

SOLUTION MANUAL
Financial Accounting
Valix and Peralta
Volume Three - 2008 Edition

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CHAPTER 1

Problem 1-1
Problem 1-3

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

Problem 1-2

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

1. C
2. C
3. C
4. A
5. D
6. D
7. D
8. C
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Problem 1-4
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1. C
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Problem 1-5

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2. A
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Problem 1-

1. D
2. C
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CHAPTER 2

Problem 2-1

Problem 2-3

1. C
2. A
3. D
4. A
5. C
6. D
7. B
8. A
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Problem 2-2

1. C
2. B
3. D
4. A
5. C

1. D
2. D
3. C
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6. D
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Problem 2-4

1. C
2. A
3. A
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6. F
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Problem 2-5

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

Problem 2-6

1. Noncurrent asset as part of intangible assets
2. Other noncurrent asset
3. Addition to bonds payable under noncurrent liability
4. Noncurrent asset as part of property, plant and equipment but with disclosure that the building construction is in progress.
5. Noncurrent asset as part of intangible assets
6. Deduction from shareholders' equity
7. Deduction from shareholders' equity
8. Current asset
9. Current liability
10. Deduction from property, plant and equipment
11. Current liability
12. Shareholders' equity as part of reserves
13. Noncurrent asset as part of property, plant and equipment
14. Noncurrent asset as part of property, plant and equipment
15. Deduction from beginning balance of retained earnings

Problem 2-7 Answer A

Accounts receivable	200,000
Trading securities	100,000
Cash and cash equivalents	150,000
Inventory	500,000
Prepaid expenses	<u>20,000</u>
	<u>970,000</u>

Problem 2-8 Answer B

Cash and cash equivalent	700,000
Trade and other receivables (1,200,000 minus 260,000)	940,000
Inventories (600,000 + 200,000)	<u>800,000</u>
Total current assets	<u>2,440,000</u>

Adjustments

1. Sales	260,000	
Accounts receivable		260,000
2. Inventory (260,000/130%)	200,000	
Cost of goods sold		200,000

Problem 2-9 Answer C

Cash (1,500,000 - 500,000)	1,000,000
Trade and other receivables	3,000,000
Inventory (2,000 000 - 200,000)	<u>1,800,000</u>
Total current assets	<u>5,800,000</u>

Problem 2-10 Answer B

Cash and cash equivalents	1,800,000
Trade and other receivables	1,150,000
Inventories	1,700,000
Prepaid expenses	<u>200,000</u>
Total current assets	<u>4,850,000</u>
Customers' accounts	1,050,000
Allowance for uncollectible accounts	(50,000)

Employees' account, current	<u>150,000</u>
Total trade and other receivables	
	<u>1,150,000</u>

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Problem 2-11 Answer A

Cash	200,000
Accounts receivable	350,000
Inventory	580,000
Prepaid expenses	120,000
Land classified as held for sale	<u>1,000,000</u>
Total current assets	<u>2,250,000</u>

The undelivered checks amounting to P300,000 should be adjusted by reversing the original entry as follows:

Cash	300,000	
Accounts payable		300,000

Accordingly, the adjusted cash balance is P200,000 (P300,000 minus the overdraft of P100,000).

Under PFRS 5, a noncurrent asset classified as "held for sale" is presented as current asset.

Problem 2-12 Answer A

Cash and cash equivalents	
209,000	
Trading securities	143,000
Trade receivables	853,000
Merchandise inventory	796,000
Prepaid expenses	<u>10,000</u>
Total current assets	<u>2,011,000</u>
Accounts receivable (808,000 + 40,000)	
848,000	
Notes receivable	100,000
Note receivable discounted	(80,000)
Allowance for doubtful accounts	<u>(15,000)</u>
Total trade receivables	<u>853,000</u>

Problem 2-13 Answer B

Cash	2,000,000
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Notes receivable	1,200,000
Note receivable discounted	(700,000)
Accounts receivable - unassigned	3,000,000
Accounts receivable - assigned	800,000
Allowance for doubtful accounts	(100,000)
Inventory (2,800,000 - 600,000)	<u>2,200,000</u>
Total current assets	<u>8,400,000</u>

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The equity of the **assignee** in assigned accounts should not be offset against the assigned accounts receivable but should be included in current liabilities.

Problem 2-14 Answer A

Current assets per book	7,300,000
Bank overdraft	300,000
Cash set aside from plant site	(2,000,000)
Goods held on consignment	(150,000)
Cash surrender value	(<u>50,000</u>)
Adjusted current assets	<u>5,400,000</u>

The bank overdraft should not be “netted” against the cash in bank but should be classified as current liability. The **writeoff** of the accounts receivable has no effect on current assets.

Problem 2-15 Answer C

Accounts payable	1,900,000
Dividends payable	500,000
Income tax payable	900,000
Note payable	<u>600,000</u>
Total current liabilities	<u>3,900,000</u>

Under PAS 1 and PAS 12, a deferred tax liability is classified as **noncurrent**.

Problem 2-16 Answer A

Accounts payable (4,000,000 + 100,000)	
4,100,000	Accrued expenses
1,500,000	
Credit balances in customers' accounts	
500,000	
Estimated liability for coupons	<u>600,000</u>
Total current liabilities	<u>6,700,000</u>

Problem 2-17 Answer C

Accounts payable	5,000,000
Bonds payable	10,000,000
Premium on bonds payable	500,000
Dividends payable	4,500,000
Income tax payable	1,500,000
Note payable - bank	<u>4,000,000</u>
Total current liabilities	<u>25,500,000</u>

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Problem 2-18 Answer D

The 10% note payable is classified as **noncurrent**. PAS 1, paragraph 64, provides that if an entity has the discretion to refinance or roll over an obligation for at least twelve months after the balance sheet date under an existing loan facility, the obligation shall be classified as **noncurrent**, even if it would otherwise be due within a shorter period.

