

Solutions Manual for Financial Accounting 13th Thomas

Chapter 1

The Financial Statements

Ethics Check

(5-10 min.) EC 1-1

- a. Objectivity and independence
- b. Due care
- c. Integrity
- d. Integrity

Short Exercises

(10 min.) S 1-1

- a. ***Corporation, limited partners of a Limited-liability partnership (LLP) and Limited-liability company (LLC).*** If any of these businesses fails and cannot pay its liabilities, creditors cannot force the owners to pay the business's debts from the owners' personal assets. Creditors can go after the general partner of a limited liability partnership.
- b. ***Proprietorship.*** There is a single owner of the business, so the owner is answerable to no other owner.
- c. ***Partnership.*** If the partnership fails and cannot pay its liabilities, creditors can force the partners to pay the business's debts from their personal assets. A partnership affords more protection for creditors than a proprietorship because there are two or more owners to share this liability.

(5 min.) S 1-2

- 1. The ***entity assumption*** applies.
- 2. Application of the entity assumption will separate Osmond's personal assets from the assets of Simple Treats, Inc. This will help Osmond, investors, and lenders know how much assets, liabilities

and equity the business has, and this knowledge will help all parties evaluate the business realistically.

(5-10 min.) S 1-3

- a. Stable-monetary-unit assumption
- b. Historical cost principle; \$300 is the accounting value of the laptop
- c. Historical cost principle; the sale price is the amount actually received from the sale
- d. Entity assumption

(10 min.) S 1-4

Computed amounts in boxes

	<u>Total Assets</u>	=	<u>Total Liabilities</u>	+	<u>Stockholders' Equity</u>
a.	\$660,000	=	\$300,000	+	\$360,000
b.	85,000	=	50,000	+	35,000
c.	350,000	=	75,000	+	275,000

(5 min.) S 1-5

1. Liabilities = Assets – Owners' Equity
2. Owners' Equity = Assets – Liabilities

This way of determining the amount of owners' equity applies to any company or your household.

(5-10 min.) S 1-6

- | | |
|--------------------------------------|-----------------------------------|
| a. Land <u>A</u> | g. Retained earnings <u>S</u> |
| b. Accrued expenses payable <u>L</u> | h. Prepaid expenses <u>A</u> |
| c. Supplies <u>A</u> | i. Accounts payable <u>L</u> |
| d. Equipment <u>A</u> | j. Accounts receivable <u>A</u> |
| e. Notes payable <u>L</u> | k. Merchandise inventory <u>A</u> |
| f. Long-term debt <u>L</u> | l. Common stock <u>S</u> |

(5-10 min.) S 1-7

1. ***Assets*** are the *economic resources* of a business that are expected to produce a benefit in the future.

Owners' (stockholders') equity represents the *insider claims* of a business, the owners' interest in its assets.

Assets and owners' equity *differ* in that assets are *resources* and owners' equity is a *claim to assets*.

Assets must be at least as large as owners' equity, so equity can be smaller than assets.

2. Both liabilities and owners' (stockholders') equity are *claims to assets*.

Liabilities are the *outsider* claims to the assets of a business; they are obligations to pay creditors.

Owners' equity represents the *insider* claims to the assets of the business; they are the owners' interest in its assets.

(5 min.) S 1-8

1. Revenues and expenses

2. Net income (or net loss)

(10 min.) S 1-9

- a. Salary expense I
- b. Dividends R, C
- c. Accounts payable B
- d. Net income I, R, C
- e. Common stock B
- f. Inventory B
- g. Interest revenue I
- h. Cash B, C
- i. Retained earnings R, B
- j. Long-term debt B
- k. Increase or decrease in cash C
- l. Net cash provided by operating activities C
- m. Sales revenue I
- n. Net cash used for financing activities C

(15-20 min.) S 1-10

- a. *Paying large dividends* will cause retained earnings to be low.
- b. Heavy *investing activity* and *paying off debts* can result in a cash shortage even if net income has been high.
- c. The single best source of cash for a business is operating activities. This source of cash is best because it results from the core operations of the business. Operating activities should be the main source of cash for a business.
- d. Borrowing, issuing stock, and selling land, buildings, and equipment can bring in cash even when the company has experienced losses. Reducing accounts receivable and inventory can also increase cash flow.

(5 min.) S 1-11

- a. I
- f. I

- | | | | |
|----|---|----|---|
| b. | B | g. | R |
| c. | C | h. | C |
| d. | R | i. | B |
| e. | B | | |

(5 min.) S 1-12

**MacKensie Services, Inc.
Income Statement
Year Ended December 31, 2021**

	<i>(millions)</i>
Revenues.....	\$394
Expenses	<u>171</u>
Net income	<u><u>\$223</u></u>

(5 min.) S 1-13

**Journey Corporation
Statement of Retained Earnings
Year Ended December 31, 2021**

	<i>(millions)</i>
Retained earnings, December 31, 2020	\$270
Add: Net income (\$460 – \$380)	80
Less: Dividends declared	<u>(64)</u>
Retained earnings, December 31, 2021	<u><u>\$286</u></u>

(10-15 min.) S 1-14

**Jackson Corporation
Balance Sheet
December 31, 2021**

(in millions)

ASSETS

Current assets:

Cash **\$ 52**

Accounts receivable **23**

Total current assets **75**

Long-term assets **45**

Total assets **\$120**

LIABILITIES

Current liabilities:

Accounts payable **\$ 21**

Total current liabilities **21**

Long-term liabilities:

Long-term notes payable **31**

Total liabilities.....	<u>52</u>
STOCKHOLDERS' EQUITY	
Common stock.....	28
Retained earnings.....	<u>40</u>
Total stockholders' equity	<u>68</u>
Total liabilities and stockholders' equity	<u>\$120</u>

**Sullivan Corporation
Balance Sheet
September 30, 2021**

	<i>(in millions)</i>
ASSETS	
Current assets:	
Cash	\$ 78
Accounts receivable	<u>27</u>
Total current assets	105
Property and equipment	27
Other long-term assets	<u>21</u>
Total assets	<u>\$153</u>
LIABILITIES	
Current liabilities:	
Accounts payable	<u>\$ 34</u>
Total current liabilities	34
Long-term liabilities:	
Long-term notes payable	<u>17</u>
Total liabilities	<u>51</u>
STOCKHOLDERS' EQUITY	
Common stock	31
Retained earnings	<u>71*</u>
Total stockholders' equity	<u>102</u>
Total liabilities and stockholders' equity	<u>\$153</u>

*Computation of retained earnings: Total assets (\$153) – total liabilities (\$51) – common stock (\$31) = \$71

Or, total stockholders' equity (\$102) – common stock (\$31) = \$71

(10-15 min.) S 1-16

**Python Legal Services, Inc.
Statement of Cash Flows
Year Ended December 31, 2021**

Cash flows from operating activities:

Net income	\$115,000
Adjustments to reconcile net income to net cash provided by operating activities	<u>(9,000)</u>
Net cash provided by operating activities	106,000

Cash flows from investing activities:

Purchases of equipment	<u>\$(20,000)</u>
Net cash used for investing activities	(20,000)

Cash flows from financing activities:

Payment of dividends	<u>\$(15,000)</u>
Net cash used for financing activities.....	<u>(15,000)</u>
Net increase in cash	71,000
Cash balance, December 31, 2020	<u>16,000</u>
Cash balance, December 31, 2021	<u><u>\$ 87,000</u></u>

(10-15 min.) S 1-17

Solve in this order:

- a. \$82**
- b. \$82**
- c. \$149**
- f. \$149**
- g. \$182**
- h. \$230**
- e. \$230**
- d. \$112**

(5 min.) S 1-18

Ethics is a factor that should be included in every business and accounting decision, beyond the potential economic and legal consequences. Ideally, for each decision, honesty and truthfulness should prevail, considering the rights of others. The decision guidelines at the end of the chapter spell out the considerations we should take when making decisions. Simply, we might ask ourselves three questions: (1) Is the action legal? (2) Who will be affected by the decision? (3) How will the decision make me feel afterward?

(10-15 min.) S 1-19

Asset (m)	Economic resources that are expected to produce a benefit in the future
Balance sheet (l)	Also called the statement of financial Position
Bookkeeping (k)	Mechanical part of accounting
Corporation (f)	Owned by stockholders whose liability is limited to the amount they have invested in the business
Equity (r)	Insider claims of a business
Ethical duties (d)	Responsibilities of the members of society to each other
Expenses (h)	Costs of doing business
Financial accounting (b)	Provides information for decision makers outside of the organization
Historical cost principle (j)	States that assets should be recorded at their actual cost on the date of purchase
Income statement (o)	Answers the question “How well did the company perform during the period?”
Investors and creditors (n)	Entities that provide money to

Liability (g) **finance a company's operations**
A debt payable to an outsider

(continued) S 1-19

Managerial accounting (c) **Provides information for managers of the organization**

Net income (a) **Total revenues minus total expenses**

Partnership (q) **A business organization form with two or more owners who are each personally liable for all of the business's debts**

Proprietorship (i) **A business organization form with a single owner who is personally liable for all of the business's debts**

Revenues (e) **Inflows of resources resulting from delivering goods or services to customers**

Statement of cash flows (p) **Reports cash flows from operating, investing, and financing activities**

(5-10 min.) S 1-20

1. Insert Function dialog box 6. Artificial intelligence

2. Formula bar
3. Spreadsheet
4. Data analytics
5. Active cell

7. Spreadsheet
8. Machine learning
9. Robotic process automation
10. Ribbon

(5-10 min.) S 1-21

1. Active cell (J)
2. Insert Sheet icon (F)
3. Row header numbers (G)
4. Worksheet tabs (K)
5. Ribbon (I)
6. File name (B)

7. Column header letters (C)
8. Zoom slider (A)
9. Ribbon tabs (H)
10. Quick Access toolbar (E)
11. Insert Function dialog box (D)
12. Formula bar (L)

Exercises

(10-15 min.) E 1-22A

Amounts in billions; (computed amounts in boxes)

	Assets	=	Liabilities	+	Stockholders' Equity
Smythe Real Estate	\$73		\$41		\$32
Odessa Florals	26		11		15
Hometown Bank	29		14		15

Odessa Florals appears to have the strongest financial position because its liabilities make up the smallest percentage of company assets ($\$11/\$26 = .42$). Stated differently, Odessa Florals' equity is the highest percentage of company assets ($\$15/\$26 = .58$).

