting equation to analyze transactions
- LO 5. Prepare financial statements
- LO 6. Use financial statements and return on assets (ROA) to evaluate business performance

Chapter 1: Teaching Outline with Lecture Notes

LO 1. Explain why accounting is important and list the users of accounting information

- a) Define the term accounting and explain what accountants do
- b) Exhibit F:1-1: Pathways Vision Model

Lecture Notes: The model emphasizes that good decisions have an impact on accounting judgments and economic activity, thus creating a circular flow of cause and effect. Accounting is defined as the information system that measures business activities, processes the information into reports, and communicates the results to decision makers. However, accountants do not simply prepare various types of accounting reports and tax returns. They also review and interpret business information using critical thinking and judgment to partner with clients and managers to help them make better business decisions.

- c) Differentiate between financial accounting and managerial accounting
- d) Exhibit F:1-2: Decision Making: Financial Versus Managerial Accounting

Lecture Notes: Financial accounting provides historical information—the company reports on events that have already occurred—to external decision makers, including investors and creditors. Managerial accounting provides more future-oriented information—many companies prepare budgets, forecasts, and projections based on future events—for internal decision makers (company managers and executives).

- e) Identify the users of accounting information:
 - i. Individuals
 - ii. Businesses
 - iii. Investors
 - iv. Creditors
 - v. Taxing authorities

Lecture Notes: The officers of a company may be (and probably are) owners as well. Not all investors are “outside” the company. The financial statements are the primary tools for providing information to outside investors; but officers may also use the statements, along with other financial information, to manage the company on a day-to-day basis.

- f) Describe career options and certifications available in the accounting profession

Lecture Notes: Certified Public Accountants, or CPAs, are licensed professional accountants who serve the general public. Certified Management Accountants, or CMAs, are certified professionals

who specialize in accounting and financial management knowledge. Not all accountants are licensed, and those who are may not necessarily be members of the AICPA and IMA, the professional associations described in the textbook. There are many other types of accounting-related associations and certifications in the United States and elsewhere around the world, including Certified Internal Auditor (CIA), Certified Government Financial Manager (CGFM), Certified Fraud Examiner (CFE), Certified Financial Manager (CFM), Enrolled Agent (EA), Certified Global Management Accountant (CGMA), Chartered Accountant (CA), Certified Financial Planner (CFP), and many more.

Accountants also need data analytics skills to be successful. An understanding of how technology is used to process financial information is critical in today's job market.

g) Exhibit F:1-3: Comparison of Accounting Positions

Suggested In-Class Exercise: E-F 1-17

LO 2. Describe the organizations and rules that govern accounting

- a) Identify accounting governing organizations, including the Financial Accounting Standards Board (FASB), the Security Exchange Commission (SEC), and the International Accounting Standards Board (IASB)
 - b) Describe Generally Accepted Accounting Principles (GAAP) and introduce the primary objective of financial reporting
 - c) Explain the economic entity assumption
 - i. Identify the different types of business organizations:
 - Sole proprietorship
 - Partnership
 - Corporation
 - Limited-liability company (LLC)
 - ii. Exhibit F:1-4: Business Organizations
 - d) Exhibit F: Explain the cost principle
 - e) Explain the going concern assumption
- Lecture Note: Point out to students that if it is known that a company should not be considered a going concern, different accounting rules from those covered in this course apply to that company.
- f) Explain the monetary unit assumption

Lecture Note: Point out to students that an implication of the monetary unit assumption is that business activities that cannot be expressed in monetary units are not represented within the financial statements. For example, a company with a well-trained workforce, talented managers, a good reputation with customers, and innovative research and development has important assets that are not represented on the balance sheet.

- g) Describe International Financial Reporting Standards (IFRS)
- h) Ethics in accounting and business
 - i. Sarbanes-Oxley Act (SOX)
 - ii. Public Company Accounting Oversight Board (PCAOB)

Lecture Notes: Not all accounting information and financial statements are publicly available; such information is disclosed by public companies only. Company size is not a determinant of public ownership; some large companies are still privately held. All companies, public and private, can follow GAAP. However, this may not be a requirement for private companies. Private companies can use other bases of accounting, such as the cash basis, unless GAAP is required due to an audit. There is also a difference between record keeping and financial statement preparation. Companies can keep their accounting records on another basis and convert the financial statements to GAAP. For example, small private companies may use the cash basis for record keeping and convert to the accrual basis for financial statement preparation.