The 12% note payable is also classified as **noncurrent**. PAS 1, paragraph 67, provides that if the refinancing occurs **between** the balance sheet date and date of issue of the statements, the refinancing is a **nonadjusting event**, meaning, the obligation is classified as **current**.

However, if the refinancing occurs **on or before** the balance sheet date, the refinancing is an **adjusting event**, meaning, the obligation is classified as **noncurrent** liability. In this case, the 12% note payable is refinanced on **December 31, 2008**.

Problem 2-19 Answer A

Accounts payable	6,500,000
Bank note payable - 10%	3,000,000
Interest payable	150,000
Mortgage note payable	2,000,000
Bonds payable - due June 30, 2009	
<u>4,000,000</u>	
Total current liabilities	<u>15,650,000</u>

The 11% bank note payable is refinanced on balance sheet date, **December 31, 2008**. PAS 1, paragraph 12, provides that if an obligation is refinanced on a long-term basis **on or before** balance sheet date, the refinancing qualifies as an adjusting event. Therefore, the 11% bank note payable is classified as **noncurrent**.

Problem 2-20 Answer C

Per book	1,500,000
Purchase return	(45,000)
Advances from customer	<u>75,000</u>
Total current liabilities	<u>1,530,000</u>

The adjustments on December 31, 2007 are:

* Accounts payable	45,000	
Purchase returns		45,000
* Accounts receivable	75,000	
Advances from customer		75,000
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Problem 2-21 Answer C

Share capital	
5,000,000	
Retained earnings	1,000,000
Treasury shares	(750,000)
Adjusted shareholders' equity	<u>5,250,000</u>

Problem 2-22 Answer A

Net assets per book	
8,750,000	
Treasury stock	(250,000)
Adjusted net assets	<u>8,500,000</u>

Problem 2-23 Answer C

Retained earnings, January 1	550,000	Preference share	450,000
Income summary - net income	500,000	Ordinary share	1,000,000
Dividends - ordinary and preference	(250,000)	Share premium	250,000
Retained earnings, December 31	<u>800,000</u>	RE	<u>800,000</u>
		Total SE	<u>2,500,000</u>

Problem 2-24 Answer A

Problem 2-25

Question 1 - Answer C

Cash	5,000,000
Accounts receivable (8,000,000 - 2,000,000)	6,000,000

Inventory	
<u>6,000,000</u>	
Total current assets	<u>17,000,000</u>

Question 2 - Answer B

Income before tax	5,000,000
Income tax (35% x 5,000,000)	<u>(1,750,000)</u>
Net income	3,250,000
Retained earnings - January 1	<u>5,000,000</u>
Total	<u>8,250,000</u>

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Problem 2-26

Question 1 - Answer B

Earnings from long term contract	
6,680,000	
Costs and expenses	
<u>5,180,000</u>	
Income before income tax	
1,500,000	
Less: Income tax (35% x 1,500,000)	
<u>525,000</u>	
Net income	975,000
Retained earnings unappropriated	900,000
Retained earnings restricted	<u>160,000</u>
Total retained earnings	<u>2,035,000</u>

Question 2 - Answer A

Note payable - noncurrent	<u>1,620,000</u>
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The "billings in excess of cost on long term contracts account" is a current liability.

PAS 11 requires that an entity shall present the **gross amount** due from customers for contract work as an asset, and the **gross amount** due to customers for contract work as a liability.

Question 3 - Answer C

Cash	600,000
Accounts receivable	3,500,000
Cost in excess of billings	<u>1,600,000</u>

Total current assets	<u>5,700,000</u>
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The prepaid taxes of P525,000 actually represent the current tax expense for 2008 and therefore should be charged to income tax expense.

Problem 2-27 Answer C

Liabilities	900,000
Share capital	
5,000,000	
Retained earnings (Net income of P1,000,000 minus cash dividend of P200,000)	
<u>800,000</u>	
Total liabilities and equity	<u>6,700,000</u>

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Problem 2-28 Answer B

Problem 2-29 Answer A

Litigation loss	
3,000,000	
Bad debt expense (3,500,000 x 90%)	<u>3,150,000</u>
Total amount of adjusting events	
<u>6,150,000</u>	

The receivable of P400,000 is nonadjusting event because the amount is still collectible although a longer term has been given but not so long as to cause it to be reclassified as noncurrent.

The investments in trading securities are measured at fair value **which must be determined on balance sheet date**. The change in the fair value on February 15, 2009 shall be recognized in the next reporting period, not on December 31, 2008.

Problem 2-30

**Easy Company
Balance sheet
December 31, 2008**

A S S E T S

Current assets:	Note
Cash and cash equivalents	
800,000	
Accounts receivable	450,000
Inventories	900,000

Prepaid expenses	(1)	<u>200,000</u>
Total current assets		2,350,000
Noncurrent assets:		
Property, plant and equipment	(2)	4,400,000
Long-term investments		950,000
Intangible asset	(3)	<u>800,000</u>
Total noncurrent assets		<u>6,150,000</u>
Total assets		<u>8,500,000</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Trade and other payables	(4)	450,000
Note payable, short-term debt		<u>200,000</u>
Total current liabilities		650,000
Noncurrent liabilities:		
Mortgage payable, due in 5 years		1,500,000
Note payable, long-term debt		<u>500,000</u>
Total noncurrent liabilities		2,000,000
Shareholders' equity:		
Share capital, P100 par		4,000,000
Share premium		500,000
Retained earnings		<u>1,350,000</u>
Total shareholders' equity		<u>5,850,000</u>
Total liabilities and stockholders' equity		<u>8,500,000</u>

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Note 1 - Prepaid expenses

Office supplies	50,000
Prepaid rent	<u>150,000</u>
Total prepaid expenses	<u>200,000</u>