Liabilities as a percent of total assets:

Smythe Real Estate: $\$41/\$73 = 0.56$

Odessa Florals: $\$11/\$26 = 0.42$

Hometown Bank: $\$14/\$29 = 0.48$

(10-15 min.) E 1-23A

Req. 1

(Amounts in millions)

	<u>Assets</u>	=	<u>Liabilities</u>	+	<u>Stockholders' Equity</u>
	\$220		\$160		
	320		380		
	<u>130</u>		<u> </u>		
Total	\$670	=	\$540	+	\$130

Req. 2 **Resources
to work with**

Req. 3 **Amount
owed to
creditors**

Req. 4 **Actually
owned by company
stockholders**

(10-20 min.) E 1-24A

	Situation		
	1	2	3
	<i>(Millions)</i>		
Total stockholders' equity,			
January 31, 2021 (\$47 – \$19).....	\$28	\$28	\$28
Add: Issuances of stock	11	-0-	15
Net income.....	13*	44*	84*
Less: Dividends declared	-0-	(20)	(75)
Net loss	-0-	-0-	-0-
Total stockholders' equity,			
January 31, 2022 (\$77 – \$25).....	\$52	\$52	\$52

*Must solve for these amounts.

(10-15 min.) E 1-25A

- a. Income statement**
- b. Balance sheet**
- c. Balance sheet**
- d. Balance sheet**
- e. Statement of retained earnings, Statement of cash flows**
- f. Balance sheet, Statement of cash flows**
- g. Statement of cash flows**
- h. Statement of cash flows**
- i. Income statement**
- j. Balance sheet, Statement of retained earnings**
- k. Income statement**
- l. Balance sheet**
- m. Income statement, Statement of retained earnings, Statement of cash flows**
- n. Balance sheet**

**Landy Products
Balance Sheet
December 31, 2021**

ASSETS**Current assets:**

Cash.....	\$ 24,000
Receivables.....	18,000
Inventory	<u>80,000</u>
Total current assets	122,000

Equipment.....	<u>182,000</u>
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Total assets	<u><u>\$304,000</u></u>
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LIABILITIES**Current liabilities:**

Accounts payable.....	<u>\$ 22,000</u>
Total current liabilities	22,000

Long-term liabilities:

Long-term notes payable.....	<u>172,000</u>
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Total liabilities	<u>194,000</u>
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STOCKHOLDERS' EQUITY

Common stock	34,500
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Retained earnings	<u>75,500*</u>
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Total stockholders' equity.....	<u>110,000</u>
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Total liabilities and stockholders' equity	<u><u>\$304,000</u></u>
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***Computation of retained earnings:**

Total assets (\$304,000) – current liabilities (\$22,000) – long-term notes payable (\$172,000) – common stock (\$34,500) = \$75,500

(10-20 min.) E 1-27A

Req. 1

**Jill Carlson Realty Company
Balance Sheet
January 31, 2021**

(Amounts in millions)

ASSETS		LIABILITIES	
Cash	\$ 57.2	Current liabilities	\$ 2.9
Receivables	0.5	Long-term liabilities	<u>102.6</u>
Investment assets (long-term)	79.4	Total liabilities	105.5
Property and equipment, net	1.6	STOCKHOLDERS'	
Other assets (long-term)	9.3	EQUITY	
		Common stock	39.2
		Retained earnings	<u>3.3*</u>
		Total stockholders' equity	42.5
		Total liabilities and	
Total assets	<u>\$148.0</u>	stockholders' equity	<u>\$148.0</u>

*Computation of retained earnings:

Total assets (\$148.0) – Total liabilities (\$105.5) – Common stock (\$39.2) = \$3.3

Req. 1

**Jill Carlson Realty Company
Income Statement
Year Ended January 31, 2021**

(Amounts in millions)

Total revenue		\$25.7
Expenses:		
Salary and other employee expenses	\$13.7	
Other expenses	7.6	
Interest expense	<u>1.5</u>	
Total expenses		<u>22.8</u>
Net income		<u>\$2.9</u>

Req. 2

The statement of retained earnings helps to compute dividends, as follows:

**Jill Carlson Realty Company
Statement of Retained Earnings
Year Ended January 31, 2021**

(Amounts in millions)

Retained earnings, beginning of year	\$2.6
Add: Net income for the year (Req. 1)	<u>2.9</u>
Subtotal	5.5
Less: Dividends declared**	<u>2.2</u>
Retained earnings, end of year (from Exercise 1-27A)	<u>\$3.3</u>

$$^{**}(\$5.5 - \$3.3 = \$2.2)$$

Req. 1

Giada Coffee Roasters Corp.
Income Statement
For the Month Ended August 31, 2022

Revenue:	
Service revenue.....	\$278,700
Expenses:	
Salary expense	\$78,500
Utilities expense	5,100
Rent expense	<u>1,800</u>
Total expenses	<u>85,400</u>
Net income	<u>\$193,300</u>

Giada Coffee Roasters Corp.
Statement of Retained Earnings
For the Month Ended August 31, 2022

Retained earnings, August 1, 2022	\$ -0-
Add: Net income for the month	<u>193,300</u>
Subtotal	193,300
Less: Dividends declared	<u>(2,800)</u>
Retained earnings, August 31, 2022	<u>\$190,500</u>

Req. 1

**Giada Coffee Roasters Corp.
Balance Sheet
August 31, 2022**

Assets		Liabilities	
Cash	\$ 5,300	Accounts payable	\$ 8,800
Office supplies	7,400		
Equipment	201,500	Stockholders' Equity	
		Common stock	14,900
		Retained earnings	<u>190,500</u>
		Total stockholders' equity	205,400
		Total liabilities and	
Total assets	<u>\$214,200</u>	stockholders' equity	<u>\$214,200</u>

(15-20 min.) E 1-31A

Req. 1

**Giada Coffee Roasters Corp.
Statement of Cash Flows
For the Month Ended August 31, 2022**

Cash flows from operating activities:

Net income	\$193,300
Adjustments to reconcile net income to net cash provided by operating activities	<u>1,400</u>
Net cash provided by operating activities	194,700

Cash flows from investing activities:

Acquisition of equipment	<u>\$(201,500)</u>
Net cash used for investing activities	(201,500)

Cash flows from financing activities:

Issuance (sale) of stock to owners	\$ 14,900
Payment of dividends	<u>(2,800)</u>
Net cash provided by financing activities	<u>12,100</u>

Net increase in cash	\$ 5,300
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Cash balance, August 1, 2022	<u>0</u>
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→ Cash balance, August 31, 2022	<u><u>\$ 5,300</u></u>
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(10-15 min.) E 1-32A

TO: Owner of Giada Coffee Roasters Corp.

FROM: Student Name

SUBJECT: Opinion of net income, dividends, financial position,
and cash flows

Your first month of operations was successful. Revenues totaled \$278,700 and net income was \$193,300. These operating results look very strong.

The company was able to pay a \$2,800 dividend, and this should make you happy with so quick a return on your investment. Your financial position looks secure, with assets of \$214,200 and liabilities of only \$8,800. Your stockholders' equity is \$205,400.

Operating activities generated cash of \$194,700, which is outstanding. Operating activities are the main source of cash, which is expected for a thriving company. You ended the month with cash of \$5,300. Based on the above facts, I believe you should stay in business.

Student responses may vary.

