CHAPTER 1

Accounting in Action

ASSIGNMENT CLASSIFICATION TABLE

Study Objectives	Questions	Brief Exercises	Exercises	A Problems	B Problems
1. Explain what accounting is.	1, 2, 5		1		
2. Identify the users and uses of accounting.	3, 4		2		
3. Understand why ethics is a fundamental business concept.			3		
4. Explain generally accepted accounting principles and the cost principle.	6		4		
5. Explain the monetary unit assumption and the economic entity assumption.	7, 8, 9, 10		4		
6. State the accounting equation, and define assets, liabilities, and owner's equity.	11, 12, 13	1, 2, 3, 4	5, 6, 7, 11	1A, 2A 4A	1B, 2B 4B
7. Analyze the effects of business transactions on the accounting equation.	14, 15, 16, 18	5, 6, 7, 8	6, 7, 8, 10, 11	1A, 2A, 4A, 5A	1B, 2B, 4B, 5B
8. Understand the four financial statements and how they are prepared.	17, 19, 20, 21	9, 10	9, 12, 13, 14, 15, 16	2A, 3A, 4A, 5A	2B, 3B, 4B, 5B

ASSIGNMENT CHARACTERISTICS TABLE

Problem Number	Description	Difficulty Level	Time Allotted (min.)
1A	Analyze transactions and compute net income.	Moderate	40–50
2A	Analyze transactions and prepare income statement, owner’s equity statement, and balance sheet.	Moderate	50–60
3A	Prepare income statement, owner’s equity statement, and balance sheet.	Moderate	50–60
4A	Analyze transactions and prepare financial statements.	Moderate	40–50
5A	Determine financial statement amounts and prepare owner’s equity statement.	Moderate	40–50
1B	Analyze transactions and compute net income.	Moderate	40–50
2B	Analyze transactions and prepare income statement, owner’s equity statement, and balance sheet.	Moderate	50–60
3B	Prepare income statement, owner’s equity statement, and balance sheet.	Moderate	50–60
4B	Analyze transactions and prepare financial statements.	Moderate	40–50
5B	Determine financial statement amounts and prepare owner’s equity statement.	Moderate	40–50

BLOOM'S TAXONOMY TABLE

Correlation Chart between Bloom's Taxonomy, Study Objectives and End-of-Chapter Exercises and Problems

Study Objective	Knowledge	Comprehension	Application	Analysis	Synthesis	Evaluation
1. Explain what accounting is.		Q1-1 Q1-5 Q1-2 E1-1				
2. Identify the users and uses of accounting.		Q1-3 E1-2 Q1-4				
3. Understand why ethics is a fundamental business concept.		E1-3				
4. Explain generally accepted accounting principles and the cost principle.		Q1-6 E1-4				
5. Explain the monetary unit assumption and the economic entity assumption.	Q1-8 Q1-9	Q1-7 Q1-10 E1-4				
6. State the accounting equation, and define assets, liabilities, and owner's equity.	Q1-11 Q1-12	Q1-13 E1-6 BE1-4 E1-7 E1-5	BE1-1 P1-2A BE1-2 P1-4A BE1-3 P1-1B E1-11 P1-2B P1-1A P1-4B			
7. Analyze the effects of business transactions on the accounting equation.		Q1-14 BE1-6 Q1-15 BE1-7 Q1-16 BE1-8 Q1-18 E1-6 BE1-5 E1-7	E1-8 P1-5A E1-10 P1-1B E1-11 P1-2B P1-1A P1-4B P1-2A P1-5B P1-4A			
8. Understand the four financial statements and how they are prepared.		Q1-17 Q1-19 BE1-10	Q1-20 P1-2A Q1-21 P1-3A BE1-9 P1-4A E1-9 P1-5A E1-12 P1-2B E1-14 P1-3B E1-15 P1-4B E1-16 P1-5B	E1-13		
Broadening Your Perspective		Exploring the Web		Financial Reporting Comparative Analysis Exploring the Web		All About You Comparative Analysis Decision Making Across the Organization Communication Activity Ethics Case

ANSWERS TO QUESTIONS

1. Yes, this is correct. Virtually every organization and person in our society uses accounting information. Businesses, investors, creditors, government agencies, and not-for-profit organizations must use accounting information to operate effectively.

2. Accounting is the process of identifying, recording, and communicating the economic events of an organization to interested users of the information. The first step of the accounting process is therefore to identify economic events that are relevant to a particular business. Once identified and measured, the events are recorded to provide a history of the financial activities of the organization. Recording consists of keeping a chronological diary of these measured events in an orderly and systematic manner. The information is communicated through the preparation and distribution of accounting reports, the most common of which are called financial statements. A vital element in the communication process is the accountant's ability and responsibility to analyze and interpret the reported information.

3. (a) Internal users are those who plan, organize, and run the business and therefore are officers and other decision makers.
(b) To assist management, accounting provides internal reports. Examples include financial comparisons of operating alternatives, projections of income from new sales campaigns, and forecasts of cash needs for the next year.

4. (a) Investors (owners) use accounting information to make decisions to buy, hold, or sell stock.
(b) Creditors use accounting information to evaluate the risks of granting credit or lending money.

5. Bookkeeping usually involves only the recording of economic events and therefore is just one part of the entire accounting process. Accounting, on the other hand, involves the entire process of identifying, recording, and communicating economic events.

6. Karen Sommers Travel Agency should report the land at $90,000 on its December 31, 2008 balance sheet. An important concept that accountants follow is the cost principle. The cost principle states that assets should be recorded at their cost. Cost has an important advantage over other valuations: it is reliable. Cost can be objectively measured and can be verified.

7. The monetary unit assumption requires that only transaction data capable of being expressed in terms of money be included in the accounting records. This assumption enables accounting to quantify (measure) economic events.

8. The economic entity assumption requires that the activities of the entity be kept separate and distinct from the activities of its owners and all other economic entities.

9. The three basic forms of business organizations are: (1) proprietorship, (2) partnership, and (3) corporation.

10. One of the advantages Maria Gonzalez would enjoy is that ownership of a corporation is represented by transferable shares of stock. This would allow Maria to raise money easily by selling a part of her ownership in the company. Another advantage is that because holders of the shares (stockholders) enjoy limited liability, they are not personally liable for the debts of the corporate entity. Also, because ownership can be transferred without dissolving the corporation, the corporation enjoys an unlimited life.