Note 2 - Property, plant and equipment

Property, plant and equipment	5,600,000
Accumulated depreciation	<u>(1,200,000)</u>
Net book value	<u>4,400,000</u>

Note 3 - Intangible asset

Patent	<u>800,000</u>
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Note 4 - Trade and other payables

Accounts payable	350,000
Accrued expenses	<u>100,000</u>
Total	<u>450,000</u>

Problem 2-31

**Simple Company
Balance sheet
December 31, 2008**

A S S E T S

	Note	
Current assets:		
Cash		420,000
Trading securities		250,000
Trade and other receivables	(1)	620,000
Inventories	(2)	1,250,000
Prepaid expenses	(3)	<u>20,000</u>
Total current assets		2,560,000
Noncurrent assets:		
Property, plant and equipment	(4)	4,640,000
Long-term investments	(5)	2,000,000
Intangible assets	(6)	<u>300,000</u>
Total noncurrent assets		<u>6,940,000</u>
Total assets		<u>9,500,000</u>

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LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:	Note	
Trade and other payables	(7)	620,000
Serial bonds payable - current portion		<u>500,000</u>
Total current liabilities		1,120,000
Noncurrent liabilities:		
Serial bonds payable - remaining portion		2,000,000
Shareholders' equity:		
Share capital		5,000,000
Share premium		500,000
Retained earnings		<u>880,000</u>
Total shareholders' equity		<u>6,380,000</u>
Total liabilities and shareholders' equity		<u>9,500,000</u>

Note 1 - Trade and other receivables

Accounts receivable	500,000
Allowance for doubtful accounts	(50,000)
Notes receivable	150,000
Claim receivable	<u>20,000</u>
Total	<u>620,000</u>

Note 2 - Inventories

Finished goods	400,000
Goods in process	600,000
Raw materials	200,000
Factory supplies	<u>50,000</u>
Total	<u>1,250,000</u>

Note 3 - Prepaid expenses

Prepaid insurance	<u>20,000</u>
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Note 4 - Property, plant and equipment

	Cost	Accum. depr.	Book value
Land	1,500,000	-	1,500,000
Building	4,000,000	1,600,000	2,400,000
Machinery	2,000,000	1,300,000	700,000
Tools	<u>40,000</u>	<u>-</u>	
<u>40,000</u>			
Total	<u>7,540,000</u>	<u>2,900,000</u>	
<u>4,640,000</u>			

12**Note 5 - Long-term investments**

Investment in bonds	1,500,000	
Plant expansion fund		<u>500,000</u>
Total		<u>2,000,000</u>

Note 6 - Intangible assets

Franchise	200,000
Goodwill	
<u>100,000</u>	

Total
300,000

Note 7 - Trade and other payables

Accounts payable
 300,000
 Notes payable
 100,000
 Income tax payable
 60,000
 Advances from customers
 100,000
 Accrued expenses
 30,000
 Accrued interest on note payable
 10,000
 Employees income tax payable
20,000
 Total
620,000

Problem 2-32

**Exemplar Company
 Balance sheet
 December 31, 2008**

A S S E T S

	Note	
Current assets:		
Cash and cash equivalents		500,000
Trading securities		280,000
Trade and other receivables	(1)	640,000
Inventories		
1,300,000		
Prepaid expenses		<u>70,000</u>
Total current assets		2,790,000
Noncurrent assets:		
Property, plant and equipment	(2)	5,300,000
Long-term investments	(3)	1,310,000
Intangible assets	(4)	3,350,000
Other noncurrent assets	(5)	<u>150,000</u>
Total noncurrent assets		<u>10,110,000</u>
Total assets		<u>12,900,000</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:	Note	
Trade and other payables	(6)	
1,000,000		
Noncurrent liabilities:		
Bonds payable		5,000,000
Premium on bonds payable		
<u>1,000,000</u>		
Total noncurrent liabilities		
6,000,000		
Shareholders' equity:		
Share capital	(7)	
7,000,000		
Reserves	(8)	
700,000		
Retained earnings (deficit)		(1,800,000)
Total shareholders' equity		<u>(1,800,000)</u>
<u>5,900,000</u>		
Total liabilities and shareholders' equity		<u>12,900,000</u>

Note 1 - Trade and other receivables

Accounts receivable	
400,000	
Allowance for doubtful accounts	
(20,000)	
Notes receivable	250,000
Accrued interest on notes receivable	<u>10,000</u>
Total	<u>640,000</u>

Note 2 - Property, plant and equipment

	Cost	Accum. depr.	Book
value			
Land	1,500,000	-	1,500,000
Building	5,000,000	2,000,000	3,000,000
Equipment	<u>1,000,000</u>	<u>200,000</u>	<u>800,000</u>
Total	<u>7,500,000</u>	<u>2,200,000</u>	<u>5,300,000</u>

Note 3 - Long-term investments

Land held for speculation	500,000
Sinking fund	400,000
Preference share redemption fund	350,000
Cash surrender value	<u>60,000</u>
Total	<u>1,310,000</u>

Note 4 - Intangible assets

Computer software	3,250,000
Lease rights	<u>100,000</u>
Total	<u>3,350,000</u>

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Note 5 - Other noncurrent assets

Advances to officers, not collectible currently	100,000
Long-term refundable deposit	<u>50,000</u>
Total	<u>150,000</u>

Note 6 - Trade and other payables

Accounts payable	400,000
Notes payable	300,000
Unearned rent income	40,000
SSS payable	10,000
Accrued salaries	100,000
Dividends payable	120,000
Withholding tax payable	<u>30,000</u>
Total	<u>1,000,000</u>

Note 7 - Share capital

Preference share capital	2,000,000
Ordinary share capital	<u>5,000,000</u>
Total	<u>7,000,000</u>