Req. 1

Edwin Company
Income Statement
For the Year Ended December 31, 2021

	<i>(millions)</i>
Revenue:	
Revenues	\$150
Expenses:	
Salary expense	\$34
Rent expense	23
Utilities expense	<u>16</u>
Total expenses	<u>73</u>
Net income	<u>\$ 77</u>

Req. 2

Edwin Company
Statement of Retained Earnings
Year Ended December 31, 2021

	<i>(millions)</i>
Retained earnings, December 31, 2020	\$ 73
Add: Net income (\$150 – \$73)	77
Less: Dividends declared	<u>(16)</u>
Retained earnings, December 31, 2021	<u>\$134</u>

(continued) E 1-33A

Req. 3

**Edwin Company
Balance Sheet
December 31, 2021**

ASSETS	<i>(in millions)</i>
Current assets:	
Cash	\$185
Accounts receivable	<u>70</u>
Total current assets	255
Property and equipment	35
Other long-term assets	<u>22</u>
Total assets	<u><u>\$312</u></u>
 LIABILITIES	
Current liabilities:	
Accounts payable	\$ 56
Total current liabilities	56
Long-term liabilities:	
Long-term notes payable	<u>26</u>
Total liabilities	<u>82</u>
 STOCKHOLDERS' EQUITY	
Common stock	96*
Retained earnings	<u>134</u>
Total stockholders' equity	<u>230</u>
Total liabilities and stockholders' equity	<u><u>\$312</u></u>

***Common stock = Total stockholders' equity (\$230) – Retained earnings (\$134) = \$96**

(10-15 min.) E 1-34B

Amounts in billions; (computed amounts in boxes)

	<u>Assets</u>	=	<u>Liabilities</u>	+	<u>Stockholders' Equity</u>
Water Street Bank	<u>\$78</u>		\$43		\$35
Pufferbelly Restaurant	30		<u>7</u>		23
Blake Gift Shop	34		7		<u>27</u>

Blake Gift Shop appears to have the strongest financial position because its liabilities make up the smallest percentage of company assets ($\$7/\$34 = .21$). Stated differently, Blake Gift Shop's equity is the highest percentage of company assets ($\$27/\$34 = .79$).

Liabilities as a percent of total assets:

Water Street Bank: $\$43/\$78 = 0.55$

Pufferbelly Restaurant: $\$7/\$30 = 0.23$

Blake Gift Shop: $\$7/\$34 = 0.21$

(10-15 min.) E 1-35B

Req. 1

(Amounts in millions)

	<u>Assets</u>	=	<u>Liabilities</u>	+	<u>Stockholders' Equity</u>
	\$240		\$100		
	390		360		
	<u>130</u>				
Total	\$760	=	\$460	+	\$300

Req. 2 Resources
to work with

Req. 3 Amount
owed to
creditors

Req. 4 Actually
owned by company
stockholders

(10-20 min.) E 1-36B

	Situation		
	1	2	3
	<i>Millions</i>		
Total stockholders' equity,			
January 31, 2021 (\$49 – \$17)	\$32	\$32	\$32
Add: Issuances of stock	3	-0-	20
Net income	14*	21*	5*
Less: Dividends declared	-0-	(4)	(8)
Net loss	-0-	-0-	-0-
Total stockholders' equity,			
January 31, 2022 (\$72 – \$23)	\$49	\$49	\$49

*Must solve for these amounts.

(10-15 min.) E 1-37B

- a. Balance sheet, Statement of cash flows**
- b. Statement of cash flows**
- c. Balance sheet**
- d. Balance sheet**
- e. Income statement, Statement of retained earnings, Statement of cash flows**
- f. Income statement**
- g. Balance sheet**
- h. Income statement**
- i. Balance sheet**
- j. Statement of cash flows**
- k. Income statement**
- l. Balance sheet**
- m. Statement of retained earnings, Statement of cash flows**
- n. Balance sheet, Statement of retained earnings**

Patterson Products
Balance Sheet
December 31, 2021

ASSETS**Current assets:**

Cash.....	\$ 20,000
Receivables.....	17,600
Inventory	<u>78,000</u>
Total current assets	115,600

Equipment.....	<u>186,000</u>
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Total assets	<u><u>\$301,600</u></u>
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LIABILITIES**Current liabilities:**

Accounts payable.....	<u>\$ 22,000</u>
Total current liabilities	22,000

Long-term liabilities:

Long-term notes payable.....	<u>173,000</u>
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Total liabilities	<u>195,000</u>
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STOCKHOLDERS' EQUITY

Common stock	28,500
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Retained earnings	<u>78,100*</u>
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Total stockholders' equity.....	<u>106,600</u>
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Total liabilities and stockholders' equity	<u><u>\$301,600</u></u>
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***Computation of retained earnings:**

Total assets (\$301,600) – current liabilities (\$22,000) – long-term notes payable (\$173,000) – common stock (\$28,500) = \$78,100

(10-20 min.) E 1-39B

Req. 1

**Mary Burke Realty Company
Balance Sheet
March 31, 2021**

(Amounts in millions)

ASSETS		LIABILITIES	
Cash	\$ 1.6	Current liabilities	\$ 2.7
Receivables	.1	Long-term liabilities	<u>102.3</u>
Investment assets	135.1	Total liabilities	105.0
Property and equipment, net	1.4	STOCKHOLDERS'	
Other assets	10.3	EQUITY	
		Common stock	27.9
		Retained earnings	<u>15.6*</u>
		Total stockholders' equity	43.5
		Total liabilities and	
Total assets	<u>\$148.5</u>	stockholders' equity	<u>\$148.5</u>

***Computation of retained earnings:**

Total assets (\$148.5) – Total liabilities (\$105.0) – Common stock (\$27.9) = \$15.6

Req. 1

**Mary Burke Realty Company
Income Statement
Year Ended March 31, 2021**

(Amounts in millions)

Total revenue	\$40.4
Expenses:	
Salary and other employee expenses	\$ 15.2
Other expenses	6.6
Interest expense	<u>0.4</u>
Total expenses	<u>22.2</u>
Net income	<u>\$18.2</u>

Req. 2

The statement of retained earnings helps to compute dividends, as follows:

**Mary Burke Realty Company
Statement of Retained Earnings
Year Ended March 31, 2021**

(Amounts in millions)

Retained earnings, beginning of year.....	\$17.2
Add: Net income for the year (<i>Req. 1</i>).....	<u>18.2</u>
Subtotal	35.4
Less: Dividends declared**	<u>19.8</u>
Retained earnings, end of year (from Exercise 1-39B).....	<u>\$15.6</u>

**(\$35.4 – \$15.6 = \$19.8)

Req. 1

Island Coffee Roasters Corporation
Income Statement
For the Month Ended August 31, 2022

Revenue:		
Service revenue		\$279,300
Expenses:		
Salary expense	\$78,100	
Utilities expense	5,800	
Rent expense	<u>1,800</u>	
Total expenses		<u>85,700</u>
Net income		<u>\$193,600</u>

Island Coffee Roasters Corporation
Statement of Retained Earnings
For the Month Ended August 31, 2022

Retained earnings, August 1, 2022.....	\$ -0-	
Add: Net income.....	<u>193,600</u>	←
Subtotal	193,600	
Less: Dividends declared.....	<u>(2,700)</u>	
Retained earnings, August 31, 2022.....	<u>\$190,900</u>	

(15-20 min.) E 1-42B

Req. 1

**Island Coffee Roasters Corporation
Balance Sheet
August 31, 2022**

Assets		Liabilities	
Cash	\$ 6,000	Accounts payable	\$ 8,900
Office supplies	7,500	Stockholders' Equity	
Equipment	200,000	Common stock.....	13,700
		Retained earnings.....	<u>190,900</u>
		Total stockholders' equity	204,600
		Total liabilities and	
Total assets	<u>\$213,500</u>	stockholders' equity	<u>\$213,500</u>

(15-20 min.) E 1-43B

Req. 1

**Island Coffee Roasters Corporation
Statement of Cash Flows
For the Month Ended August 31, 2022**

Cash flows from operating activities:

Net income.....	\$193,600
Adjustments to reconcile net income to net cash provided by operations.....	<u>1,400</u>
Net cash provided by operating activities	195,000

Cash flows from investing activities:

Acquisition of equipment	\$(200,000)
Net cash used for investing activities	(200,000)

Cash flows from financing activities:

Issuance (sale) of stock to owners	\$ 13,700
Payment of dividends	<u>(2,700)</u>
Net cash provided by financing activities..	<u>11,000</u>

Net increase in cash	\$ 6,000
----------------------------	----------

→Cash balance, August 1, 2022.....	<u>0</u>
------------------------------------	----------

Cash balance, August 31, 2022.....	<u><u>\$ 6,000</u></u>
------------------------------------	------------------------

(10-20 min.) E 1-44B

TO: Owner of Island Coffee Roasters Corporation
FROM: Student Name
SUBJECT: Opinion of net income, dividends, financial position, and cash flows

Your first month of operations was successful. Revenues totaled \$279,300 and net income was \$193,600. These operating results look very strong.

The company was able to pay a \$2,700 dividend, and this should make you happy with so quick a return on your investment. Your financial position looks secure, with assets of \$213,500 and liabilities of only \$8,900. Your stockholders' equity is \$204,600.

Operating activities generated cash of \$195,000, which is respectable. Operating activities are the main source of cash, which is expected for a thriving company. You ended the month with cash of \$6,000. Based on the above facts, I believe you should stay in business.

Student responses may vary.