The Sarbanes-Oxley Act and the PCAOB relate to public companies. As a rule, public companies are more regulated (in terms of accounting information) than private companies. Some companies are now going private; one reason for doing so may be to reduce the compliance cost associated with these additional regulations.

Although much has been written and discussed about the possibility of convergence of U.S. GAAP and IFRS, complete convergence appears to be increasingly unlikely. The SEC previously announced a policy dedicated to investigating endorsement of IFRS, but political winds now seem to be shifting. Furthermore, standard-setting paths of FASB and IASB sometimes converge, as in recent development of unified revenue recognition standards, but sometimes fail to converge, as in recent issuance of very different guidance on leases. For now, U.S. GAAP continue to be different in many respects from IFRS, a condition which seems likely to continue for the foreseeable future, although efforts to increase similarities also continue to meet with some degree of success.

Suggested In-Class Exercise: E-F 1-18

LO 3. Describe the accounting equation and define assets, liabilities, and equity

- a) The accounting equation: $\text{Assets} = \text{Liabilities} + \text{Equity}$
- b) Define assets
- c) Define liabilities

d) Define equity

Lecture Notes: The accounting equation must always balance. Demonstrate that the accounting equation always balances, not just at the beginning of the year (or any accounting period). During the year, the change in assets equals the change in liabilities plus the change in equity. At the end of the year, the new values of the accounting equation will balance.

Beginning of Year	Assets =	Liabilities +	Equity
During the Year	Δ Assets =	Δ Liabilities +	Δ Equity
End of Year	New Assets =	New Liabilities +	New Equity

Suggested In-Class Exercise: E-F 1-21

LO 4. Use the accounting equation to analyze transactions

a) Transaction analysis for Smart Touch Learning

- i. Transaction 1—Owner contribution
- ii. Transaction 2—Purchase of land for cash
- iii. Transaction 3—Purchase of office supplies on account
- iv. Transaction 4—Earning of service revenue for cash
- v. Transaction 5—Earning of service revenue on account
- vi. Transaction 6—Payment of expenses with cash
- vii. Transaction 7—Payment on account (Accounts Payable)
- viii. Transaction 8—Collection on account (Accounts Receivable)
- ix. Transaction 9—Owner withdrawal of cash

b) Exhibit F:1-5: Analysis of Transactions, Smart Touch Learning

Lecture Notes: Every basic transaction always affects at least two accounts. Becoming familiar with each of the nine basic transactions and the two accounts affected by each will promote development of students' transaction analysis skills. Demonstrate the following transaction analysis process for each transaction:

1. Identify the accounts and the account type.
2. Decide if each account increases or decreases.
3. Determine if the accounting equation is in balance.

When this process is applied correctly, the accounting equation will always balance. Thus, for all transactions that occur during the year:

During the Year	$\Delta \text{ Assets} =$	$\Delta \text{ Liabilities} +$	$\Delta \text{ Equity}$
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Note that every transaction affects the balance sheet in some way—increasing or decreasing an asset, liability, or equity account—but may or may not affect another financial statement. Remind students that there are four kinds of equity accounts: owner’s capital, owner’s withdrawals, revenues, and expenses. Thus, there are four ways that equity can change during the year:

During the Year	$\Delta \text{ Assets} =$	$\Delta \text{ Liabilities}$	$+ \text{ Owner's Capital}$
			$+ \text{ Revenues}$
			$- \text{ Expenses}$
			$- \text{ Owner's Withdrawals}$

Also, it may be helpful to point out that some transactions affect only one side of the accounting equation (left or right), yet the accounting equation still balances. For example, when a company purchases supplies with cash, one asset increases and another asset decreases—with no effect on liabilities and equity. Thus, the accounting equation balances.