11. The basic accounting equation is Assets = Liabilities + Owner's Equity.

12. (a) Assets are resources owned by a business. Liabilities are claims against assets. Put more simply, liabilities are existing debts and obligations. Owner's equity is the ownership claim on total assets.
(b) Owner's equity is affected by owner's investments, drawings, revenues, and expenses.

13. The liabilities are: (b) Accounts payable and (g) Salaries payable.

14. Yes, a business can enter into a transaction in which only the left side of the accounting equation is affected. An example would be a transaction where an increase in one asset is offset by a decrease in another asset. An increase in the Equipment account which is offset by a decrease in the Cash account is a specific example.

15. Business transactions are the economic events of the enterprise recorded by accountants because they affect the basic equation.
(a) The death of the owner of the company is not a business transaction as it does not affect the basic equation.
(b) Supplies purchased on account is a business transaction as it affects the basic equation.
(c) An employee being fired is not a business transaction as it does not affect the basic equation.
(d) A withdrawal of cash from the business is a business transaction as it affects the basic equation.

16. (a) Decrease assets and decrease owner's equity.
(b) Increase assets and decrease assets.
(c) Increase assets and increase owner's equity.
(d) Decrease assets and decrease liabilities.

17. (a) Income statement.
(b) Balance sheet.
(c) Income statement.
(d) Balance sheet.
(e) Balance sheet and owner's equity statement.
(f) Balance sheet.

18. No, this treatment is not proper. While the transaction does involve a receipt of cash, it does not represent revenues. Revenues are the gross increase in owner's equity resulting from business activities entered into for the purpose of earning income. This transaction is simply an additional investment made by the owner in the business.

19. Yes. Net income does appear on the income statement—it is the result of subtracting expenses from revenues. In addition, net income appears in the statement of owner's equity—it is shown as an addition to the beginning-of-period capital. Indirectly, the net income of a company is also included in the balance sheet. It is included in the capital account which appears in the owner's equity section of the balance sheet.

20.	(a)	Ending capital balance	$198,000
		Beginning capital balance	168,000
		Net income	$ 30,000
	(b)	Ending capital balance	$198,000
		Beginning capital balance	168,000
			30,000
		Deduct: Investment	13,000
		Net income	$ 17,000
21.	(a)	Total revenues ($20,000 + $70,000)	$90,000
	(b)	Total expenses ($26,000 + $40,000)	$66,000
	(c)	Total revenues	$90,000
		Total expenses	66,000
		Net income	$24,000

SOLUTIONS TO BRIEF EXERCISES

BRIEF EXERCISE 1-1

(a) $90,000 – $50,000 = $40,000 (Owner's Equity).
(b) $40,000 + $70,000 = $110,000 (Assets).
(c) $94,000 – $60,000 = $34,000 (Liabilities).

BRIEF EXERCISE 1-2

(a) $120,000 + $232,000 = $352,000 (Total assets).
(b) $190,000 – $80,000 = $110,000 (Total liabilities).
(c) $800,000 – 0.5($800,000) = $400,000 (Owner's equity).

BRIEF EXERCISE 1-3

(a) ($800,000 + $150,000) – ($500,000 – $80,000) = $530,000 (Owner's equity).
(b) ($500,000 + $100,000) + ($800,000 – $500,000 – $70,000) = $830,000 (Assets).
(c) ($800,000 – $80,000) – ($800,000 – $500,000 + $120,000) = $300,000 (Liabilities).

BRIEF EXERCISE 1-4

A	(a)	Accounts receivable	A	(d)	Office supplies
L	(b)	Salaries payable	OE	(e)	Owner's investment
A	(c)	Equipment	L	(f)	Notes payable

BRIEF EXERCISE 1-5

	Assets	Liabilities	Owner's Equity
(a)	+	+	NE
(b)	+	NE	+
(c)	–	NE	–

BRIEF EXERCISE 1-6

	Assets	Liabilities	Owner's Equity
(a)	+	NE	+
(b)	–	NE	–
(c)	NE	NE	NE

BRIEF EXERCISE 1-7

E	(a)	Advertising expense	D	(e)	Bergman, Drawing
R	(b)	Commission revenue	R	(f)	Rent revenue
E	(c)	Insurance expense	E	(g)	Utilities expense
E	(d)	Salaries expense			

BRIEF EXERCISE 1-8

R	(a)	Received cash for services performed
NOE	(b)	Paid cash to purchase equipment
E	(c)	Paid employee salaries

BRIEF EXERCISE 1-9

LOPEZ COMPANY
Balance Sheet
December 31, 2008

Assets	
Cash	$ 49,000
Accounts receivable	72,500
Total assets	$121,500
Liabilities and Owner's Equity	
Liabilities	
Accounts payable	$ 90,000
Owner's equity	
Kim Lopez, Capital	31,500
Total liabilities and owner's equity	$121,500

BRIEF EXERCISE 1-10

BS	(a)	Notes payable
IS	(b)	Advertising expense
OE, BS	(c)	Trent Buchanan, Capital
BS	(d)	Cash
IS	(e)	Service revenue

SOLUTIONS TO EXERCISES

EXERCISE 1-1

C	Analyzing and interpreting information.
R	Classifying economic events.
C	Explaining uses, meaning, and limitations of data.
R	Keeping a systematic chronological diary of events.
R	Measuring events in dollars and cents.
C	Preparing accounting reports.
C	Reporting information in a standard format.
I	Selecting economic activities relevant to the company.
R	Summarizing economic events.

EXERCISE 1-2

(a) *Internal users*

Marketing manager
Production supervisor
Store manager
Vice-president of finance

External users

Customers
Internal Revenue Service
Labor unions
Securities and Exchange Commission
Suppliers

(b)

I	Can we afford to give our employees a pay raise?
E	Did the company earn a satisfactory income?
I	Do we need to borrow in the near future?
E	How does the company's profitability compare to other companies?
I	What does it cost us to manufacture each unit produced?
I	Which product should we emphasize?
E	Will the company be able to pay its short-term debts?

EXERCISE 1-3

Larry Smith, president of Smith Company, instructed Ron Rivera, the head of the accounting department, to report the company's land in their accounting reports at its market value of $170,000 instead of its cost of $100,000, in an effort to make the company appear to be a better investment. The cost principle requires that assets be recorded and reported at their cost, because cost is reliable and can be objectively measured and verified.