Req. 1

Brewster Company
Income Statement
For the Year Ended December 31, 2021

	<i>(millions)</i>
Revenue:	
Revenues	\$146
Expenses:	
Salary expense	\$28
Rent expense	23
Utilities expense	<u>19</u>
Total expenses	<u>70</u>
Net income	<u><u>\$76</u></u>

Req. 2

Brewster Company
Statement of Retained Earnings
Year Ended December 31, 2021

	<i>(millions)</i>
Retained earnings, December 31, 2020	\$ 76
Add: Net income (\$146 – \$70)	76
Less: Dividends declared	<u>(15)</u>
Retained earnings, December 31, 2021	<u><u>\$137</u></u>

Req. 3

**Brewster Company
Balance Sheet
December 31, 2021**

ASSETS	<i>(in millions)</i>
Current assets:	
Cash	\$175
Accounts receivable	<u>85</u>
Total current assets	260
Property and equipment	39
Other long-term assets	<u>25</u>
Total assets	<u>\$324</u>
 LIABILITIES	
Current liabilities:	
Accounts payable	\$ 56
Total current liabilities	56
Long-term liabilities:	
Long-term notes payable	<u>33</u>
Total liabilities	<u>89</u>
 STOCKHOLDERS' EQUITY	
Common stock	98*
Retained earnings	<u>137</u>
Total stockholders' equity	<u>235</u>
 Total liabilities and stockholders' equity	<u>\$324</u>

*Common stock = Total stockholders' equity (\$235) – Retained earnings (\$137) = \$98

Quiz

Q1-46 A

Q1-47 A

Q1-48 B

Q1-49 B

Q1-50 b

Q1-51 a

Assets	=	Liabilities	+	Stockholders' Equity
+ \$83,000	=	+ \$23,000	+	+ \$60,000

Q1-52 a

Q1-53 B

Q1-54 B

Q1-55 A

Q1-56 d

Q1-57 c [\$260,000 – \$185,000 – \$81,000 – \$28,000 = \$(34,000)]

Q1-58 b (\$300,000 + \$200,000 – \$55,000 = \$445,000)

Q1-59 D

Q1-60 C

Q1-61 c

	Assets	=	Liabilities	+	Stockholders' Equity
Beg.	\$149,000	=	\$27,000*	+	\$122,000
Changes			+ 69,000		
End.	\$236,000*	=	\$96,000*	+	\$140,000

*Must solve for these amounts.

Quiz (continued)

		<u>Assets – Liabilities = Stockholders' equity</u>			
Q1-62	b	Beg. bal.	\$350,000	– \$23,000 =	\$327,000
		+ Net income			+ X
		– Dividends			<u>– 75,000</u>
		End. bal.	\$530,000	– \$36,000 =	\$494,000

$$\$327,000 + X - \$75,000 = \$494,000; X = \$242,000$$

Q1-63 d

Problems

(30 min.) P 1-64A

Computed amounts in boxes.

	Kennedy Corp.	Caring Co.	Childress, Inc.
	<i>(Millions)</i>		
BALANCE SHEET			
<i>Beginning:</i>			
Assets	\$76	\$30	\$17
Liabilities.....	51	21	1
Common stock	7	7	6
Retained earnings	18	2	10
<i>Ending:</i>			
Assets	\$86	\$48	\$20
Liabilities.....	53	32	0
Common stock	7	12	8
Retained earnings	26	4	12
INCOME STATEMENT			
Revenues	\$227	\$165	\$22
Expenses	218	157	18
Net income.....	\$ 9	\$ 8	\$ 4
STATEMENT OF RETAINED EARNINGS			
Beginning RE.....	\$18	\$ 2	\$ 10
+ Net income.....	9	8	4
- Dividends declared	(1)	(6)	(2)
= Ending RE	\$26	\$ 4	\$ 12

(continued) P 1-64A

	<u>Kennedy Corp.</u>	<u>Caring Co.</u>	<u>Childress, Inc.</u>
	<i>Millions</i>		
Net income.....	\$9 <i>Highest</i>	\$8	\$4
% of net income to revenues	$\frac{\$9}{\$227} = 4.0\%$	$\frac{\$8}{\$165} = 4.8\%$	$\frac{\$4}{\$22} = 18.2\%$ <i>Highest</i>

Req. 1

**City News, Inc.
Balance Sheet
May 31, 2021**

ASSETS		LIABILITIES	
Cash	\$ 10,000	Accounts payable	\$ 6,500
Accounts receivable	2,600	Note payable	<u>50,000</u>
Notes receivable	15,800	Total liabilities	56,500
Office supplies	700	STOCKHOLDERS'	
Land	81,000	EQUITY	
Equipment	35,600	Stockholders' equity	89,200*
		Total liabilities and	
Total assets	<u>\$145,700</u>	stockholders' equity	<u>\$145,700</u>

*Total assets (\$145,700) – Total liabilities (\$56,500) = Stockholders' equity (\$89,200).

Req. 2

City News, Inc. is in *better (not worse)* financial position than the erroneous balance sheet reports. Total assets (\$145,700) are \$7,800 higher than originally reported (\$137,900), liabilities are \$14,700 lower than originally reported, and stockholders' equity is \$22,500 higher than reported originally.

Req. 3

The following accounts are not reported on the balance sheet because they are expenses. These accounts are reported on the *income statement*.

Utilities expense
Advertising expense

Salary expense
Interest expense

Req. 1

Brandon Hilton Realtor, Inc.
Balance Sheet
June 30, 2022

ASSETS		LIABILITIES	
Cash	\$ 55,000	Accounts payable	\$ 16,000
Office supplies	8,000	Note payable	<u>112,000</u>
Land	165,000	Total liabilities	128,000
Furniture	30,000	STOCKHOLDERS'	
Franchise	20,000	EQUITY	
		Common stock	65,000
		Retained earnings	<u>85,000*</u>
		Total stockholders' equity	150,000
		Total liabilities and	
Total assets	<u>\$278,000</u>	stockholders' equity	<u>\$278,000</u>

*Total assets (\$278,000) – Total liabilities (\$128,000) – Common stock (\$65,000) = Retained earnings (\$85,000).

Req. 2

It appears that the business can pay its debts. Total assets exceed total liabilities.

Req. 3

Personal items not reported on the *balance sheet* of the business:

- a. Personal cash (\$15,000)
- b. Personal account payable (\$3,400)
- g. Personal residence (\$334,000) and mortgage payable (\$182,000)

Req. 1

**Oak Hill Garden Supply, Inc.
Income Statement
Year Ended December 31, 2021**

Revenue		
Service revenue.....		\$452,600
Expenses		
Salary expense	\$108,400	
Rent expense.....	41,200	
Interest expense.....	10,300	
Utilities expense.....	8,800	
Property tax expense.....	<u>7,400</u>	
Total expenses		<u>176,100</u>
Net income		<u>\$276,500</u>

Req. 2

**Oak Hill Garden Supply, Inc.
Statement of Retained Earnings
Year Ended December 31, 2021**

Retained earnings, December 31, 2020.....	\$ 364,600
Add: Net income	<u>276,500</u>
Subtotal	641,100
Less: Dividends declared	<u>(107,000)</u>
Retained earnings, December 31, 2021	<u>\$ 534,100</u>

Req. 3

**Oak Hill Garden Supply, Inc.
Balance Sheet
December 31, 2021**

ASSETS		LIABILITIES	
Cash	\$ 44,000	Accounts payable	\$ 26,000
Accounts receivable	84,900	Interest payable	2,700
Supplies	6,300	Note payable	<u>99,600</u>
Land	25,000	Total liabilities	128,300
Building	406,000	STOCKHOLDERS'	
Equipment	110,000	EQUITY	
		Common stock	13,800
		Retained earnings	<u>534,100</u>
		Total stockholders' equity	547,900
		Total liabilities and	
Total assets	<u>\$676,200</u>	stockholders' equity	<u>\$676,200</u>

Req. 4

- a. Oak Hill Garden Supply was profitable; net income was \$276,500.
- b. Retained earnings increased by \$169,500 — from \$364,600 to \$534,100.
- c. Stockholders' equity (\$547,900) exceeds liabilities (\$128,300).

The stockholders have a greater claim against Oak Hill Garden Supply's assets than do the company's creditors.

Req. 1

Mitchell Company
Statement of Cash Flows
Year Ended March 31, 2022

*Millions***Cash flows from operating activities:**

Net income.....	\$ 3,020
Adjustments to reconcile net income to net cash provided by operating activities	<u>2,420</u>
Net cash provided by operating activities	5,440

Cash flows from investing activities:

Purchases of property, plant, and equipment.....	\$(2,640)
Sales of property, plant, and equipment	25
Other investing cash payments.....	<u>(195)</u>
Net cash used for investing activities	(2,810)

Cash flows from financing activities:

Issuance of common stock.....	\$ 190
Payment of dividends	<u>(265)</u>
Net cash used for financing activities.....	<u>(75)</u>

Net increase in cash.....	\$ 2,555
Cash, beginning.....	<u>220</u>
Cash, ending	<u><u>\$ 2,775</u></u>

Req. 2

Operating activities provided the largest amount of cash. This signals financial strength because operations should be the main source of cash.