Suggested In-Class Exercise: E-F 1-27

LO 5. Prepare financial statements

- a) Exhibit F:1-6: Financial Statements
 - i. Exhibit F:1-7: Income Statement
 - ii. Exhibit F:1-8: Statement of Owner’s Equity
 - iii. Exhibit F:1-9: Balance Sheet
 - iv. Exhibit F:1-10: Statement of Cash Flows

Lecture Notes: Each of the financial statements required by GAAP focuses on a different aspect of the company’s financial position or financial activity. All four statements should be completed and analyzed in order to get a complete picture of a company. Emphasize the links between the statements.

The income statement shows the change in equity that results from the operation of the business during the year and is prepared first. The owner’s equity statement shows the change in equity from profits earned less owner’s withdrawals during the year and is prepared second. Balance sheets show the financial position of the company at specific points in time and is prepared third. The statement of cash flows explains the change in Cash in relation to everything else that changed during the year and is the final statement to be prepared.

Each financial statement should have a company name, a statement title, and some form of date. The income statement tracks profitability—revenues minus expenses. Remember that “profit” doesn’t necessarily mean “money”; the profit may not have been collected in cash yet. The statement of owner’s equity shows the changes in capital for a business entity over a period of time. As profits

increase, owner's equity will increase; as withdrawals are paid, profits remaining in the business will decrease. The balance sheet shows the financial position of the company at a specific point in time, such as at the end of the year. The balance sheet will probably change the day after it is prepared. All the other financial statements describe what happened to the company *during* the year. The statement of cash flows describes how the balance of the Cash account changed in relation to changes in other assets, liabilities, and all the components of equity.

Financial position (the balance sheet) is different from profitability (the income statement). A company could be very profitable and do a terrible job of managing its profits or vice versa. Students probably know a person who is like this. Some people have high income levels and end up with very little net worth because they do not manage their finances effectively. On the other hand, some people have modest income levels and do a very good job of managing their finances.

The statement of cash flows shows how the company is generating and using its cash. Students may have heard the phrase "cash is king." A company must have cash to pay its outstanding bills. Some recent accounting fraud cases involved companies that reported great profits but no corresponding cash flow—a possible red flag!

Net income and cash flow are separate concepts; neither is always positive. A company could have net income and negative cash flow in one year, and then the company could have a net loss and positive cash flow in another year. Many creditors will focus on cash flow in order to determine whether a company can generate cash in order to pay back any outstanding liabilities.

The owner's equity balance does not represent the balance in the Cash account. Students sometimes think the owner can simply make withdrawals from profits earned at any given time. However, the income included in owner's equity is based on accrual accounting and may not yet have been collected in cash. In addition, some items that have been paid in cash may not be included in net income until some future period.

Suggested In-Class Exercises: E-F 1-31, E-F 1-32, E-F 1-33

LO 6. Use financial statements and return on assets (ROA) to evaluate business performance

- a) Review financial statements of Kohl's Corporation.
(see <http://www.pearsonhighered.com/Horngren>)
- b) Explain return on assets (ROA)

Lecture Notes: Information presented in the financial statements is largely based on historical cost—the cost principle. The balance sheet values of major assets such as land, buildings, and equipment are based on the historical cost of those assets and may not represent their fair market value. For example, land purchased 10 years ago is likely to be worth more than the original cost, but it would still be valued on the balance sheet at original cost. This difference between the fair market value and the balance sheet value is sometimes called "hidden assets." How are the "true" values of a company's assets determined? One could have them appraised, but even then, the current fair market value of assets does not represent the value of the company as a whole. Don't forget about subtracting liabilities! But, of course, even then the resulting value of owner's equity (fair market value of all the assets minus liabilities) does not necessarily represent the true market value of the company as a whole.

Return on assets measures how well a company uses its assets to generate profits. It is calculated by dividing net income by average total assets. Average total assets is calculated by adding the beginning and ending total assets for the time period and then dividing by two.

Suggested In-Class Exercise: E-F 1-27

Chapter 1: Handout for Student Notes

LO 1. Why is accounting important?