Note 8 - Reserves

Share premium – preference	500,000
Share premium – ordinary	<u>200,000</u>
Total	<u>700,000</u>

Problem 2-33

**Relax Company
Balance Sheet
December 31, 2008**

A S S E T S

Current assets:	Note	
Cash		400,000
Trade accounts receivable	(1)	750,000
Inventories		1,000,000
Prepaid expenses		<u>100,000</u>
Total current assets		2,250,000
Noncurrent assets:		
Property, plant and equipment	(2)	5,600,000
Investment in associate		1,300,000

Intangible assets	(3)	<u>350,000</u>
Total noncurrent assets		<u>7,250,000</u>
Total assets		<u>9,500,000</u>

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LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:	Note		
Trade and other payables	(4)		1,350,000
Mortgage note payable-current portion		<u>400,000</u>	
Total current liabilities			1,750,000
Noncurrent liabilities:			
Mortgage note payable, remaining position		1,600,000	
Bank loan payable, due June 30, 2010		<u>500,000</u>	
Total noncurrent liabilities			2,100,000
Shareholders' equity:			
Share capital		3,000,000	
Reserves	(5)	1,400,000	
Retained earnings		<u>1,250,000</u>	
Total shareholders' equity			<u>5,650,000</u>
Total liabilities and shareholders' equity			<u>9,500,000</u>

Note 1 - Trade accounts receivable

Accounts receivable	800,000
Allowance for doubtful accounts	(<u>50,000</u>)
Net realizable value	
<u>750,000</u>	

Note 2 - Property, plant and equipment

	Cost	Accum. depr.	Book value
Land	500,000	-	500,000
Building	5,000,000	2,000,000	
3,000,000			
Machinery	3,000,000	1,200,000	
1,800,000			
Equipment	<u>400,000</u>	<u>100,000</u>	
<u>300,000</u>			
Total	<u>8,900,000</u>	<u>3,300,000</u>	
<u>5,600,000</u>			

Note 3 - Intangible assets

Trademark	150,000
Secret processes and formulas	<u>200,000</u>
Total	<u>350,000</u>

Note 4 - Trade and other payables

Notes payable	750,000
Accounts payable	350,000
Income tax payable	50,000
Accrued expenses	60,000
Estimated liability for damages	<u>140,000</u>
Total	<u>1,350,000</u>

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Note 5 - Reserves

Additional paid in capital	300,000
Retained earnings appropriated for plant expansion	1,000,000
Retained earnings appropriated for contingencies	<u>100,000</u>
Total	<u>1,400,000</u>

Problem 2-34

**Dilemma Company
Balance Sheet
December 31, 2008**

A S S E T S

	Note		
Current assets:			
Cash		800,000	
Trading equity securities		400,000	
Trade and other receivables	(1)	740,000	
Inventory		1,000,000	
Prepaid expenses		<u>160,000</u>	
Total current assets			3,100,000
Noncurrent assets:			
Property, plant and equipment	(2)	6,700,000	
Intangible asset	(3)	<u>200,000</u>	
Total noncurrent assets			<u>6,900,000</u>
Total assets			<u>10,000,000</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:			
Trade and other payables	(4)		1,200,000
Noncurrent liabilities:			
Bonds payable	(5)	1,800,000	
Note payable to bank, due July 1, 2010		<u>250,000</u>	
Total noncurrent liabilities			2,050,000
Shareholders' equity:			

Share capital, P100 par, 40,000 shares authorized 30,000 shares issued		3,000,000
Reserves	(6)	250,000
Retained earnings	(7)	3,750,000
Treasury shares, at cost, 2,000 shares		(250,000)
Total shareholders' equity		<u>6,750,000</u>
Total liabilities and shareholders' equity		<u>10,000,000</u>

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Note 1 - Trade and other receivables

Accounts receivable	750,000
Allowance for doubtful accounts	(50,000)
Dividend receivable	
<u>40,000</u>	
Total	<u>740,000</u>

Note 2 - Property, plant and equipment

	Cost	Accum. depr.	Book value
Land	500,000	-	500,000
Building in process	5,000,000	-	5,000,000
Machinery and equipment	<u>1,500,000</u>	<u>300,000</u>	
<u>1,200,000</u>			
Total	<u>7,000,000</u>	<u>300,000</u>	<u>6,700,000</u>

Note 3 - Intangible asset

Patent	<u>200,000</u>
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Note 4 - Trade and other payables

Accounts payable	900,000
Accrued expenses	150,000
Accrued interest on bonds payable (2,000,000 x 10% x 3/12)	
50,000	
Liability for loss on lawsuit	
<u>100,000</u>	
Total	<u>1,200,000</u>

Note 5 - Bonds payable

Bonds payable	2,000,000
Discount on bonds payable	(200,000)
	<u>1,800,000</u>

Note 6 - Reserves

Retained earnings appropriated for treasury shares	<u>250,000</u>
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Note 7 - Retained earnings

Unadjusted balance		
4,000,000		
Add: Cancellation of appropriation for contingencies		<u>150,000</u>
Total		4,150,000
Less: Interest accrued on bonds payable		50,000
Appropriated for treasury stock	250,000	
Actual loss on lawsuit		<u>100,000</u>
<u>400,000</u>		
Unappropriated retained earnings		
<u>3,750,000</u>		

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Problem 2-35

**Socorro Corporation
Balance Sheet
December 31, 2008**

ASSETS

	Note		
Current assets:			
Cash and cash equivalents	(1)	700,000	
Trade accounts receivable	(2)	700,000	
Inventories		600,000	
Prepaid expenses	(3)	<u>50,000</u>	
Total current assets			2,050,000
Noncurrent assets:			
Property, plant and equipment	(4)	4,150,000	
Long-term investment	(5)	1,000,000	
Investment property	(6)	500,000	
Intangible assets	(7)	550,000	
Other noncurrent assets	(8)	<u>450,000</u>	
Total noncurrent assets			<u>6,650,000</u>
Total assets			<u>8,700,000</u>