(40-50 min.) P 1-69A

INCOME STATEMENT

			2022	2021	
Revenues	13,920	= \$	k	\$14,750	
Cost of goods sold			(11,100)	A	= (11,680)
Other expenses			<u>(1,300)</u>	<u>(1,200)</u>	
Income before income taxes			1,520	1,870	
Income taxes (35% tax rate).....	532	=	<u>l</u>	<u>(655)</u>	
Net income	988	=	<u>\$ m</u>	<u>\$ b</u>	= 1,215

STATEMENT OF RETAINED EARNINGS

Beginning balance	3,825	= \$	n	\$ 2,680	
Net income	988	=	o	C	= 1,215
Dividends declared			<u>(92)</u>	<u>(70)</u>	
Ending balance	4,721	=	<u>\$ p</u>	<u>\$ d</u>	= 3,825

BALANCE SHEET

Assets:

Cash	1,020	= \$	q	\$ e	= 1,180
Property, plant and equipment.....			1,547	1,316	
Other assets	11,959	=	<u>r</u>	<u>11,104</u>	
Total assets	14,526	=	<u>\$ s</u>	<u>\$13,600</u>	

Liabilities:

Current liabilities	4,815	= \$	t	\$ 5,660	
Long-term debt			4,350	3,370	
Other liabilities.....			<u>35</u>	<u>180</u>	
Total liabilities.....			9,200	F	= 9,210

Stockholders' Equity:

Common stock.....			\$ 425	\$ 425	
Retained earnings	4,721	=	u	G	= 3,825
Other stockholders' equity			<u>180</u>	<u>140</u>	
Total stockholders' equity	5,326	=	<u>v</u>	<u>4,390</u>	
Total liabilities and stockholders' equity	14,526	=	<u>\$ w</u>	<u>\$ h</u>	= 13,600

STATEMENT OF CASH FLOWS.....

Net cash provided by operating activities	630	= \$	x	\$ 875	
Net cash used for investing activities			(270)	(425)	

Net cash used for financing activities		<u>(520)</u>	<u>(520)</u>		
Increase (decrease) in cash		(160)	1	=	(70)
Cash at beginning of year	1,180	=	<u>y</u>	<u>1,250</u>	
Cash at end of year	1,020	=	<u>\$ z</u>	<u>\$ j</u>	= 1,180

(30 min.) P 1-70B

Computed amounts in boxes

	Babble Co.	Floralties, Inc.	Drake Co.
	<i>Millions</i>		
Balance Sheet			
<i>Beginning:</i>			
Assets.....	\$ 79	\$ 35	\$ 13
Liabilities.....	51	15	5
Common stock	1	5	2
Retained earnings	27	15	6
<i>Ending:</i>			
Assets.....	\$ 88	\$ 53	\$ 15
Liabilities.....	52	27	4
Common stock	1	12	5
Retained earnings	35	14	6
INCOME STATEMENT			
Revenues	\$227	\$163	\$ 27
Expenses.....	218	153	23
Net income	\$ 9	\$ 10	\$ 4
STMT. OF RETAINED EARNINGS			
Beginning RE.....	\$ 27	\$ 15	\$ 6

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Chapter 1 The Financial Statements 1-55

+ Net income	→	<u>9</u>	10 —	4 —
– Dividends declared		<u>(1)</u>	<u>(11)</u>	<u>(4)</u>
= Ending RE		<u>\$ 35</u>	<u>\$ 14</u> —	<u>\$ 6</u> ←

(continued) P 1-70B

	<u>Babble Co.</u>	<u>Floralties, Inc.</u>	<u>Drake Co.</u>
	<i>Millions</i>		
Net income	\$9	\$10 <i>Highest</i>	\$4
% of net income to revenues	$\frac{\$9}{\$227} = 4.0\%$	$\frac{\$10}{\$163} = 6.1\%$	$\frac{\$4}{\$27} = 14.8\%$ <i>Highest</i>

Req. 1

**Parker Design, Inc.
Balance Sheet
March 31, 2021**

ASSETS		LIABILITIES	
Cash	\$ 8,000	Accounts payable	\$ 3,500
Accounts receivable	3,900	Note payable	<u>53,000</u>
Notes receivable	13,000	Total liabilities	56,500
Office supplies	1,400	STOCKHOLDERS'	
Land	86,000	EQUITY	
Equipment	39,000	Stockholders' equity	94,800*
		Total liabilities and	
Total assets	<u>\$151,300</u>	stockholders' equity	<u>\$151,300</u>

*Total assets (\$151,300) – Total liabilities (\$56,500) = Stockholders' equity (\$94,800).

Req. 2

Parker Design, Inc. is in a *better* financial position than the erroneous balance sheet reports. Assets are \$9,800 greater and liabilities are \$16,300 less than originally reported, and equity is \$26,100 greater than reported originally.

Req. 3

The following accounts are not reported on the balance sheet because they are expenses. Expenses are reported on the *income statement*.

Utilities expense
Advertising expense
Salary expense
Interest expense

Req. 1

Hudson Alvarez Realtor, Inc.
Balance Sheet
June 30, 2022

ASSETS		LIABILITIES	
Cash	\$ 44,000	Accounts payable	\$ 9,000
Office supplies	4,000	Note payable	<u>102,000</u>
Land	162,000	Total liabilities	111,000
Furniture	17,600	STOCKHOLDERS'	
Franchise	16,000	EQUITY	
		Common stock	75,000
		Retained earnings	<u>57,600*</u>
		Total stockholders' equity	<u>132,600</u>
Total assets	<u>\$243,600</u>	Total liabilities and stockholders' equity	<u>\$243,600</u>

*Total assets (\$243,600) – Total liabilities (\$111,000) – Common stock (\$75,000) = Retained earnings (\$57,600).

Req. 2

It appears that Hudson Alvarez's business can pay its debts. Total assets far exceed total liabilities.

Req. 3

Personal items not reported on the *balance sheet* of the business:

- a. Personal cash (\$17,000)
- b. Personal account payable (\$6,500)
- g. Personal residence (\$419,000) and personal mortgage (\$179,000)

Req. 1

**Full Moon Products, Inc.
Income Statement
Year Ended December 31, 2021**

Revenue:

Service revenue.....	\$451,600
----------------------	-----------

Expenses:

Salary expense	\$108,900
----------------------	-----------

Rent expense.....	41,000
-------------------	--------

Interest expense.....	10,000
-----------------------	--------

Utilities expense.....	8,100
------------------------	-------

Property tax expense.....	<u>7,300</u>
---------------------------	--------------

Total expenses	<u>175,300</u>
----------------------	----------------

Net income	<u>\$276,300</u>
------------------	------------------

Req. 2

**Full Moon Products, Inc.
Statement of Retained Earnings
Year Ended December 31, 2021**

Retained earnings, December 31, 2020.....	\$364,800
---	-----------

Add: Net income.....	<u>276,300</u>
----------------------	----------------

Subtotal	641,100
----------	---------

Less: Dividends declared	<u>(108,000)</u>
--------------------------------	------------------

Retained earnings, December 31, 2021	<u>\$533,100</u>
--	------------------

Req. 3

**Full Moon Products, Inc.
Balance Sheet
December 31, 2021**

ASSETS		LIABILITIES	
Cash	\$ 46,000	Accounts payable	\$ 25,000
Accounts receivable	85,000	Interest payable	2,800
Supplies	6,200	Note payable	<u>99,200</u>
Land	29,000	Total liabilities	127,000
Building	405,000	STOCKHOLDERS'	
Equipment	115,000	EQUITY	
		Common stock	26,100
		Retained earnings	<u>533,100</u>
		Total stockholders' equity	559,200
		Total liabilities and	
Total assets	<u>\$686,200</u>	stockholders' equity	<u>\$686,200</u>

Req. 4

- a. Full Moon Products was profitable; net income was \$276,300.
- b. Retained earnings increased by \$168,300 — from \$364,800 to \$533,100.
- c. Total equity (\$559,200) exceeds total liabilities (\$127,000).

Therefore, the stockholders have a greater claim against the company's assets than do the creditors.

(20 min.) P 1-74B

Req. 1

**Tidal Wave Company
Statement of Cash Flows
Year Ended March 31, 2022**

	<i>Millions</i>
Cash flows from operating activities:	
Net income.....	\$ 3,050
Adjustments to reconcile net income to net cash provided by operating activities	<u>2,380</u>
Net cash provided by operating activities	5,430
 Cash flows from investing activities:	
Purchases of property, plant, and equipment.....	\$(3,500)
Sales of property, plant, and equipment	60
Other investing cash payments.....	<u>(200)</u>
Net cash used for investing activities	(3,640)
 Cash flows from financing activities:	
Issuance of common stock.....	\$ 200
Payment of dividends.....	<u>(360)</u>
Net cash used for financing activities.....	<u>(160)</u>
 Net increase in cash.....	\$1,630
Cash, beginning.....	<u>270</u>
Cash, ending	<u><u>\$ 1,900</u></u>

Req. 2

Operating activities provided the bulk of Tidal Wave Company's cash. This is a sign of strength because operations should be the main source of cash.