The stakeholders include stockholders and creditors of Smith Company, potential stockholders and creditors, other users of Smith's accounting reports, Larry Smith, and Ron Rivera. All users of Smith's accounting reports could be harmed by relying on information which violates accounting principles. Larry Smith could benefit if the company is able to attract more investors, but would be harmed if the fraudulent reporting is discovered. Similarly, Ron Rivera could benefit by pleasing his boss, but would be harmed if the fraudulent reporting is discovered.

Ron's alternatives are to report the land at $100,000 or to report it at $170,000. Reporting the land at $170,000 is not appropriate since it would mislead many people who rely on Smith's accounting reports to make financial decisions. Ron should report the land at its cost of $100,000. He should try to convince Larry Smith that this is the appropriate course of action, but be prepared to resign his position if Smith insists.

EXERCISE 1-4

1. **Incorrect. The *cost principle* requires that assets be recorded and reported at their cost.**

2. **Correct. The *monetary unit assumption* requires that companies include in the accounting records only transaction data that can be expressed in terms of money.**

3. **Incorrect. The *economic entity assumption* requires that the activities of the entity be kept separate and distinct from the activities of its owner and all other economic entities.**

EXERCISE 1-5

Asset	Liability	Owner's Equity
Cash	Accounts payable	Karin Meredith, Capital
Cleaning equipment	Notes payable	
Cleaning supplies	Salaries payable	
Accounts receivable		

EXERCISE 1-6

1. Increase in assets and increase in owner's equity.
2. Decrease in assets and decrease in owner's equity.
3. Increase in assets and increase in liabilities.
4. Increase in assets and increase in owner's equity.
5. Decrease in assets and decrease in owner's equity.
6. Increase in assets and decrease in assets.
7. Increase in liabilities and decrease in owner's equity.
8. Increase in assets and decrease in assets.
9. Increase in assets and increase in owner's equity.

EXERCISE 1-7

1.	(c)	5.	(d)
2.	(d)	6.	(b)
3.	(a)	7.	(e)
4.	(b)	8.	(f)

EXERCISE 1-8

(a) 1. Owner invested $15,000 cash in the business.
 2. Purchased office equipment for $5,000, paying $2,000 in cash and the balance of $3,000 on account.
 3. Paid $750 cash for supplies.
 4. Earned $8,300 in revenue, receiving $4,600 cash and $3,700 on account.
 5. Paid $1,500 cash on accounts payable.

EXERCISE 1-8 (Continued)

6. Owner withdrew $2,000 cash for personal use.
7. Paid $650 cash for rent.
8. Collected $450 cash from customers on account.
9. Paid salaries of $4,900.
10. Incurred $500 of utilities expense on account.

(b)	Investment	$15,000
	Service revenue	8,300
	Drawings	(2,000)
	Rent expense	(650)
	Salaries expense	(4,900)
	Utilities expense	(500)
	Increase in capital	$15,250

(c)	Service revenue	$8,300
	Rent expense	(650)
	Salaries expense	(4,900)
	Utilities expense	(500)
	Net income	$2,250

EXERCISE 1-9

S. MOSES & CO.
Income Statement
For the Month Ended August 31, 2008

Revenues		
Service revenue		$8,300
Expenses		
Salaries expense	$4,900	
Rent expense	650	
Utilities expense	500	
Total expenses		6,050
Net income		$2,250

EXERCISE 1-9 (Continued)

S. MOSES & CO.
Owner's Equity Statement
For the Month Ended August 31, 2008

S. Moses, Capital, August 1		$ 0
Add: Investments	$15,000	
Net income	2,250	17,250
		17,250
Less: Drawings		2,000
S. Moses, Capital, August 31		$15,250

S. MOSES & CO.
Balance Sheet
August 31, 2008

Assets	
Cash	$ 8,250
Accounts receivable	3,250
Supplies	750
Office equipment	5,000
Total assets	$17,250
Liabilities and Owner's Equity	
Liabilities	
Accounts payable	$ 2,000
Owner's equity	
S. Moses, Capital	15,250
Total liabilities and owner's equity	$17,250

EXERCISE 1-10

(a)	Owner's equity—12/31/07 ($400,000 – $250,000)	$150,000
	Owner's equity—1/1/07	100,000
	Increase in owner's equity	50,000
	Add: Drawings	15,000
	Net income for 2007	$ 65,000

EXERCISE 1-10 (Continued)

(b)	Owner's equity—12/31/08 ($460,000 – $300,000)	$160,000
	Owner's equity—1/1/08—see (a)	150,000
	Increase in owner's equity	10,000
	Less: Additional investment	50,000
	Net loss for 2008	$ 40,000

(c)	Owner's equity—12/31/09 ($590,000 – $400,000)	$190,000
	Owner's equity—1/1/09—see (b)	160,000
	Increase in owner's equity	30,000
	Less: Additional investment	15,000
		15,000
	Add: Drawings	30,000
	Net income for 2009	$ 45,000

EXERCISE 1-11

(a)	Total assets (beginning of year)		$95,000
	Total liabilities (beginning of year)		85,000
	Total owner's equity (beginning of year)		$10,000
(b)	Total owner's equity (end of year)		$40,000
	Total owner's equity (beginning of year)		10,000
	Increase in owner's equity		$30,000
	Total revenues		$215,000
	Total expenses		175,000
	Net income		$ 40,000
	Increase in owner's equity		$30,000
	Less: Net income	$(40,000)	
	Add: Drawings	24,000	(16,000)
	Additional investment		$14,000
(c)	Total assets (beginning of year)		$129,000
	Total owner's equity (beginning of year)		80,000
	Total liabilities (beginning of year)		$ 49,000

EXERCISE 1-11 (Continued)

(d)

Total owner's equity (end of year)		$130,000
Total owner's equity (beginning of year)		80,000
Increase in owner's equity		$ 50,000
Total revenues		$100,000
Total expenses		55,000
Net income		$ 45,000
Increase in owner's equity		$50,000
Less: Net income	$(45,000)	
Additional investment	(25,000)	(70,000)
Drawings		$20,000