- Decision makers: The users of accounting information
 - Individuals
 - Businesses
 - Investors
 - Creditors
 - Taxing authorities
- Accounting matters

LO 2. What are the organizations and rules that govern accounting?

- Governing organizations
- Generally Accepted Accounting Principles (GAAP)
- The economic entity assumption
- The cost principle

- The going concern assumption
- The monetary unit assumption
- International Financial Reporting Standards
- Ethics in accounting and business

LO 3. What is the accounting equation?

- Assets
- Liabilities
- Equity

LO 4. How do you analyze a transaction?

- Transaction analysis for Smart Touch Learning
 - Transaction 1—Owner contribution
 - Transaction 2—Purchase of land for cash
 - Transaction 3—Purchase of office supplies on account

- Transaction 4—Earning of service revenue for cash
- Transaction 5—Earning of service revenue on account
- Transaction 6—Payment of expenses with cash
- Transaction 7—Payment on account (Accounts Payable)
- Transaction 8—Collection on account (Accounts Receivable)
- Transaction 9—Owner withdrawal of cash

LO 5. How do you prepare financial statements?

- Income statement
- Statement of owner's equity
- Balance sheet
- Statement of cash flows

LO 6. How do you use financial statements to evaluate business performance?

- Kohl's Corporation
(see <http://www.pearsonhighered.com/Horngren>)

- Return on assets (ROA)

Chapter 1: Student Chapter Summary

LO 1. Explain why accounting is important and list the users of accounting information

Accounting is the language of business. Financial accounting is used by a variety of decision makers outside the company, including individuals, businesses, investors, creditors, and taxing authorities, while managerial accounting is directed to decision makers inside the company. All businesses need accountants. Accountants work in public accounting, private accounting, and governmental accounting jobs. Accountants can be licensed as a Certified Public Accountant (CPA), Certified Global Management Accountant (CGMA), or Certified Management Accountant (CMA), or Certified Financial Planner (CFP). Further, non-accountant business professionals require accounting knowledge as well, as they regularly utilize accounting information to make business decisions.

LO 2. Describe the organizations and rules that govern accounting

The rules that govern accounting are called Generally Accepted Accounting Principles (GAAP). The Financial Accounting Standards Board (FASB) is responsible for the creation and governance of U.S. GAAP. The Securities and Exchange Commission (SEC) oversees the U.S. financial markets and other standard setters, such as the FASB.

A thorough understanding of GAAP is essential to the use and preparation of financial statements. The primary objective of financial reporting is to provide information useful for making investment and credit decisions. Financial statement information must be relevant and have faithful representation to be considered useful. Relevant information is timely and is capable of making a difference in the user's decision. Information is faithfully representative when it is complete, neutral, and free from material error.

Four accounting principles are introduced. The economic entity assumption requires that the subject of a set of accounting financial statements is a single economic unit separate and distinct from its owners and from other economic units. The cost principle requires that transactions record acquisition of assets and services at their actual cost. The going concern assumption specifies that financial reporting should presume the entity will remain in operation for the foreseeable future. The monetary unit assumption requires that only economic events that can be measured in monetary units are represented in the financial statements.

LO 3. Describe the accounting equation and define assets, liabilities, and equity

The fundamental relationship on which all accounting is based is represented by the accounting equation: $\text{Assets} = \text{Liabilities} + \text{Equity}$. Assets are economic resources with future benefits. Liabilities are obligations owed to others. Equity represents the residual value of the assets left over after obligations represented by the liabilities are fulfilled.

LO 4. Use the accounting equation to analyze transactions

Transactions are economic events that affect the financial position of the company and can be measured reliably. Basic transactions affect at least two accounts. Transactions are analyzed in three steps:

- Step 1. Identify the accounts and the account type (Asset, Liability, or Equity).
- Step 2. Decide whether each account increases or decreases.
- Step 3. Determine whether the accounting equation is in balance.