(40-50 min.) P 1-75B*(Thousands)***INCOME STATEMENT**

		2022	2021	
Revenues	13,800 =	\$ k	\$16,175	
Cost of goods sold		(11,020)	a	= (13,115)
Other expenses		<u>(1,250)</u>	<u>(1,220)</u>	
Income before income taxes.....		1,530	1,840	
Income taxes (35% tax rate).....	536 =	<u>l</u>	<u>644</u>	
Net income.....	994 =	<u>\$ m</u>	<u>\$ b</u>	= 1,196

STATEMENT OF RETAINED EARNINGS

Beginning balance	3,726 =	\$ n	\$ 2,670	
Net income.....	994 =	o	c	= 1,196
Dividends declared		<u>(98)</u>	<u>(140)</u>	
Ending balance	4,622 =	<u>\$ p</u>	<u>\$ d</u>	= 3,726

BALANCE SHEET**Assets:**

Cash	980 =	\$ q	\$ e	= 1,090
Property, plant and equipment		1,487	1,316	
Other assets	12,205 =	<u>r</u>	<u>12,060</u>	
Total assets.....	14,672 =	<u>\$ s</u>	<u>\$14,466</u>	

Liabilities:

Current liabilities.....	3,955 =	\$ t	\$ 5,610	
Long-term debt.....		4,450	3,360	
Other liabilities		<u>995</u>	<u>1,140</u>	
Total liabilities.....		9,400	f	= 10,110

Stockholders' Equity:

Common stock		\$ 450	\$ 450	
Retained earnings	4,622 =	u	g	= 3,726
Other stockholders' equity.....		<u>200</u>	<u>180</u>	
Total stockholders' equity	5,272 =	<u>v</u>	<u>4,356</u>	
Total liabilities and stockholders' equity	14,672 =	<u>\$ w</u>	<u>\$ h</u>	= 14,466

STATEMENT OF CASH FLOWS

Net cash provided by operating activities	700 =	\$ x	\$ 875	
Net cash used for investing activities.....		(300)	(575)	
Net cash used for financing activities.....		<u>(510)</u>	<u>(500)</u>	
Increase (decrease) in cash		(110)	i	= (200)

Cash at beginning of year	1,090	=	_____y	<u>1,290</u>	
Cash at end of year	980	=	<u>\$_____z</u>	<u>\$_____j</u>	= 1,090

Serial Case

(15-20 min) C1-76

1. The Cheesecake Factory is organized as a corporation, per the name of the business (“Incorporated”).
2. Net income flows from the Income Statement to the Statement of Retained Earnings.
3. Ending retained earnings flows from the Statement of Retained Earnings to the Balance Sheet
4. Ending cash and cash equivalents flows from the Statement of Cash Flows to the Balance Sheet
5. The Cheesecake Factory earned net income of \$127,293 (in thousands) in fiscal 2019. This income was earned from January 1, 2019 to December 31, 2019.

6. The Cheesecake Factory’s accounting equation (in thousands):

$$\begin{array}{rclcl}
 \text{Assets} & = & \text{Liabilities} & + & \text{Shareholders' Equity} \\
 \$2,840,593 & = & \$2,268,851^* & + & \$571,742
 \end{array}$$

7. Cheesecake Factory had \$2,840,593 (Total Assets) to work with and owes \$2,268,851* (Total Liabilities) to creditors. (Numbers in thousands)

$$*(\$614,587 + \$1,654,264 = \$2,268,851)$$

Decision Cases

(30-40 min.) C1-77

Req. 1

Based solely on these balance sheets, Insley Sales Co. appears to be the better credit risk because:

- 1. Queens Service has more assets (\$150,000) than Insley Sales (\$65,000), but Queens Service owes much more in liabilities (\$130,000 versus \$15,000 for Insley Sales). Insley Sales' stockholders' equity is far greater than that of Queens Service (\$50,000 compared to \$20,000). Insley Sales is not heavily in debt, but Queens Service is.**
- 2. You would be better off granting the loan to Insley Sales. You should consider what will happen if the borrower cannot pay you back as planned. Queens Service has far more liabilities to pay, and it may be hard for Queens Service to come up with the money to pay you. On the other hand, Insley Sales has little debt to pay to others before paying you.**

Student responses may vary.

(20-30 min.) C1-78

Req. 1

Flowers Unlimited, Inc. Income Statement Year Ended Dec. 31, 2021		Flowers Unlimited, Inc. Balance Sheet Dec. 31, 2021	
Revenue.....	\$140,000 ¹	Cash.....	\$ 6,000
Expenses.....	<u>140,000</u> ²	Other assets....	<u>90,000</u> ³
Net income.....	\$ <u>-0-</u>	Total assets.....	<u>\$96,000</u>
		Liabilities.....	\$70,000 ⁴
		S/H Equity.....	<u>26,000</u> ⁵
		Total liabilities and S/H equity	<u>\$96,000</u>

¹\$100,000 + \$40,000 = \$140,000

²\$80,000 + \$50,000 + \$10,000 = \$140,000

³\$100,000 – \$50,000 + \$40,000 = \$90,000

⁴\$60,000 + \$10,000 = \$70,000

⁵\$96,000 – \$70,000 = \$26,000

Req. 2

The company's *financial position* is much *weaker* than originally reported. Assets and stockholders' equity are lower and liabilities are higher. *Results of operations* are *worse* than reported. The company did not earn any profit.

Req. 3

Based on the actual figures, I would *not* invest in Flowers Unlimited for reasons given in *Req. 2*.

Ethical Issue

(40-50 min) C1-79

Note to instructor: student responses will vary on this problem. Keep the discussion pointed toward use of the multiple-criteria model for making good ethical decisions, pointing out elements of students' reasoning that may be faulty or incomplete. It might be useful to have a debate or role play, assigning students to different sides of the issue (for or against accepting a copy of the exam).

Req. 1

The fundamental ethical issue in this situation is whether you should accept a copy of the old exam from your friend.

Req. 2

The stakeholders are:

- a. You**
- b. Your friend**
- c. The remainder of the students in the class**
- d. The professor**
- e. The University**
- f. Your family**

(This may not be a complete list; you may think of more.)

Consequences are discussed in requirement 3.

Req. 3

Analysis of the problem:

Economic perspective: If use of the old exam turns out to help you (it may not) you might improve your grade and allow you to retain your scholarship. This might help you and your family financially. If you use the exam to your unfair advantage, and you are reported, you and possibly your friend might receive grades of F in the class although you might otherwise have passed. This could cause adverse economic consequences to you, your friend and your families.

Legal perspective: Although it may not violate local or federal law, giving or accepting copies of old exams may violate the university's honor code, which serves the same purpose as a legal code in this case. If you use the old exam and it turns out that you violated the University's honor code, both you and your friend could be in trouble. Your family and your friend's family could also be impacted by any adverse consequences to you or her. Academic institutions establish policies against academic dishonesty because cheating hurts everyone—the student who commits the act, the other students in the class whose rights to fair treatment are violated by cheating, and the professor who must endure hours of investigating, reporting, and perhaps testifying.

Ethical perspective: Receiving questionable help from others in the face of policies that prohibit it is, at best, risky, and at worst, downright wrong. Cheating is similar to stealing, since it is stealing

the work of another without their permission. It is usually accompanied by lying to cover it up, or at least, not revealing the truth. Cheating violates other students' rights to fair and equal treatment. It violates the instructor's rights to run a course as a "fair game" for all participants. Because the students and faculty are hurt by cheating, the university is hurt too. If cheating goes unpunished, grades are inflated, ultimately damaging the academic reputation of the institution and eroding the value of its degrees. Parents of students who are caught cheating have to endure the agony of working through the problem with their son or daughter, and perhaps the social stigma that comes from adverse publicity.

These are just some of the arguments against cheating. Of course, there is a question in this case as to whether taking the test actually violates the professor's or the university's policies.

Req. 4

It would be helpful to find out what the professor's policies are with respect to the use of fraternity and sorority test files. The university might have a blanket policy on this. (Some students might spend a little time researching this by reading the university's honor code on their web site; just reading the honor code will be an eye-opening

experience for most students). Advise your students to research the use of fraternity and sorority test files on the university web site, or to

(continued) C1-79

discuss the issue with the head of the department or the chair of the university honor council.

Unfortunately, in this case, there is not much time. Researching the issue in the university's honor code takes valuable time away from studying for the exam, which, if you do, could help you raise your grade and solve the whole problem!

Probably the best solution to this problem is "when in doubt, don't." You may not do well on the test, but at least you won't have to live with the terrible consequences of being accused as a cheater. It should make you feel better in the long run that, although you may not make the highest grades in the class, at least you are not a cheater.

Req. 5

Cheating is very closely related to stealing, which is a form of fraud. When employees steal from their companies, they steal property that belongs to others. There are economic, legal, and ethical consequences to the company, the employee and their families, and customers (who ultimately have to pay for fraud through higher prices). We will study fraud in depth in Chapter 4.

Focus on Financials: Apple Inc.

(20-30 min.) C1-80

- 1. Students can emphasize a variety of points regarding Apple Inc., and its industry. For example, a discussion on the product innovation and competitive changes in technology would be appropriate. Additionally, discussing recent news articles related to Apple or its competitors would also be appropriate. Student answers will vary.**
- 2. Some important information in this portion of the financials is the description of their distribution channels (third-party resellers), competitors (product innovation, market opportunities, etc.), and supply chain (shortages, component availability, outsourcing, etc). Additionally, the seasonality of Apple's business is important to note given that it has higher sales in its first quarter relative to the last three. Lastly, it may come as a surprise that Apple employs approximately 137,000 full-time employees. (Student answers will vary.)**
- 3. Samsung, Google, Sony, or HP are some of Apple Inc.'s competitors. It is important to identify competitors because competitors tend to have similar business dynamics to one another, meaning that their financial statements can be compared to and benchmarked against each other. Student answers will vary.**

(continued) C1-80

4. ***Net income***, because it shows the overall result of all the revenues minus all the expenses for a period. In effect, net income gives the results of operations in a single figure and shows whether the company has been profitable. Apple's net income after taxes decreased from \$59.5 billion in 2018 to \$55.3 billion in 2019, which is unfavorable.