EXERCISE 1-12

LINDA STANLEY CO.
Income Statement
For the Year Ended December 31, 2008

Revenues		
Service revenue		$62,500
Expenses		
Salaries expense	$30,000	
Rent expense	10,400	
Utilities expense	3,100	
Advertising expense	1,800	
Total expenses		45,300
Net income		$17,200

LINDA STANLEY CO.
Owner's Equity Statement
For the Year Ended December 31, 2008

Linda Stanley, Capital, January 1	$48,000
Add: Net income	17,200
	65,200
Less: Drawings	6,000
Linda Stanley, Capital, December 31	$59,200

EXERCISE 1-13

MENDEZ COMPANY
Balance Sheet
December 31, 2008

Assets	
Cash	$15,000
Accounts receivable	8,500
Supplies	8,000
Equipment	46,000
Total assets	$77,500
Liabilities and Owner's Equity	
Liabilities	
Accounts payable	$20,000
Owner's equity	
Mendez, Capital ($67,500 – $10,000)	57,500
Total liabilities and owner's equity	$77,500

EXERCISE 1-14

(a)

Camping fee revenues	$140,000
General store revenues	50,000
Total revenue	190,000
Expenses	150,000
Net income	$ 40,000

(b)

DEER PARK
Balance Sheet
December 31, 2008

Assets	
Cash	$ 23,000
Supplies	2,500
Equipment	105,500
Total assets	$131,000

EXERCISE 1-14 (Continued)

DEER PARK
Balance Sheet (Continued)
December 31, 2008

Liabilities and Owner's Equity	
Liabilities	
Notes payable	$ 60,000
Accounts payable	11,000
Total liabilities	71,000
Owner's equity	
Jan Nab, Capital ($131,000 – $71,000)	60,000
Total liabilities and owner's equity	$131,000

EXERCISE 1-15

SUMMERS CRUISE COMPANY
Income Statement
For the Year Ended December 31, 2008

Revenues		
Ticket revenue		$325,000
Expenses		
Salaries expense	$142,000	
Maintenance expense	95,000	
Property tax expense	10,000	
Advertising expense	3,500	
Total expenses		250,500
Net income		$ 74,500

EXERCISE 1-16

KEVIN JOHNSON, ATTORNEY
Owner's Equity Statement
For the Year Ended December 31, 2008

Kevin Johnson, Capital, January 1	$ 23,000	(a)
Add: Net income	139,000	(b)
	162,000	
Less: Drawings	79,000	
Kevin Johnson, Capital, December 31	$ 83,000	(c)

EXERCISE 1-16 (Continued)

Supporting Computations

(a)	Assets, January 1, 2008	$85,000
	Liabilities, January 1, 2008	62,000
	Capital, January 1, 2008	$23,000
(b)	Legal service revenue	$350,000
	Total expenses	211,000
	Net income	$139,000
(c)	Assets, December 31, 2008	$168,000
	Liabilities, December 31, 2008	85,000
	Capital, December 31, 2008	$ 83,000

SOLUTIONS TO PROBLEMS

PROBLEM 1-1A

(a)

BARONE REPAIR SHOP

	Cash	+	Accounts Receivable	+	Supplies	+	Equipment	=	Accounts Payable	+	N. Barone, Capital	
1.	+$10,000										+$10,000	Investment
	10,000							=			10,000	
2.	–5,000						+$5,000					
	5,000					+	5,000	=		+	10,000	
3.	–400										–400	Rent Expense
	4,600					+	5,000	=		+	9,600	
4.	–500				+$500							
	4,100			+	500	+	5,000	=		+	9,600	
5.									+$250		–250	Adv. Expense
	4,100			+	500	+	5,000	=	250	+	9,350	
6.	+5,100										+5,100	Service Revenue
	9,200			+	500	+	5,000	=	250	+	14,450	
7.	–1,000										–1,000	Drawings
	8,200			+	500	+	5,000	=	250	+	13,450	
8.	–2,000										–2,000	Salaries Expense
	6,200			+	500	+	5,000	=	250	+	11,450	
9.	–140										–140	Utilities Expense
	6,060			+	500	+	5,000	=	250	+	11,310	
10.			+$750								+750	Service Revenue
	6,060	+	750	+	500	+	5,000	=	250	+	12,060	
11.	+120		–120									
	$ 6,180	+	$630	+	$500	+	$5,000	=	$250	+	$12,060	

$\underbrace{\text{Cash} + \text{Accounts Receivable} + \text{Supplies} + \text{Equipment}}_{\$12,310} = \underbrace{\text{Accounts Payable} + \text{N. Barone, Capital}}_{\$12,310}$

PROBLEM 1-1A (Continued)

(b)

Ending capital		$12,060
Add: Drawings		1,000
		13,060
Deduct: Investments		10,000
Net income		$ 3,060

OR

Service revenue($5,100 + $750)		$5,850
Expenses		
Salaries	$2,000	
Rent	400	
Advertising	250	
Utilities	140	2,790
Net income		$3,060

PROBLEM 1-2A

(a)

MARIA GONZALEZ, VETERINARIAN

	Cash	+	Accounts Receivable	+	Supplies	+	Office Equipment	=	Notes Payable	+	Accounts Payable	+	M. Gonzalez, Capital	
Bal.	$ 9,000	+	$1,700	+	$600	+	$ 6,000	=			$3,600	+	$13,700	
1.	–2,900										–2,900			
	6,100	+	1,700	+	600	+	6,000	=			700	+	13,700	
2.	+1,300		–1,300											
	7,400	+	400	+	600	+	6,000	=			700	+	13,700	
3.	–800						+2,100				+1,300			
	6,600	+	400	+	600	+	8,100	=			2,000	+	13,700	
4.	+2,500		+5,500										+8,000	Serv. Revenue
	9,100	+	5,900	+	600	+	8,100	=			2,000	+	21,700	
5.	–1,000												–1,000	Drawings
	8,100	+	5,900	+	600	+	8,100	=			2,000	+	20,700	
													–1,700	Salaries Exp.
													–900	Rent Expense
6.	–2,900												–300	Adv. Expense
	5,200	+	5,900	+	600	+	8,100	=			2,000	+	17,800	
7.											+170		–170	Utilities Exp.
	5,200	+	5,900	+	600	+	8,100	=			2,170	+	17,630	
8.	+10,000								+$10,000					
	$15,200	+	$5,900	+	$600	+	$ 8,100	=	$10,000	+	$2,170	+	$17,630	