LO 5. Prepare financial statements

Four financial statements are prepared for each accounting period. The income statement reports net income or net loss, calculated as revenues earned minus expenses incurred, for a specific period of time. The statement of owner's equity reports the change in retained earnings from net income (or net loss) minus dividends for a specific period of time. The balance sheet reports the financial position (assets, liabilities, and equity) of the company at a specific point in time. The statement of cash flows reports the cash receipts and cash payments categorized by operating, investing, and financing activities. The financial statements are prepared in the following order: (1) income statement, (2) statement of owner's equity, (3) balance sheet, and (4) statement of cash flows.

LO 6. Use financial statements and return on assets (ROA) to evaluate business performance

The income statement evaluates profitability. The statement of owner's equity shows the amount of earnings kept and reinvested in the company. The balance sheet lists the economic resources owned, the debts and obligations owed, and the residual interest that remains for the owner. The statement of cash flows shows the change in cash resulting from operating, investing, and financing activities. Return on assets measures how profitably the company uses its assets.

Chapter 1: Assignment Grid and Other Materials

	LO 1	LO 2	LO 3	LO 4	LO 5	LO 6
S-F:1-1	X					
S-F:1-2		X				
S-F:1-3		X				
S-F:1-4		X				
S-F:1-5		X				
S-F:1-6			X			
S-F:1-7			X			
S-F:1-8			X			
S-F:1-9				X		
S-F:1-10				X		
S-F:1-11					X	
S-F:1-12					X	
S-F:1-13					X	
S-F:1-14					X	
S-F:1-15					X	
S-F:1-16						X
E-F:1-17	X					
E-F:1-18		X				
E-F:1-19			X		X	
E-F:1-20			X			
E-F:1-21			X			
E-F:1-22			X			
E-F:1-23			X			
E-F:1-24			X			
E-F:1-25				X		
E-F:1-26				X		
E-F:1-27				X		
E-F:1-28				X		
E-F:1-29				X		
E-F:1-30					X	
E-F:1-31					X	
E-F:1-32					X	
E-F:1-33					X	
E-F:1-34					X	
E-F:1-35					X	
E-F:1-36					X	
E-F:1-37					X	
E-F:1-38					X	
E-F:1-39						X

	LO 1	LO 2	LO 3	LO 4	LO 5	LO 6
E-F:1-40A				X		X
P-F:1-41A				X		
P-F:1-42A				X		
P-F:1-43A					X	
P-F:1-44A					X	
P-F:1-45A					X	
P-F:1-46A				X	X	
P-F:1-47A				X	X	X
P-F:1-48B				X		
P-F:1-49B				X		
P-F:1-50B					X	
P-F:1-51B					X	
P-F:1-52B					X	
P-F:1-53B					X	
P-F:1-54B				X	X	X

S – Short Exercises (*Easy*)

E – Exercises (*Moderate*)

P – Problems (*Difficult*)

Other End-of-Chapter Materials:

Continuing Problem P1-55
Tying It All Together Case 1-1
Decision Case 1-1
Ethical Issue 1-1
Fraud Case 1-1
Financial Statement Case 1-1

CHAPTER 1 TEN-MINUTE QUIZ

Circle the letter of the best response.

1. Financial markets in the United States are regulated by which of the following organizations?
 - A. American Institute of Certified Public Accountants (AICPA)
 - B. Financial Accounting Standards Board (FASB)
 - C. International Accounting Standards Board (IASB)
 - D. Securities and Exchange Commission (SEC)
2. Which accounting principle or assumption sets forth an entity as one business, separate from its owners?
 - A. Economic entity assumption
 - B. Cost principle
 - C. Monetary unit assumption
 - D. Going concern assumption
3. Which accounting principle or assumption assumes that an entity will remain in operation for the foreseeable future?
 - A. Economic entity assumption
 - B. Cost principle
 - C. Monetary unit assumption
 - D. Going concern assumption
4. Red Door Boutique is famous for fashion wristwatches and leather purses. At the end of a recent year, Red Door's total assets added up to \$485,000,000, and liabilities were \$163,000,000. How much was Red Door's equity?
 - A. \$163,000,000
 - B. \$322,000,000
 - C. \$485,000,000
 - D. \$648,000,000
5. Assume that Red Door Boutique purchased supplies on account for \$58,000. How would this transaction affect Red Door's accounting equation?
 - A. Increase assets and liabilities by \$58,000
 - B. Increase assets and equity by \$58,000
 - C. Increase liabilities and equity by \$58,000
 - D. Increase one asset and decrease another asset by \$58,000
6. Which field of accounting provides information to external decision makers such as investors and lenders?
 - A. Investment accounting
 - B. Tax accounting
 - C. Managerial accounting
 - D. Financial accounting