5. Apple Inc.'s largest expense is cost of sales. The company has cost of sales for products and cost of sales for services. The former is the cost of the products that the company sells, such as iPhones, iPads, Apple TVs, software, and Mac desktops. The cost of sales for services pertains to the cost of services that Apple provides such as iCloud, Siri, and Maps. Another title of this account is *cost of goods sold*. In this chapter, The Walt Disney Company called this account cost of products and cost of services.

6. Total resources (total assets) at September 28, 2019.....\$338,516 million

Assets
\$338,516 million

Amount owed (total liabilities) at September 28, 2019....\$248,028 million

Portion of the company's assets owned by the stockholders (stockholders' equity) at September 28, 2019.....\$90,488 million

Apple Inc.'s accounting equation (*in millions*):

(continued) C1-80

- 7. At September 29, 2018, Apple Inc. had \$25,913 million of cash and cash equivalents. At September 28, 2019, Apple Inc. had \$48,844 million of cash and cash equivalents.**

Focus on Analysis: Under Armour, Inc.

(30 min.) C1-81

- 1. Under Armour, Inc. is an athletic apparel company. Students can emphasize a variety of points regarding Under Armour, Inc. and its industry. For example, a discussion on the brand, new product development, etc. would be appropriate. Additionally, discussing recent news articles related to Under Armour or its competitors would also be appropriate. (Student answers will vary.)**

- 2. Note 1 states Under Armour is a developer, marketer and distributor of branded performance apparel, footwear, and accessories. These products are sold worldwide and worn by athletes of all levels and consumers with active lifestyles.**

- 3. Nike, Adidas, and Columbia Sportswear are some of Under Armour, Inc.'s competitors. It is important to identify competitors because competitors tend to have similar business dynamics to one another, meaning that their financial statements can be compared to and benchmarked against each other. (Student answers will vary.)**

4. Under Armour, Inc.'s Accounting Equation (*in thousands*):

Assets	=	Liabilities	+	Shareholders' Equity
\$4,843,531	=	\$2,693,444	+	\$2,150,087

If we express the numbers in millions:

Assets	=	Liabilities	+	Shareholders' Equity
\$4,843	=	\$2,693	+	\$2,150

Under Armour, Inc. appears to be in strong financial condition. Total assets are significantly higher than the amount of total liabilities. This suggests that the company will have no difficulty paying its debts and will have money to expand.

5. The result of operations for 2019 was a net income of \$92,139 thousand, following two years of net losses. This is good news for Under Armour, Inc. Revenue exceeded expenses for fiscal 2019, and there appears to be a reversal of the company's fortunes from previous years. It is too early to tell, however, whether profitability is a trend.

6. According to Under Armour, Inc.'s Consolidated Statements of Stockholders' Equity, the cause of the company's increase in retained earnings during 2019 was comprehensive income of \$92,139 thousand. (Comprehensive income is closely related to net income.)

7. The Consolidated Balance Sheets report cash and cash equivalents as part of the company's financial position. The Consolidated

(continued) C1-81

Statements of Cash Flows tell why cash and cash equivalents increased or decreased. Operating activities provided \$509,031 thousand, investing activities used \$147,113 thousand, and financing activities used \$137,070 thousand.

Group Projects

Student responses will vary.

Chapter 1: The Financial Statements

Learning Objectives

1. **Explain** why accounting is critical to business
2. **Explain and apply** underlying accounting concepts, assumptions, and principles
3. **Apply** the accounting equation to business organizations
4. **Construct** financial statements and **analyze** the relationships among them
5. **Evaluate** business decisions ethically
6. **Identify** tools and technologies used in accounting and business

Chapter Outline

- I. Accounting – Critical to Business
 - A. Decision makers
 1. Individuals
 2. Investors and creditors
 3. Regulatory bodies
 4. Nonprofit organizations
 - B. Financial accounting vs. management accounting
 - C. Organizing a business
 1. Proprietorship
 2. Partnership
 3. Limited-liability company
 4. Corporation
- II. Underlying Accounting Concepts, Assumptions, and Principles
 - A. Financial Accounting Standards Board (FASB)/Generally Accepted Accounting Principles (GAAP)
 - B. International Accounting Standards Board (IASB)/International Financial Reporting Standard (IFRS)
 - C. Fundamental qualitative characteristics
 1. Relevance
 2. Faithful representation
 - D. Enhancing (supplementary) qualitative characteristics
 1. Comparability
 2. Verifiability
 3. Timeliness
 4. Understandability
 - E. Cost/benefit
 - F. Entity assumption

- G. Continuity (going-concern) assumption
- H. Historical cost principle
- I. Stable-monetary-unit assumption
- III. Application of the Accounting Equation ($\text{Assets} = \text{Liabilities} + \text{Equity}$)
 - A. Assets – economic resources with future benefit
 - B. Liabilities – “outsider claims”
 - C. Owners’ equity – “insider claims”
 - 1. Paid-in capital
 - 2. Retained earnings
 - a. Revenues
 - b. Expenses
 - c. Dividends
- IV. Construct Financial Statements and Analyze the Relationships Among Them
 - A. The Income Statement ($\text{Revenues} - \text{Expenses} = \text{Net Income (Net Loss)}$)
 - 1. Revenues and
 - 2. Gains
 - 3. Expenses and
 - 4. Losses
 - B. Statement of Retained Earnings ($\text{Beginning Retained Earnings} + \text{Net Income} - \text{Dividends} = \text{Ending Retained Earnings}$)
 - C. Balance Sheet ($\text{Assets} = \text{Liabilities} + \text{Equity}$)
 - 1. Assets
 - a. Current assets
 - b. Long-term (non-current) assets
 - 2. Liabilities
 - a. Current liabilities
 - b. Long-term liabilities
 - 3. Stockholders’ equity
 - a. Paid-in capital (common stock and additional paid-in capital)
 - b. Retained earnings
 - c. Sometimes, Treasury stock and/or Other equity
 - D. Statement of Cash Flows ($\text{Net cash flow from (Operating Activities} + \text{or} - \text{Investing Activities} + \text{or} - \text{Financing Activities)} + \text{Beginning Cash balance} = \text{Ending Cash balance}$)
- V. Evaluate Business Decisions Ethically
 - A. The role of judgment
 - B. Economic factors
 - C. Legal factors
 - D. Ethical factors
 - E. AICPA Code of Professional Conduct

- VI. Identify Tools and Technologies Used in Accounting and Business
- A. Spreadsheets
 - B. Data Analytics
 - C. Artificial Intelligence (AI) and Machine Learning
 - D. Robotic Process Automation (RPA)
 - E. Technology Risks
 - F. Introduction to Excel

Chapter Activities

1. Chapter Opener

Chapter 1 spotlights The Walt Disney Company and details the services and products the worldwide entertainment corporation provides and sells, its network of theme parks, movies, and stores, and financial information for the year ended September 28, 2019. Additionally, the section introduces the terms “revenues” and “net income.” Discuss with the students the many different ways Disney generates revenues as they produce and provide entertainment; mention the services and goods that the company sells and the prices related to those items. Talk about the flow of revenues from goods and services sold to the financial statements and how those revenues become part of net income. Visit <http://www.disney.com> and read about the company’s many different sources of revenues. From the company’s website, <https://thewaltdisneycompany.com>, you can also download the most current annual report. Throughout this chapter, there are many references to information from Disney’s financial statements.

Additionally, ask the students what information they would need from the financial statements if they had \$10,000 to invest. How would they decide if The Walt Disney Company was a good investment?

2. Accounts Activity

On slips of paper, list accounts and distribute one slip of paper to each student. You can use the following chart of accounts as an example:

Cash
Accounts Receivable
Inventory
Prepaid Rent
Office Supplies
Land
Automobiles
Buildings
Patents
Copyrights
Trademark
Accounts Payable
Income Taxes Payable
Interest Payable
Notes Payable
Salaries and Wages Payable
Bonds Payable
Common Stock

Retained Earnings
Sales Revenue
Interest Revenue
Rent Revenue
Advertising Expense
Commissions Expense
Cost of Goods Sold
Depreciation Expense
Income Tax Expense
Insurance Expense
Interest Expense
Salary and Wage Expense
Supplies Expense
Dividends
Dividends Payable

Divide the room up into five areas: assets, liabilities, stockholders' equity, revenues, and expenses. Ask the students to move to their particular area of the room depending on what account types they have been assigned. Quiz each student to confirm that he or she is in the correct section of the room. Move the students accordingly if they are in the wrong section. Repeat the exercise by dividing the room into a balance sheet section and an income statement section. Again, quiz the students to confirm that they are in the correct area for that particular financial statement and move them, if necessary.