LIABILITIES AND EQUITY

Current liabilities:			
Trade and other payables	(9)	820,000	
Serial bonds payable-current portion		<u>100,000</u>	
Total current liabilities			920,000
Noncurrent liabilities:			
Serial bonds payable-remaining portion		400,000	
Unearned leasehold income-remaining portion		<u>280,000</u>	

Total noncurrent liabilities		680,000
Equity:		
Share capital	(10)	5,150,000
Reserves	(11)	1,050,000
Retained earnings	(12)	1,200,000
Treasury shares, at cost		(<u>300,000</u>)
Total equity		<u>7,100,000</u>
Total liabilities and equity		<u>8,700,000</u>

Note 1 - Cash and cash equivalents

Cash	500,000
Money market placement	<u>200,000</u>
Total	<u>700,000</u>

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Note 2 - Trade accounts receivable

Accounts receivable	750,000
Allowance for doubtful accounts	(<u>50,000</u>)
Net realizable value	
<u>700,000</u>	

Note 3 - Prepaid expenses

Store supplies	
<u>50,000</u>	

Note 4 - Property, plant and equipment

	Cost	Accum. depr.	Book value
Land	400,000	-	400,000
Building	3,500,000	500,000	3,000,000
Equipment	<u>1,000,000</u>	<u>250,000</u>	
<u>750,000</u>			
Total	<u>4,900,000</u>	<u>750,000</u>	
<u>4,150,000</u>			

Note 5 - Long-term investment

Investment in bonds	
<u>1,000,000</u>	

Note 6 - Investment property

Land for undetermined use	
<u>500,000</u>	

Note 7 - Intangible assets

Trademark	300,000
Patent	<u>250,000</u>
Total	<u>550,000</u>

Note 8 - Other noncurrent assets

Advances to officers	150,000
Restricted foreign deposit	<u>300,000</u>
Total	<u>450,000</u>

Note 9 - Trade and other payables

Accounts payable	500,000
Note payable	100,000
Income tax payable	150,000
Unearned leasehold income-current portion	<u>70,000</u>
Total	<u>820,000</u>

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Note 10 - Common stock

Share capital issued	5,000,000
Stock dividend payable	<u>150,000</u>
Total	<u>5,150,000</u>

Note 11 - Reserves

Share premium	250,000
Retained earnings appropriated for plant expansion	500,000
Retained earnings appropriated for treasury share	<u>300,000</u>
Total reserves	<u>1,050,000</u>

Note 12 - Retained earnings

Retained earnings unappropriated	1,500,000
Appropriation for treasury share	<u>(300,000)</u>
Adjusted balance	<u>1,200,000</u>

Problem 2-36

**Magna Company
Balance Sheet**

December 31, 2008

A S S E T S

	Note		
Current assets:			
Cash		400,000	
Trading equity securities		100,000	
Trade accounts receivable	(1)	700,000	
Inventories		800,000	
Prepaid expenses		<u>100,000</u>	
Total current assets			2,100,000
Noncurrent assets:			
Property, plant and equipment	(2)	7,150,000	
Long-term investments	(3)	300,000	
Intangible assets	(4)	<u>300,000</u>	
Total noncurrent assets			<u>7,750,000</u>
Total assets			<u>9,850,000</u>

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LIABILITIES AND EQUITY

	Note		
Current liabilities:			
Trade and other payables	(5)	550,000	
Note payable-short-term debt		<u>450,000</u>	
Total current liabilities			1,000,000
Noncurrent liabilities:			
Bonds payable	(6)	1,900,000	
Note payable-long-term debt		<u>300,000</u>	
Total noncurrent liabilities			2,200,000
Equity:			
Share capital	(7)	2,750,000	
Reserves	(8)	1,450,000	
Retained earnings		<u>2,450,000</u>	
Total equity			<u>6,650,000</u>
Total liabilities and equity			<u>9,850,000</u>

Note 1 - Trade accounts receivable

Accounts receivable	750,000
Allowance for doubtful accounts	<u>(50,000)</u>
Net realizable value	
<u>700,000</u>	

Note 2 - Property, plant and equipment

value	Cost	Accum. depr.	Book
Land	1,250,000	-	1,250,000
Land for future plant site	1,500,000	-	1,500,000
Building	5,000,000	1,600,000	
3,400,000			
Equipment	<u>1,400,000</u>	<u>400,000</u>	
<u>1,000,000</u>			
Total	<u>9,150,000</u>	<u>2,000,000</u>	
<u>7,150,000</u>			

Note 3 - Long-term investments

Investment in equity securities	250,000
Cash surrender value	<u>50,000</u>
Total	<u>300,000</u>

Note 4 - Intangibles assets

Franchise	100,000
Goodwill	<u>200,000</u>
Total	<u>300,000</u>

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Note 5 - Trade and other payables

Accounts payable	400,000
Taxes payable	<u>150,000</u>
Total	<u>550,000</u>

Note 6 - Bonds payable

Bonds payable	2,000,000
Discount on bonds payable	(<u>100,000</u>)
<u>1,900,000</u>	

Note 7 - Share capital

Preference share capital, P5 stated value, 300,000 shares authorized, 150,000 shares issued	750,000
Ordinary share capital, P20 par value, 400,000 shares authorized, 100,000 shares issued	<u>2,000,000</u>
Total	<u>2,750,000</u>

Note 8 - Reserves

Share premium-preference 250,000	
Share premium-ordinary	1,000,000
Retained earnings appropriated for contingencies	<u>200,000</u>
Total	<u>1,450,000</u>