$29,800 = $29,800

PROBLEM 1-2A (Continued)

(b)

MARIA GONZALEZ, VETERINARIAN
Income Statement
For the Month Ended September 30, 2008

Revenues		
Service revenue		$8,000
Expenses		
Salaries expense	$1,700	
Rent expense	900	
Advertising expense	300	
Utilities expense	170	
Total expenses		3,070
Net income		$4,930

MARIA GONZALEZ, VETERINARIAN
Owner's Equity Statement
For the Month Ended September 30, 2008

M. Gonzalez, Capital, September 1	$13,700
Add: Net income	4,930
	18,630
Less: Drawings	1,000
M. Gonzalez, Capital, September 30	$17,630

MARIA GONZALEZ, VETERINARIAN
Balance Sheet
September 30, 2008

Assets

Cash	$15,200
Accounts receivable	5,900
Supplies	600
Office equipment	8,100
Total assets	$29,800

Liabilities and Owner's Equity

Liabilities	
Notes payable	$10,000
Accounts payable	2,170
Total liabilities	12,170
Owner's equity	
M. Gonzalez, Capital	17,630
Total liabilities and owner's equity	$29,800

PROBLEM 1-3A

(a)

SKYLINE FLYING SCHOOL
Income Statement
For the Month Ended May 31, 2008

Revenues		
Lesson revenue		$7,500
Expenses		
Fuel expense	$2,500	
Rent expense	1,200	
Advertising expense	500	
Insurance expense	400	
Repair expense	400	
Total expenses		5,000
Net income		$2,500

SKYLINE FLYING SCHOOL
Owner's Equity Statement
For the Month Ended May 31, 2008

Jeff Wilkins, Capital, May 1		$ 0
Add: Investments	$45,000	
Net income	2,500	47,500
		47,500
Less: Drawings		1,500
Jeff Wilkins, Capital, May 31		$46,000

SKYLINE FLYING SCHOOL
Balance Sheet
May 31, 2008

Assets	
Cash	$ 5,600
Accounts receivable	7,200
Equipment	64,000
Total assets	$76,800

PROBLEM 1-3A (Continued)

SKYLINE FLYING SCHOOL
Balance Sheet (Continued)
May 31, 2008

Liabilities and Owner's Equity	
Liabilities	
Notes payable	$30,000
Accounts payable	800
Total liabilities	30,800
Owner's equity	
Jeff Wilkins, Capital	46,000
Total liabilities and owner's equity	$76,800

(b)

SKYLINE FLYING SCHOOL
Income Statement
For the Month Ended May 31, 2008

Revenues		
Lesson revenue ($7,500 + $900)		$8,400
Expenses		
Fuel expense ($2,500 + $1,500)	$4,000	
Rent expense	1,200	
Advertising expense	500	
Insurance expense	400	
Repair expense	400	
Total expenses		6,500
Net income		$1,900

SKYLINE FLYING SCHOOL
Owner's Equity Statement
For the Month Ended May 31, 2008

Jeff Wilkins, Capital, May 1		$ 0
Add: Investments	$45,000	
Net income	1,900	46,900
		46,900
Less: Drawings		1,500
Jeff Wilkins, Capital, May 31		$45,400

PROBLEM 1-4A

(a)

MILLER DELIVERIES

	Assets				= Liabilities		+ Owner's Equity	
Date	Cash	+ Accounts Receivable	+ Supplies	+ Delivery Van	= Notes Payable	+ Accounts Payable	+ M. Miller, Capital	
June 1	$10,000						$10,000	Investment
2	(2,000)			$12,000	$10,000			
3	(500)						(500)	Rent Expense
5		$4,400					4,400	Service Revenue
9	(200)						(200)	Drawings
12			$150			$150		
15	1,250	(1,250)						
17						100	(100)	Gasoline Expense
20	1,500						1,500	Service Revenue
23	(500)				(500)			
26	(250)						(250)	Utilities Expense
29	(100)					(100)		
30	(1,000)						(1,000)	Salaries Expense
	$ 8,200	+ $3,150	+ $150	+ $12,000	= $ 9,500	+ $150	+ $13,850	

PROBLEM 1-4A (Continued)

(b)

MILLER DELIVERIES
Income Statement
For the Month Ended June 30, 2008

Revenues		
Service revenue ($4,400 + $1,500)		$5,900
Expenses		
Salaries expense	$1,000	
Rent expense	500	
Utilities expense	250	
Gasoline expense	100	
Total expenses		1,850
Net income		$4,050

(c)

MILLER DELIVERIES
Balance Sheet
June 30, 2008

Assets	
Cash	$ 8,200
Accounts receivable	3,150
Supplies	150
Delivery van	12,000
Total assets	$23,500
Liabilities and Owner's Equity	
Liabilities	
Notes payable	$ 9,500
Accounts payable	150
Total liabilities	9,650
Owner's equity	
M. Miller, Capital	13,850
Total liabilities and owner's equity	$23,500

PROBLEM 1-5A

(a)

Karma Company		Yates Company		McCain Company		Dench Company	
(a)	$ 45,000	(d)	$50,000	(g)	$120,000	(j)	$ 80,000
(b)	115,000	(e)	62,000	(h)	70,000	(k)	250,000
(c)	10,000	(f)	48,000	(i)	431,000	(l)	435,000

(b)

YATES COMPANY
Owner's Equity Statement
For the Year Ended December 31, 2008

Capital, January 1		$ 60,000
Add: Investment	$15,000	
Net income	35,000	50,000
		110,000
Less: Drawings		48,000
Capital, December 31		$ 62,000

(c) The sequence of preparing financial statements is income statement, owner's equity statement, and balance sheet. The interrelationship of the owner's equity statement to the other financial statements results from the fact that net income from the income statement is reported in the owner's equity statement and ending capital reported in the owner's equity statement is the amount reported for owner's equity on the balance sheet.