Difficult Topics

- Statement of Cash Flows

Chapter 1: Assignment Grid

					(Will have an X if available)	
Assignment	Topic(s)	L.O.	Estimated Time (minutes)	Level of Difficulty	Excel Projects	General Ledger Templates
S1-1	Explain and differentiate between business organizations	1	10	Easy		
S1-2	Identify relevant accounting assumptions	2	5	Easy		
S1-3	Identify underlying accounting concepts, assumptions, and principles	2	5-10	Easy		
S1-4	Apply the accounting equation	3	10	Easy		
S1-5	Apply the accounting equation	3	5	Easy		
S1-6	Identify assets, liabilities, and stockholders' equity accounts	3	5-10	Easy		
S1-7	Accounting equation	3	5-10	Easy		
S1-8	Identify income statement components	4	5	Easy		
S1-9	Identify appropriate financial statement	4	10	Easy		
S1-10	Explain aspects of financial statements	4	15-20	Medium		
S1-11	Identify appropriate financial statement use	4	5	Easy		
S1-12	Construct an income statement	4	5	Easy		
S1-13	Construct a statement of retained earnings	4	5	Easy		
S1-14	Construct a balance sheet	4	10-15	Easy	X	
S1-15	Solve for retained earnings and construct a balance sheet	4	10-15	Medium		

Assignment	Topic(s)	L.O.	Estimated Time (minutes)	Level of Difficulty	Excel Projects	General Ledger Templates
S1-16	Construct a statement of cash flows	4	10-15	Medium		
S1-17	Construct an income statement, statement of retained earnings, and balance sheet	4	10-15	Medium	X	
S1-18	Evaluate business decisions ethically	5	5	Easy		
S1-19	Match vocabulary terms with definitions	1,2,3, 4,5	10-15	Medium		
S1-20	Identify tools and technologies used in accounting and business	6	5-10	Easy		
S1-21	Identify basic Excel components	6	5-10	Easy		
E1-22A	Apply the accounting equation; evaluate business operations	3,4	10-15	Medium		
E1-23A	Apply the accounting equation; evaluate business operations	3,4	10-15	Medium		
E1-24A	Apply the accounting equation; evaluate business operations	3,4	10-20	Medium		
E1-25A	Identify financial statement by type of information	4	10-15	Medium		
E1-26A	Construct a balance sheet	4	10-20	Medium		
E1-27A	Apply the accounting equation; construct a balance sheet	3,4	10-20	Medium		
E1-28A	Construct an income statement and a statement of retained earnings	4	15-25	Medium		
E1-29A	Construct an income statement and a statement of retained earnings	4	15-20	Medium		
E1-30A	Construct a balance sheet	4	15-20	Medium		

Assignment	Topic(s)	L.O.	Estimated Time (minutes)	Level of Difficulty	Excel Projects	General Ledger Templates
E1-31A	Construct a statement of cash flows	4	15-20	Medium		
E1-32A	Evaluate business operations through the financial statements	4	10-15	Difficult		
E1-33A	Construct an income statement, statement of retained earnings, and balance sheet	4	20-25	Medium		
E1-34B	Apply the accounting equation; evaluate business operations	3,4	10-15	Medium		
E1-35B	Apply the accounting equation; evaluate business operations	3,4	10-15	Medium		
E1-36B	Apply the accounting equation; evaluate business operations	3,4	10-20	Medium		
E1-37B	Identify financial statement by type of information	4	10-15	Medium		
E1-38B	Construct a balance sheet	4	10-20	Medium		
E1-39B	Apply the accounting equation; construct a balance sheet	3,4	10-20	Medium		
E1-40B	Construct an income statement and a statement of retained earnings	4	15-25	Medium		
E1-41B	Construct an income statement and a statement of retained earnings	4	15-20	Medium		
E1-42B	Construct a balance sheet	4	15-20	Medium		
E1-43B	Construct a statement of cash flows	4	15-20	Medium		
E1-44B	Evaluate business operations through the financial statements	4	10-20	Difficult		

Assignment	Topic(s)	L.O.	Estimated Time (minutes)	Level of Difficulty	Excel Projects	General Ledger Templates
E1-45B	Construct an income statement, statement of retained earnings, and balance sheet	4	20-25	Medium		
Q1-46 – Q1-63	Quiz questions	All	20-30	Medium		
P1-64A	Apply the accounting equation; evaluate business operations	3,4	30	Medium		
P1-65A	Apply the accounting equation; evaluate business operations; construct a balance sheet	3,4	20-25	Medium		
P1-66A	Apply underlying accounting concepts; evaluate business operations; construct a balance sheet	2,3,4	20-25	Difficult		
P1-67A	Evaluate business operations; construct and analyze an income statement, a statement of retained earnings, and a balance sheet	3,4	30-45	Medium		
P1-68A	Evaluate business operations; construct a statement of cash flows	3,4	20	Medium		
P1-69A	Construct financial statements	4	40-50	Medium		
P1-70B	Apply the accounting equation; evaluate business operations	3,4	30	Medium		
P1-71B	Apply the accounting equation; evaluate business operations; construct a balance sheet	3,4	20-25	Medium		

Assignment	Topic(s)	L.O.	Estimated Time (minutes)	Level of Difficulty	Excel Projects	General Ledger Templates
P1-72B	Apply underlying accounting concepts; evaluate business operations; construct a balance sheet	2,3,4	20-25	Difficult		
P1-73B	Evaluate business operations; construct and analyze an income statement, a statement of retained earnings, and a balance sheet	3,4	30-45	Medium		
P1-74B	Evaluate business operations; construct a statement of cash flows	3,4	20	Medium		
P1-75B	Construct financial statements	4	40-50	Medium		
C1-76 The Cheesecake Factory	Analyze basic financial statement information	3,4	15-20	Medium		
C1-77 Decision Case 1	Explain accounting language; evaluate business operations through financial statements	1,4	30-40	Medium		
C1-78 Decision Case 2	Evaluate business operations through financial statements; correct errors; construct financial statements	3,4	20-30	Medium		
C1-79 Ethical Issue	Evaluate ethical decisions	5	40-50	Medium		
C1-80 Focus on Financials—Apple Inc.	Apply the accounting equation; evaluate business operations	3,4	20-30	Medium		
C1-81 Focus on Analysis—Under Armour, Inc.	Apply the accounting equation; evaluate business operations	3,4	30	Medium		
Group Project 1	Bank Loan	All	45-60	Difficult		

Assignment	Topic(s)	L.O.	Estimated Time (minutes)	Level of Difficulty	Excel Projects	General Ledger Templates
Group Project 2	Going Public	All	45-60	Difficult		

Answer Key to Chapter 1 Quiz (Quiz on following pages.)

1. A
2. B
3. C
4. D
5. A
6. D
7. A
8. C
9. A
10. D
11. D

Name _____ Date _____
Section _____

CHAPTER 1
10-MINUTE QUIZ

Circle the letter of the best response.

1. Which of these is a liability?
A. Long-Term Debt
B. Accounts Receivable
C. Cash
D. Inventory
2. Assumption that any organization or person that stands apart as a separate economic unit:
A. Continuity (going-concern) assumption.
B. Entity assumption.
C. Stable-monetary-unit assumption.
D. Historical cost principle.
3. Which financial statement is sometimes known as the statement of financial position?
A. Income Statement
B. Statement of Retained Earnings
C. Balance Sheet
D. Statement of Cash Flows
4. If total liabilities decreased by \$100,000 and total assets decreased by \$180,000 during the same accounting time period, what happened to total owners' equity during this period?
A. \$180,000 increase
B. \$180,000 decrease
C. \$80,000 increase
D. \$80,000 decrease
5. The equation for the Income Statement is:
A. Net Income = Total Revenues and Gains – Total Expenses and Losses
B. Net Income = Total Revenues and Gains + Total Expenses and Losses
C. Net Income = Total Revenues and Losses – Total Expenses and Gains
D. Net Income = Total Revenues and Losses + Total Expenses and Gains

6. Jennie Browne the owner of a small business. She has decided to save money during her initial years of operation by not hiring a professional accountant. She does not add noncash types of compensation included in some of the costs of her assets. Which accounting principle, concept, or assumption does this violate?
 - A. Entity assumption
 - B. Continuity (going-concern) assumption
 - C. Stable-monetary-unit assumption
 - D. Historical cost principle

7. The _____ states that accountants should assume that the dollar's purchasing power is stable over time.
 - A. Stable-monetary-unit assumption
 - B. Continuity (going-concern) assumption
 - C. Historical cost principle
 - D. Entity assumption

8. Which section of the balance sheet contains retained earnings and paid-in capital?
 - A. Assets
 - B. Liabilities
 - C. Stockholders' Equity
 - D. Long Term Assets

9. Listed below are the account balances of the Spark Corporation:

Accounts Payable	\$ 63,000
Building	190,000
Cash	88,000
Common Stock	150,000
Dividends	5,000
Land	160,000
Miscellaneous Expense	3,000
Service Revenue	250,000
Equipment	35,000
Note Payable due in 60 days	125,000
Long-Term Debt	13,000
Salary Expense	120,000

Total Assets are:

- A. \$473,000.
- B. \$438,000.
- C. \$248,000.
- D. \$385,000.

10. Listed below are the account balances of the Golden Corporation:

Accounts Payable	\$ 75,000
Cash	100,000
Common Stock	200,000
Dividends	10,000
Land	170,000
Miscellaneous Expense	10,000
Service Revenue	147,000
Equipment	130,000
Note Payable due in 90 days	60,000
Long-Term Debt	15,000
Salary Expense	87,000

Net Income (Net Loss) is:

- A. \$60,000
- B. \$40,000
- C. (\$18,000)
- D. \$50,000

Alternative Multiple-Choice Question on new Learning Objective

11. What is the most widely used program in business for spreadsheets?
- A. Robotic Process Automation (RPA)
 - B. Data Analytics
 - C. Apple Numbers
 - D. Microsoft Excel