7. Which of the following is a characteristic of a limited-liability company?
- A. Indefinite life
 - B. Separate taxable entity
 - C. One or more owners
 - D. Personally liability of owner
8. Last year, Internet Service Company (ISC) sold services on account for \$75,000 and incurred expenses totaling \$48,000. At the end of the year, the balance for Accounts Receivable was \$10,000, and the balance for Accounts Payable was \$8,000. What was ISC's net income or net loss for the year?
- A. Net income of \$29,000
 - B. Net income of \$27,000
 - C. Net income of \$25,000
 - D. Net income of \$9,000
9. The income statement reports the
- A. financial position for a specific period.
 - B. financial position on a specific date.
 - C. results of operations for a specific period.
 - D. results of operations on a specific date.
10. On the 20XX income statement, Red Door Boutique reported net income of \$900,000. The company reported beginning total assets of \$8,000,000 and ending total assets of \$10,000,000. What is Red Door's return on assets for 20XX?
- A. 9.00%
 - B. 10.00%
 - C. 11.25%
 - D. 25.00%

Answer Key to Ten-Minute Quiz:

1. D

2. A

3. D

4. B

Assets = Liabilities + Equity

\$485,000,000 = \$163,000,000 + Equity

Equity = \$485,000,000 – \$163,000,000 = \$322,000,000

5. A

6. D

7. A

8. B

Net Income (Loss) = Revenues – Expenses = \$75,000 – \$48,000 = \$27,000

9. C

10. B

Return on assets = Net Income / Average total assets = \$900,000 / [(\$800,000,000 + \$10,000,000) / 2] = \$900,000 / \$9,000,000 = 10.00%

Extra Critical Thinking Questions

Decision Case 1-2

Dave and Reba Guerrero saved all their married life to open a bed and breakfast (B&B) named Tres Amigos. They invested \$100,000 of their own money. The business then got a \$100,000 bank loan for the \$200,000 needed to get started. The company bought a rundown old Spanish colonial home in Tucson for \$80,000. It cost another \$50,000 to renovate. They found most of the furniture at antique shops and flea markets—for a total cost of \$20,000. Kitchen equipment cost \$10,000, and a computer system cost \$2,000.

Prior to the grand opening, the banker requests a report on their activities thus far. The bank statement of Tres Amigos shows a cash balance of \$38,000. Dave and Reba believe that the \$38,000 represents net income for the period, and they feel pretty good about the results of their business. To better understand how well they are doing, they prepare the following income statement for presentation to the bank:

Tres Amigos Bed and Breakfast		
Income Statement		
Six Months Ended June 30, 20XX		
Revenues:		
Owner's capital	\$ 100,000	
Bank loan	<u>100,000</u>	
Total revenues		\$ 200,000
Expenses:		
Cost of the house	80,000	
Renovation to the house	50,000	
Furniture expense	20,000	
Kitchen equipment expense	10,000	
Computer expense	<u>2,000</u>	
Total expenses		<u>162,000</u>
Net Income		<u><u>\$ 38,000</u></u>

Requirements

1. Suppose you are the Guerreras' banker, and they have given you this income statement. Would you congratulate them on their net income? If so, explain why. If not, how would you advise them to measure the net income of the business? Does the amount of cash in the bank measure net income? Explain.
2. Prepare the balance sheet for Tres Amigos based on these data.

Decision Case 1-2: Solution

Requirement 1

The banker would not congratulate the Guerreras for their net income because they have not measured net income properly. In fact, they have no net income at all. Net income is revenues minus expenses, and the Guerreras do not have any revenues or expenses. The amount of cash in the bank does not measure net income, as it is the result of a loan from the bank.