PROBLEM 1-1B

(a)

MATRIX TRAVEL AGENCY

	Cash	+	Accounts Receivable	+	Supplies	+	Office Equipment	=	Accounts Payable	+	Jenny Russo, Capital	
1.	+$10,000										+$10,000	Investment
	10,000							=			10,000	
2.	–400										–400	Rent Expense
	9,600							=			9,600	
3.	–2,500						+$2,500					
	7,100					+	2,500	=			9,600	
4.									+$300		–300	Adv. Expense
	7,100					+	2,500	=	300	+	9,300	
5.	–600				+$600							
	6,500			+	600	+	2,500	=	300	+	9,300	
6.	+3,000		+$6,500								+9,500	Serv. Revenue
	9,500	+	6,500	+	600	+	2,500	=	300	+	18,800	
7.	–200										–200	Drawings
	9,300	+	6,500	+	600	+	2,500	=	300	+	18,600	
8.	–300								–300			
	9,000	+	6,500	+	600	+	2,500	=	0		18,600	
9.	–2,200										–2,200	Salaries Exp.
	6,800	+	6,500	+	600	+	2,500	=			16,400	
10.	+4,000		–4,000									
	$10,800	+	$2,500	+	$600	+	$2,500	=	$ 0	+	$16,400	

$16,400 $16,400

PROBLEM 1-1B (Continued)

(b)

Ending capital	$16,400
Add: Drawings	200
	16,600
Deduct: Investments	10,000
Net income	$ 6,600

OR

Service revenue		$9,500
Expenses		
Salaries	$2,200	
Rent	400	
Advertising	300	2,900
Net income		$6,600

PROBLEM 1-2B

(a)

CINDY BELTON, ATTORNEY AT LAW

	Cash	+	Accounts Receivable	+	Supplies	+	Office Equipment	=	Notes Payable	+	Accounts Payable	+	Cindy Belton, Capital	
Bal.	$4,000	+	$1,500	+	$500	+	$5,000	=			$4,200	+	$ 6,800	
1.	+1,400		–1,400											
	5,400	+	100	+	500	+	5,000	=			4,200	+	6,800	
2.	–2,700										–2,700			
	2,700	+	100	+	500	+	5,000	=			1,500	+	6,800	
3.	+3,000		+6,000										+9,000	Service Revenue
	5,700	+	6,100	+	500	+	5,000	=			1,500	+	15,800	
4.	–400						+1,000				+600			
	5,300	+	6,100	+	500	+	6,000	=			2,100	+	15,800	
5.	–4,250												–3,000	Salaries Expense
													–900	Rent Expense
													–350	Advertising Expense
	1,050	+	6,100	+	500	+	6,000	=			2,100	+	11,550	
6.	–750												–750	Drawings
	300	+	6,100	+	500	+	6,000	=			2,100	+	10,800	
7.	+2,000								+$2,000					
	2,300	+	6,100	+	500	+	6,000	=	2,000	+	2,100	+	10,800	
8.											+250		–250	Utilities Expense
	$2,300	+	$6,100	+	$500	+	$6,000	=	$2,000	+	$2,350	+	$10,550	

$14,900 $14,900

PROBLEM 1-2B (Continued)

(b)

CINDY BELTON, ATTORNEY AT LAW
Income Statement
For the Month Ended August 31, 2008

Revenues		
Service revenue		$9,000
Expenses		
Salaries expense	$3,000	
Rent expense	900	
Advertising expense	350	
Utilities expense	250	
Total expenses		4,500
Net income		$4,500

CINDY BELTON, ATTORNEY AT LAW
Owner's Equity Statement
For the Month Ended August 31, 2008

Cindy Belton, Capital, August 1	$ 6,800
Add: Net income	4,500
	11,300
Less: Drawings	750
Cindy Belton, Capital, August 31	$10,550

PROBLEM 1-2B (Continued)

CINDY BELTON, ATTORNEY AT LAW
Balance Sheet
August 31, 2008

Assets

Cash	$ 2,300
Accounts receivable	6,100
Supplies	500
Office equipment	6,000
Total assets	$14,900

Liabilities and Owner's Equity

Liabilities	
Notes payable	$ 2,000
Accounts payable	2,350
Total liabilities	4,350
Owner's equity	
Cindy Belton, Capital	10,550
Total liabilities and owner's equity	$14,900

PROBLEM 1-3B

(a)

DIVINE COSMETICS CO.
Income Statement
For the Month Ended June 30, 2008

Revenues		
Service revenue		$6,000
Expenses		
Supplies expense	$1,600	
Gas and oil expense	800	
Advertising expense	500	
Utilities expense	300	
Total expenses		3,200
Net income		$2,800

DIVINE COSMETICS CO.
Owner's Equity Statement
For the Month Ended June 30, 2008

Michelle Bullock, Capital, June 1		$ 0
Add: Investments	$26,200	
Net income	2,800	29,000
		29,000
Less: Drawings		1,200
Michelle Bullock, Capital, June 30		$27,800

DIVINE COSMETICS CO.
Balance Sheet
June 30, 2008

Assets

Cash	$11,000
Accounts receivable	4,000
Cosmetic supplies	2,000
Equipment	25,000
Total assets	$42,000

DIVINE COSMETICS CO.
Balance Sheet (Continued)
June 30, 2008

Liabilities and Owner's Equity

Liabilities	
Notes payable	$13,000
Accounts payable	1,200
Total liabilities	14,200
Owner's equity	
Michelle Bullock, Capital	27,800
Total liabilities and owner's equity	$42,000

(b)

DIVINE COSMETICS CO.
Income Statement
For the Month Ended June 30, 2008

Revenues		
Service revenue ($6,000 + $800)		$6,800
Expenses		
Supplies expense	$1,600	
Gas and oil expense ($800 + $100)	900	
Advertising expense	500	
Utilities expense	300	
Total expenses		3,300
Net income		$3,500

DIVINE COSMETICS CO.
Owner's Equity Statement
For the Month Ended June 30, 2008

Michelle Bullock, Capital, June 1		$ 0
Add: Investments	$26,200	
Net income	3,500	29,700
		29,700
Less: Drawings		1,200
Michelle Bullock, Capital, June 30		$28,500

PROBLEM 1-4B

(a)

GELLER CONSULTING

	Assets				=	Liabilities		+	Owner's Equity	
Date	Cash	+ Accounts Receivable	+ Supplies	+ Office Equipment	=	Notes Payable	+ Accounts Payable	+	L. Geller, Capital	
May 1	$ 8,000								$ 8,000	Investment
2	(800)								(800)	Rent Expense
3			$500				$ 500			
5	(50)								(50)	Advertising Expense
9	3,000								3,000	Service Revenue
12	(700)								(700)	Drawings
15		$5,300							5,300	Service Revenue
17	(3,000)								(3,000)	Salaries Expense
20	(500)						(500)			
23	3,000	(3,000)								
26	5,000					$5,000				
29				$2,800			2,800			
30	(150)								(150)	Utilities Expense
	$13,800	+ $2,300	+ $500	+ $2,800	=	$5,000	+ $2,800	+	$11,600	