Problem 2-37

Summa Company Balance Sheet December 31, 2008

ASSETS

Current assets:	Note		
Cash	(1)	700,000	
Bond sinking fund		2,000,000	
Trade and other receivables	(2)	830,000	
Inventory		1,200,000	
Prepaid expenses		<u>100,000</u>	
Total current assets			4,830,000
Noncurrent assets:			
Property, plant and equipment	(3)	5,500,000	
Investment property		700,000	
Intangible asset	(4)	<u>370,000</u>	
Total noncurrent assets			<u>6,570,000</u>
Total assets			<u>11,400,000</u>

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LIABILITIES AND EQUITY

Current liabilities:	Note		
Trade and other payables	(5)	2,050,000	
Bonds payable due June 30, 2009		<u>2,000,000</u>	
Total current liabilities			4,050,000
Noncurrent liability:			
Deferred tax liability			650,000
Equity:			
Share capital	(6)	3,500,000	
Reserves	(7)	500,000	
Retained earnings		<u>2,700,000</u>	
Total equity			<u>6,700,000</u>
Total liabilities and equity			<u>11,400,000</u>

Note 1 - Cash

Cash on hand	50,000
Cash in bank	<u>650,000</u>
	<u>700,000</u>

Note 2 - Trade and other receivables

Accounts receivable	650,000
Allowance for doubtful accounts	(50,000)
Notes receivable	200,000
Accrued interest receivable	<u>30,000</u>
Total	<u>830,000</u>

Note 3 - Property, plant and equipment

	Cost	Accum. depr.	Book value
Land	1,000,000	-	1,000,000
Building	5,500,000	2,500,000	
3,000,000			
Furniture and equipment	<u>2,400,000</u>	<u>900,000</u>	
<u>1,500,000</u>			
Total	<u>8,900,000</u>	<u>3,400,000</u>	
<u>5,500,000</u>			

Note 4 - Intangible asset

Patent	<u>370,000</u>
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24**Note 5 - Trade and other payables**

Accounts payable	1,000,000
Notes payable	850,000
Accrued taxes	50,000
Other accrued liabilities	<u>150,000</u>
Total	<u>2,050,000</u>

Note 6 - Share capital

Authorized share capital, 50,000 shares, P100 par	
5,000,000	
Unissued share capital	(2,000,000)
Issued share capital	
3,000,000	

Subscribed share capital, 10,000 shares	1,000,000
Subscription receivable	(<u>500,000</u>) <u>500,000</u>
Paid in capital	<u>3,500,000</u>

Note 7 - Reserves

Share premium	300,000
Retained earnings appropriated for contingencies	<u>200,000</u>
Total	<u>500,000</u>

Problem 2-38

**Boracay Company
Balance sheet
December 31, 2008**

A S S E T S

Current assets:	Note		
Cash and cash equivalents	(1)	1,200,000	
Trading equity securities		400,000	
Trade receivables	(2)	1,000,000	
Inventory (1,300,000 - 50,000 - 250,000)		1,000,000	
Prepaid expenses	(3)	<u>50,000</u>	
Total current assets			3,650,000
Noncurrent assets:			
Property, plant and equipment	(4)	3,950,000	
Intangible asset	(5)	<u>100,000</u>	
Total noncurrent assets			<u>4,050,000</u>
Total assets			<u>7,700,000</u>

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LIABILITIES AND EQUITY

Current liabilities:	Note		
Trade and other payables	(6)		2,050,000
Noncurrent liability:			
Mortgage payable			2,000,000
Equity:			
Ordinary share capital, P100 par		3,000,000	
Share premium		200,000	
Retained earnings	(7)	<u>450,000</u>	
Total equity			<u>3,650,000</u>

Total liabilities and equity 7,700,000

Note 1 - Cash and cash equivalents

Cash in bank 700,000
Money market placement 500,000
Total 1,200,000

Note 2 - Trade receivables

Accounts receivable 800,000
Notes receivable 200,000
Total 1,000,000

Note 3 - Prepaid expenses

Office supplies 50,000

Note 4 - Property, plant and equipment

	Cost	Accum. depr.	Book
value			
Land	1,000,000	-	1,000,000
Building	3,000,000	300,000	2,700,000
Office equipment	<u>250,000</u>	<u>-</u>	
<u>250,000</u>			
Total	<u>4,250,000</u>	<u>300,000</u>	
<u>3,950,000</u>			

Note 5 - Intangible asset

Goodwill 100,000

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Note 6 - Trade accounts and other payables

Accounts payable 1,500,000
Withholding tax payable 100,000
Accrued salaries payable 250,000
Accrued interest payable 200,000
Total 2,050,000

Note 7 - Retained earnings

Net assets per book		
4,200,000		
Contributed capital		<u>3,200,000</u>
Unadjusted retained earnings		1,000,000
Unrecorded expenses:		
Salaries	250,000	
Depreciation on building (3,000,000/20 x 2)		<u>300,000</u>
<u>550,000</u>		
Adjusted retained earnings		
<u>450,000</u>		

Problem 2-39

**Dakak Company
Balance Sheet
December 31, 2008**

A S S E T S

Current assets:	Note		
Cash and cash equivalents		500,000	
Trading equity securities		600,000	
Accounts receivable		750,000	
Inventories		<u>850,000</u>	
Total current assets			2,700,000
Noncurrent assets:			
Property, plant and equipment	(1)	4,000,000	
Long-term investment	(2)	<u>2,250,000</u>	
Total noncurrent assets			<u>6,250,000</u>
Total assets			<u>8,950,000</u>

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LIABILITIES AND EQUITY

Current liabilities:	Note		
Trade and other payables	(3)	1,500,000	
Bonds payable-current portion		<u>500,000</u>	
Total current liabilities			2,000,000
Noncurrent liabilities:			
Bonds payable-remaining portion		1,500,000	
Note payable, due December 31, 2009		800,000	