Requirement 2

TRES AMIGOS BED AND BREAKFAST			
Balance Sheet			
June 30, 20XX			
Assets		Liabilities	
Cash	\$ 38,000	Bank Loan Payable	\$ 100,000
Computer	2,000		
Kitchen Equipment	10,000		
Furniture	20,000	Owner's Equity	
Building (\$80,000 + \$50,000)	130,000	Owner's Capital	100,000
		Total Liabilities and Owner's	
Total Assets	\$ 200,000	Equity	\$ 200,000

Team Project 1-1

You are opening Quail Creek Pet Kennel. Your purpose is to earn a profit, and you organize as a sole proprietorship.

Requirements

1. Make a detailed list of 10 factors you must consider to establish the business.
2. Identify 10 or more transactions that your business will undertake to open and operate the kennel.
3. Prepare the Quail Creek Pet Kennel income statement, statement of owner's equity, and balance sheet at the end of the first month of operations. Use made-up figures and include a complete heading for each financial statement. Date the balance sheet as of January 31, 20XX.
4. Discuss how you will evaluate the success of your business and how you will decide whether to continue its operation.

Team Project 1-1: Solution

Requirement 1

1. How to organize the business—as a proprietorship, a partnership, an LLC, or a corporation (You have decided to organize as a sole proprietorship.)
2. Where to locate the business
3. How much of your own time and money to commit to the business
4. How to finance the business—with your own personal money, with equity contributions from others, or through borrowing
5. How many people to employ for the business
6. How to measure the business's success or failure; how to account for the assets, liabilities, and operations of the business
7. What type of animals to board (dogs only, dogs and cats, birds, reptiles, and so on)
8. Whether to sell pet foods, toys, and other supplies
9. Whether to offer obedience lessons and other pet training
10. How to advertise the business (newspapers, radio, posters, online)

Student answers may vary.

Requirement 2

1. Make an initial cash investment contribution to start the business
2. Purchase land and building
3. Renovate the building to make it suitable for a kennel
4. Purchase pet food and other supplies that will be needed to operate the kennel
5. Advertising
6. Earn service revenue
7. Pay utility bills
8. Pay for veterinarian services
9. Pay employee wages
10. Borrow money
11. Pay owner withdrawals

Student answers may vary.

Team Project 1-1: Solution (cont'd)
Requirement 3

QUAIL CREEK PET KENNEL			
Income Statement			
Month Ended January 31, 20XX			
Revenue:			
Service Revenue			\$ 10,000
Expenses:*			
Wages Expense	\$ 2,000		
Supplies Expense	400		
Advertising Expense	300		
Utilities Expense	100		
Total Expense			2,800
Net Income			<u>\$ 7,200</u>

*Students may also include depreciation expense on the building.

QUAIL CREEK PET KENNEL			
Statement of Owner's Equity			
Month Ended January 31, 20XX			
Owner's Equity, January 1, 20XX			\$ 0
Owner's contribution			30,000
Net income for the month			7,200
			<u>37,200</u>
Withdrawals			(2,000)
Owner's Equity, January 31, 20XX			<u>\$ 35,200</u>

QUAIL CREEK PET KENNEL			
Balance Sheet			
January 31, 20XX			
	Assets		Liabilities
Cash	\$ 1,500	Accounts Payable	\$ 1,000
Supplies	200		
Building	25,000		
Land	9,500		
		Owner's Equity	
		Owner's Capital	35,200
		Total Owner's Equity	<u>35,200</u>
		Total Liabilities and Owner's	
Total Assets	<u>\$ 36,200</u>	Equity	<u>\$ 36,200</u>

Team Project 1-1: Solution (cont'd)

Requirement 4

We evaluate the success of the business by considering its:

- Net income or net loss for the period, as reported on the income statement
- Financial position at the end of the period, as reported on the balance sheet

A profitable business that should continue is one that shows net income for the period, assets exceeding liabilities, and positive cash flow.

Team Project 1-2

You are promoting a rock concert in your area. Your purpose is to earn a profit, and you organize Concert Enterprises as a sole proprietorship.