PROBLEM 1-4B (Continued)

(b)

GELLER CONSULTING
Income Statement
For the Month Ended May 31, 2008

Revenues		
Service revenue ($3,000 + $5,300)		$8,300
Expenses		
Salaries expense	$3,000	
Rent expense	800	
Utilities expense	150	
Advertising expense	50	
Total expenses		4,000
Net income		$4,300

(c)

GELLER CONSULTING
Balance Sheet
May 31, 2008

Assets	
Cash	$13,800
Accounts receivable	2,300
Supplies	500
Office equipment	2,800
Total assets	$19,400
Liabilities and Owner's Equity	
Liabilities	
Notes payable	$ 5,000
Accounts payable	2,800
Total liabilities	7,800
Owner's equity	
L. Geller, Capital	11,600
Total liabilities and owner's equity	$19,400

PROBLEM 1-5B

(a)

McKane Company		Selara Company		Gordon Company		Hindi Company	
(a)	$30,000	(d)	$40,000	(g)	$124,000	(j)	$ 50,000
(b)	95,000	(e)	45,000	(h)	80,000	(k)	225,000
(c)	5,000	(f)	28,000	(i)	413,000	(l)	460,000

(b)

McKANE COMPANY
Owner's Equity Statement
For the Year Ended December 31, 2008

Capital, January 1		$30,000
Add: Investment	$ 5,000	
Net income	15,000	20,000
		50,000
Less: Drawings		10,000
Capital, December 31		$40,000

(c) The sequence of preparing financial statements is income statement, owner's equity statement, and balance sheet. The interrelationship of the owner's equity statement to the other financial statements results from the fact that net income from the income statement is reported in the owner's equity statement and ending capital reported in the owner's equity statement is the amount reported for owner's equity on the balance sheet.

BYP 1-1 FINANCIAL REPORTING PROBLEM

(a) PepsiCo's total assets at December 31, 2005 were $31,727 million and at December 25, 2004 were $27,987 million.

(b) PepsiCo had $1,716 million of cash and cash equivalents at December 31, 2005.

(c) PepsiCo had accounts payable (and other current liabilities) totaling $5,971 million on December 31, 2005 and $5,599 million on December 25, 2004.

(d) PepsiCo reports net sales for three consecutive years as follows:

2003	$26,971 million
2004	$29,261 million
2005	$32,562 million

(e) From 2004 to 2005, PepsiCo's net income decreased $134 million from $4,212 million to $4,078 million.

BYP 1-2 COMPARATIVE ANALYSIS PROBLEM

(a)

(in millions)	PepsiCo	Coca-Cola
1. Total assets	$31,727	$29,427
2. Accounts receivable (net)	$ 3,261	$ 2,281
3. Net sales	$32,562	$23,104
4. Net income	$ 4,078	$ 4,872

(b) PepsiCo's total assets were approximately 8% greater than Coca-Cola's total assets, and PepsiCo's net sales were 41% greater than Coca-Cola's net sales. In addition, PepsiCo's accounts receivable were 43% greater than Coca-Cola's and represent 10% of its net sales. Coca-Cola's accounts receivable amount to 9.9% of its net sales. Both PepsiCo's and Coca-Cola's accounts receivable are at satisfactory levels, being comparable to a 30-day collection period.

Coca-Cola's net income was 119.5% of PepsiCo's. It appears that these two companies' operations are comparable in some ways, with Coca-Cola's operations slightly more profitable.

BYP 1-3 EXPLORING THE WEB

(a) The field is normally divided into three broad areas: auditing, financial/tax, and management accounting.

(b) The skills required in these areas:

People skills, sales skills, communication skills, analytical skills, ability to synthesize, creative ability, initiative, computer skills.

(c) The skills required in these areas differ as follows:

	Auditing	Financial and Tax	Management Accounting
People skills	Medium	Medium	Medium
Sales skills	Medium	Medium	Low
Communication skills	Medium	Medium	High
Analytical skills	High	Very High	High
Ability to synthesize	Medium	Low	High
Creative ability	Low	Medium	Medium
Initiative	Medium	Medium	Medium
Computer skills	High	High	Very High

(d) Some key job functions in accounting:

Auditing: Work in audit involves checking accounting ledgers and financial statements within corporations and government. This work is becoming increasingly computerized and can rely on sophisticated random sampling methods. Audit is the bread-and-butter work of accounting. This work can involve significant travel and allows you to really understand how money is being made in the company that you are analyzing. It’s great background!

Budget Analysis: Budget analysts are responsible for developing and managing an organization’s financial plans. There are plentiful jobs in this area in government and private industry. Besides quantitative skills many budget analyst jobs require good people skills because of negotiations involved in the work.

BYP 1-3 (Continued)

Financial: Financial accountants prepare financial statements based on general ledgers and participate in important financial decisions involving mergers and acquisitions, benefits/ERISA planning, and long-term financial projections. This work can be varied over time. One day you may be running spreadsheets. The next day you may be visiting a customer or supplier to set up a new account and discuss business. This work requires a good understanding of both accounting and finance.

Management Accounting: Management accountants work in companies and participate in decisions about capital budgeting and line of business analysis. Major functions include cost analysis, analysis of new contracts, and participation in efforts to control expenses efficiently. This work often involves the analysis of the structure of organizations. Is responsibility to spend money in a company at the right level of our organization? Are goals and objectives to control costs being communicated effectively? Historically, many management accountants have been derided as "bean counters." This mentality has undergone major change as management accountants now often work side by side with marketing and finance to develop new business.

Tax: Tax accountants prepare corporate and personal income tax statements and formulate tax strategies involving issues such as financial choice, how to best treat a merger or acquisition, deferral of taxes, when to expense items and the like. This work requires a thorough understanding of economics and the tax code. Increasingly, large corporations are looking for persons with both an accounting and a legal background in tax. A person, for example, with a JD and a CPA would be especially desirable to many firms.