Other noncurrent liability	(4)	<u>200,000</u>	
Total noncurrent liabilities			2,500,000
Equity:			
Share capital, P100 par, 50,000 shares		5,000,000	
Share premium		500,000	
Retained earnings (deficit)	(5)	<u>(1,050,000)</u>	
Total equity			<u>4,450,000</u>
Total liabilities and equity			<u>8,950,000</u>

Note 1 - Property, plant and equipment

Property, plant and equipment	6,000,000
Accumulated depreciation	<u>(2,000,000)</u>
Net book value	<u>4,000,000</u>

Note 2 - Long term investment

Advances to subsidiary	<u>2,250,000</u>
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Note 3 - Trade and other payables

Accounts payable	1,000,000
Accrued expenses	100,000
Customers' deposit	<u>400,000</u>
Total	<u>1,500,000</u>

Note 4 - Other noncurrent liability

Advances from officer, not repayable currently	
<u>200,000</u>	

Note 5 - Retained earnings

Equity per book	4,800,000
Contributed capital	<u>5,500,000</u>
Unadjusted retained earnings	(700,000)
Writeoff of goodwill	<u>(350,000)</u>
Deficit	<u>(1,050,000)</u>

CHAPTER 3**Problem 3-1**

1. C
2. C
3. A
4. B
5. C

Problem 3-2

1. A
2. B
3. B
4. A
5. C

Problem 3-3 Answer D

Capital - December 31	2,500,000
Add: Withdrawals - merchandise at cost	<u>200,000</u>
Total	2,700,000
Less: Capital - January 1	2,000,000
Additional investment (1,000,000 + 120,000)	<u>1,120,000</u>

	<u>3,120,000</u>
Net loss	<u>(420,000)</u>

Problem 3-4 Answer B

Total assets - January 1		
5,000,000		
Less: Total liabilities		2,000,000
Contributed capital		<u>2,000,000</u>
<u>4,000,000</u>		
Retained earnings - January 1		
<u>1,000,000</u>		
 Total assets - December 31		
7,500,000		
Less: Total liabilities		3,200,000
Contributed capital (2,000,000 + 500,000 + 300,000)		<u>2,800,000</u>
		<u>6,000,000</u>
Retained earnings - December 31		1,500,000
Add: Dividends paid		<u>500,000</u>
Total		2,000,000
Less: Retained earnings - January 1		<u>1,000,000</u>
Net income		<u>1,000,000</u>

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Problem 3-5 Answer D

Effect on net assets

Decrease	Increase
Cash	450,000
Accounts receivable	300,000
Merchandise inventory	200,000
Accounts payable	100,000
Prepaid expenses	20,000
Accrued expenses	40,000
Unearned rental income	30,000
Notes payable	200,000
Accrued interest payable	<u>30,000</u>
Total	<u>700,000</u>
	<u>670,000</u>
Solution:	
Net increase (700,000 - 670,000)	30,000
Add: Withdrawals	<u>100,000</u>
Total	130,000
Less:	
Additional investment	<u>500,000</u>

Net loss (370,000)

Problem 3-6 Answer B

Assets	3,000,000
Less: Liabilities	<u>(200,000)</u>
Shareholders' equity	2,800,000
Less: Contributed capital (15,000 x 150)	2,250,000
Increase in contributed capital - 2,000 shares	<u>250,000</u>
<u>2,500,000</u>	
Retained earnings, December 31	300,000
Add: Dividends	<u>500,000</u>
Net income	<u>800,000</u>

Problem 3-7 Answer A

Beginning inventory	1,600,000
Purchases	5,300,000
Purchase discounts	<u>(100,000)</u>
	<u>5,200,000</u>
Goods available for sale	6,800,000
Less:	
Ending inventory	<u>2,150,000</u>
Cost of goods sold	<u>4,650,000</u>

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Problem 3-8 Answer A

Inventory - January 1	4,500,000
Purchases	<u>6,000,000</u>
Goods available for sale	10,500,000
Less:	
Inventory - December 31	<u>2,500,000</u>
Cost of goods sold before writedown	8,000,000
Loss on inventory writedown	<u>1,500,000</u>
Cost of goods sold after writedown	<u>9,500,000</u>

Problem 3-9 Answer A

Finished goods - January 1	1,000,000
Cost of goods manufactured	<u>5,000,000</u>
Goods available for sale	6,000,000
Less:	
Finished goods - December 31	<u>(1,200,000)</u>
Cost of goods sold	<u>4,800,000</u>

Problem 3-10 Answer A

Beginning raw materials	220,000
Raw materials purchases	<u>3,000,000</u>
Raw materials available for use	3,220,000
Ending raw materials	<u>300,000</u>
Less:	
Raw materials used	2,920,000
Direct labor	1,200,000
Factory overhead:	
Indirect labor	600,000
Taxes and depreciation - factory	200,000
Utilities (60% x 500,000)	<u>300,000</u>
	<u>1,100,000</u>
Total manufacturing cost	5,220,000
Beginning work in process	<u>400,000</u>
Total cost of good in process	5,620,000
Ending work in process	<u>(480,000)</u>
Cost of goods manufactured	5,140,000
Beginning finished goods	<u>250,000</u>
Goods available for sale	5,390,000
Ending finished goods	<u>(180,000)</u>
Cost of goods sold	<u>5,210,000</u>

31**Problem 3-11 Answer D**

Raw materials purchased	4,300,000
Increase in raw materials	<u>(150,000)</u>
Raw materials used	4,150,000
Direct labor	2,000,000
Factory overhead	<u>3,000,000</u>
Total manufacturing cost	9,150,000
Increase in goods in process	<u>(500,000)</u>
Cost of goods manufactured	8,650,000
Decrease in finished goods	<u>350,000</u>
Cost of goods sold	<u>9,000,000</u>