Requirements

1. Make a detailed list of 10 factors you must consider to establish the business.
2. Describe 10 of the items your business must arrange in order to promote and stage the rock concert.
3. Prepare your business's income statement, statement of owner's equity, and balance sheet on June 30, 20XX, immediately after the rock concert. Use made-up amounts and include a complete heading for each financial statement. For the income statement and the statement of owner's equity, assume the period is the three months ended June 30, 20XX.
4. Assume that you will continue to promote rock concerts if the venture is successful. If it is unsuccessful, you will terminate the business within three months after the concert. Discuss how you will evaluate the success of your venture and how you will decide whether to continue in business.

Team Project 1-2: Solution

(Suggested answers)

Requirement 1

1. How to organize the business—as a proprietorship, a partnership, an LLC, or a corporation (Assume you have decided to organize as a sole proprietorship.)
2. Where to locate the headquarters of the business
3. How much of your own time and money to commit to the business
4. How to finance the business—with your own personal money, with equity contributions from others, or through borrowing
5. How many people to employ for the business
6. How to measure the business's success or failure; how to account for the assets, liabilities, and operations of the business
7. What type of music to feature; what age group or interest group to appeal to
8. Whether to sell concessions (food, drinks, T-shirts, and so on) yourself or to arrange for outsiders to sell concessions at the concert
9. How to advertise the business (newspapers, radio, posters, online)

- Whether to sponsor the concerts yourself or to arrange for corporate or charitable organizations to sponsor the concerts

Requirement 2

- Which band (or bands) to feature at the concerts
- How much and when to pay the performers (flat rate or a percentage of gate receipts)
- Where to stage the concerts and how to pay for the site rental
- Need for city or county permits to stage a concert
- How to ensure security at the concert
- How to get people to come to the concert—how to advertise the concerts (newspapers, radio, posters, or other) and how much to pay for advertising
- How to offer concessions (buy and sell them yourself or arrange for outside concessionaires). If outsiders, how will they be compensated—keep their own revenues or share them with you?
- Need for traffic control if the crowd disrupts city traffic
- Weather considerations if the concert is staged outdoors
- Timing of the concert in relation to other events in the area at the time.

Team Project 1-2: Solution (cont'd)

Requirement 3

CONCERT ENTERPRISES		
Income Statement		
Three Months Ended June 30, 20XX		
Revenue:		
Ticket Sales Revenue		\$ 300,000
Concession Revenue		50,000
Total Revenue		350,000
Expenses:		
Band Expense	\$ 100,000	
Advertising Expense	50,000	
Concession Expense	20,000	
Rent Expense	15,000	
Security Expense	10,000	
Utilities Expense	3,000	
Permits Expense	2,000	
Total Expenses		200,000
Net Income		\$ 150,000

Team Project 1-2: Solution (cont'd)

CONCERT ENTERPRISES	
Statement of Owner's Equity	
Three Months Ended June 30, 20XX	
Owner's Equity, April 1, 20XX	\$ 0
Owner's contribution	1,000
Net income for quarter	150,000
	151,000
Withdrawals	(10,000)
Owner's Equity, June 30, 20XX	\$ 141,000

CONCERT ENTERPRISES			
Balance Sheet			
June 30, 20XX			
Assets		Liabilities	
Cash	\$ 136,000	Accounts Payable	\$ 7,000
Accounts Receivable	8,000		
Supplies	4,000	Owner's Equity	
		Owner's Capital	1,000
		Owner's Equity	140,000
		Total Owner's Equity	141,000
		Total Liabilities and Owner's	
Total Assets	\$ 148,000	Equity	\$ 148,000

Requirement 4

We evaluate the success of the business by considering its:

- Net income or net loss for the period, as reported on the income statement
- Financial position at the end of the period, as reported on the balance sheet

A profitable business that should continue is one that shows net income for the period, assets exceeding liabilities, and positive cash flow.

Communication Activity 1-1

Using 25 words or fewer, illustrate the accounting equation and explain each part of the accounting equation.

Communication Activity 1-1: Solution

Assets = Liabilities + Equity simply shows the resources that a business owns and the claims that others have against those resources (assets).