(e) Junior Staff Accountant $36-63,000

BYP 1-4 DECISION MAKING ACROSS THE ORGANIZATION

(a) **The estimate of the $6,100 loss was based on the difference between the $25,000 invested in the driving range and the bank balance of $18,900 at March 31. This is not a valid basis for determining income because it only shows the change in cash between two points in time.**

(b) **The balance sheet at March 31 is as follows:**

CHIP-SHOT DRIVING RANGE
Balance Sheet
March 31, 2008

Assets	
Cash	$18,900
Caddy shack	8,000
Equipment	800
Total assets	$27,700
Liabilities and Owner's Equity	
Liabilities	
Accounts payable ($150 + $100)	$ 250
Owner's equity	
Mary and Jack Gray, Capital	27,450
Total liabilities and owner's equity	$27,700

As shown in the balance sheet, the owner's capital at March 31 is $27,450. The estimate of $2,450 of net income is the difference between the initial investment of $25,000 and $27,450. This was not a valid basis for determining net income because changes in owner's equity between two points in time may have been caused by factors unrelated to net income. For example, there may be drawings and/or additional capital investments by the owner(s).

BYP 1-4 (Continued)

(c) **Actual net income for March can be determined by adding owner's drawings to the change in owner's capital during the month as shown below:**

Owner's capital, March 31, per balance sheet	$27,450
Owner's capital, March 1	25,000
Increase in owner's capital	2,450
Add: Drawings	1,000
Net income	$ 3,450

Alternatively, net income can be found by determining the revenues earned [described in (d) below] and subtracting expenses.

(d) **Revenues earned can be determined by adding expenses incurred during the month to net income. March expenses were Rent, $1,000; Wages, $400; Advertising, $750; and Utilities, $100 for a total of $2,250. Revenues earned, therefore, were $5,700 ($2,250 + $3,450). Alternatively, since all revenues are received in cash, revenues earned can be computed from an analysis of the changes in cash as follows:**

Beginning cash balance		$25,000
Less: Cash payments		
Caddy shack	$8,000	
Golf balls and clubs	800	
Rent	1,000	
Advertising	600	
Wages	400	
Drawings	1,000	11,800
Cash balance before revenues		13,200
Cash balance, March 31		18,900
Revenues earned		$ 5,700

BYP 1-5 COMMUNICATION ACTIVITY

To: Lynn Benedict
From: Student

I have received the balance sheet of New York Company as of December 31, 2008. A number of items in this balance sheet are not properly reported. They are:

1. The balance sheet should be dated as of a specific date, not for a period of time. Therefore, it should be dated "December 31, 2008."

2. Equipment should be shown as an asset and reported below Supplies on the balance sheet.

3. Accounts receivable should be shown as an asset, not a liability, and reported between Cash and Supplies on the balance sheet.

4. Accounts payable should be shown as a liability, not an asset. The note payable is also a liability and should be reported in the liability section.

5. Liabilities <u>and</u> owner's equity should be shown on the balance sheet. Don Wenger, Capital and Don Wenger, Drawing are not liabilities.

6. Don Wenger, Capital and Don Wenger, Drawing are part of owner's equity. The Drawing account is not reported on the balance sheet but is subtracted from Don Wenger, Capital to arrive at owner's equity at the end of the period.

BYP 1-5 (Continued)

A correct balance sheet is as follows:

NEW YORK COMPANY
Balance Sheet
December 31, 2008

Assets	
Cash	$ 9,000
Accounts receivable	6,000
Supplies	2,000
Equipment	25,500
	$42,500
Liabilities and Owner's Equity	
Liabilities	
Notes payable	$10,500
Accounts payable	8,000
Total liabilities	18,500
Owner's equity	
Don Wenger, Capital ($26,000 – $2,000)	24,000
Total liabilities and owner's equity	$42,500

BYP 1-6 ETHICS CASE

(a) The students should identify all of the stakeholders in the case; that is, all the parties that are affected, either beneficially or negatively, by the action or decision described in the case. The list of stakeholders in this case are:

- Steve Baden, interviewee.
- Both Baltimore firms.
- Great Northern College.

(b) The students should identify the ethical issues, dilemmas, or other considerations pertinent to the situation described in the case. In this case the ethical issues are:

- Is it proper that Steve charged both firms for the total travel costs rather than split the actual amount of $296 between the two firms?

- Is collecting $592 as reimbursement for total costs of $296 ethical behavior?

- Did Steve deceive both firms or neither firm?

(c) Each student must answer the question for himself/herself. Would you want to start your first job having deceived your employer before your first day of work? Would you be embarrassed if either firm found out that you double-charged? Would your school be embarrassed if your act was uncovered? Would you be proud to tell your professor that you collected your expenses twice?

BYP 1-7 ALL ABOUT YOU: THE ETHICS OF FINANCIAL AID

(a) Answers to the following will vary depending on students' opinions.

(1) This does not represent the hiding of assets, but rather a choice as to the order of use of assets. This would seem to be ethical.
(2) This does not represent the hiding of assets, but rather is a change in the nature of assets. Since the expenditure was necessary, although perhaps accelerated, it would seem to be ethical.
(3) This represents an intentional attempt to deceive the financial aid office. It would therefore appear to be both unethical and potentially illegal.
(4) This is a difficult issue. By taking the leave, actual net income would be reduced. The form asks the applicant to report actual net income. However, it is potentially deceptive since you do not intend on taking unpaid absences in the future, thus future income would be higher than reported income.

(b) Companies might want to overstate net income in order to potentially increase the stock price by improving investors' perceptions of the company. Also, a higher net income would make it easier to receive debt financing. Finally, managers would want a higher net income to increase the size of their bonuses.

(c) Sometimes companies want to report a lower income if they are negotiating with employees. For example, professional sports teams frequently argue that they can not increase salaries because they aren't making enough money. This also occurs in negotiations with unions. For tax accounting (as opposed to the financial accounting in this course) companies frequently try to minimize the amount of reported taxable income.

(d) Unfortunately many times people who are otherwise very ethical will make unethical decisions regarding financial reporting. They might be driven to do this because of greed. Frequently it is because their superiors have put pressure on them to take an unethical action, and they are afraid to not follow directions because they might lose their job. Also, in some instances top managers will tell subordinates that they should be a team player, and do the action because it would help the company, and therefore would help fellow employees.