Problem 3-12 Answer C

Beginning materials	200,000
Purchases	2,500,000
Purchase discounts	<u>(100,000)</u>
Transportation in	<u>200,000</u>
Raw materials available for use	2,800,000
Ending materials (600,000 - 200,000)	<u>(400,000)</u>
Raw materials used	2,400,000

Direct labor	3,000,000
Manufacturing overhead	<u>1,500,000</u>
Total manufacturing cost	6,900,000
Beginning goods in process	<u>300,000</u>
Total cost of goods in process	7,200,000
Ending goods in process (500,000 - 300,000)	<u>(200,000)</u>
Cost of goods manufactured	7,000,000
Beginning finished goods	<u>400,000</u>
Goods available for sale	7,400,000
Ending finished goods (700,000 - 400,000)	<u>(300,000)</u>
Cost of goods sold	<u>7,100,000</u>

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Problem 3-13 Answer A

Beginning raw materials	400,000
Purchases of raw materials	
<u>2,300,000</u>	
Raw materials available for use	
2,700,000	
Ending raw materials	(
<u>340,000)</u>	
Raw materials used	
2,360,000	
Direct labor	
1,980,000	
Factory overhead:	
Depreciation of factory building	320,000
Factory supervisor's salary	560,000
Indirect labor	<u>360,000</u>
<u>1,240,000</u>	
Total manufacturing cost	
5,580,000	
Beginning goods in process	
<u>760,000</u>	
Total goods in process	
6,340,000	

Ending goods in process
(1,000,000)
 Cost of goods manufactured
5,340,000

Problem 3-14 Answer C

Advertising
 1,500,000
 Freight out
 750,000
 Rent for office space (1,800,000 x 1/2)
 900,000 Sales salaries and commission
1,400,000 Total selling expenses
4,550,000

Problem 3-15 Answer D

Property taxes
 250,000
 Doubtful accounts
 1,600,000
 Officers' salaries
 1,500,000
 Insurance
850,000
 Total administrative expenses
4,200,000

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Problem 3-16 Answer C

Cost of sales = 20%/40% = 50%

Sales			100%
2,000,000	Cost of sales		
<u>50%</u>	<u>1,000,000</u>	Gross income	

	50%	1,000,000	Expenses
400,000	Interest expense	20%	
<u>5%</u>	<u>100,000</u>		
Income before income tax		<u>25%</u>	
500,000			
Income tax (35% x 500,000)			
<u>175,000</u>			
Net income			
<u>325,000</u>			
Income before income tax (325,000/65%)			
<u>500,000</u>			
Sales (500,000/25%)			
<u>2,000,000</u>			

Problem 3-17 Answer C

Sales	
9,600,000	
Cost of sales (9,600,000/160%)	
<u>6,000,000</u>	
Gross income	
3,600,000	
Selling and administrative expenses (30% x 9,600,000)	
<u>2,880,000</u>	
Net income	
<u><u>720,000</u></u>	

Problem 3-18 Answer A

Sales	3,000,000	Cost of sales	
		<u>1,200,000</u>	
Gross income	1,800,000		
Interest revenue			
<u>100,000</u>			
Total	1,900,000		
Expenses:			
Commissions		200,000	
Freight out		60,000	
Administrative expenses		300,000	
Doubtful accounts		60,000	

Loss on sale of equipment	<u>180,000</u>
(800,000)	
Income from continuing operations before tax	
<u>1,100,000</u>	

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Problem 3-19 Answer C

Sales	
50,000,000	
Cost of goods sold	
(30,000,000)	
Gross income	
20,000,000	
Gain on expropriation	
2,000,000	
Investment income	
<u>3,000,000</u>	
Total income	
25,000,000	
Expenses:	
Selling expenses	5,000,000
General and administrative	4,000,000
Finance cost	<u>1,500,000</u>
<u>10,500,000</u>	
Income before tax	
14,500,000	
Income tax expense	
(5,000,000)	
Net income	
<u>9,500,000</u>	

Interest expense		
2,000,000		
Gain on early extinguishment		
<u>500,000</u>		(
Finance cost		
<u>1,500,000</u>		

Problem 3-20 Answer A

Sales	
5,000,000	
Cost of goods sold	
(2,800,000)	

Gross income	
2,200,000	
Other income (400,000 + 50,000)	
<u>450,000</u>	
Total income	
2,650,000	
Expenses:	
Selling expenses	700,000
General and administrative	<u>600,000</u>
<u>1,300,000</u>	
Income before income tax	
1,350,000	
Income tax expense	
(<u>150,000</u>)	
Income from continuing operations	
<u>1,200,000</u>	

The credit balance in the foreign translation adjustment account is an addition to shareholders' equity.

Problem 3-21 Answer D

Net income per book	
7,410,000	
Add: Unrealized loss	540,000
Adjustment of profit of prior year	<u>750,000</u>
<u>1,290,000</u>	
Adjusted net income	
<u>8,700,000</u>	

The unrealized loss on available for sale securities is a deduction from total shareholders' equity.

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The adjustment of profit of prior year is shown in the statement of retained earnings.

Problem 3-22 Answer D

Reported income before tax	
5,000,000	
Add: Adjustment of profit of prior year	
<u>1,400,000</u>	
Total	
6,400,000	
Less: Dividend received from Cinn	
<u>320,000</u>	

Corrected income before tax
6,080,000

Problem 3-23 Answer D

Problem 3-24 Answer A

Problem 3-25 Answer C

Replacement cost		
5,500,000		
Deductible clause		
<u>250,000</u>		
Proceeds of insurance policy		
5,250,000		
Less: Carrying amount	1,500,000	
Cost of dismantling		<u>100,000</u>
<u>1,600,000</u>		
Gain on involuntary conversion		
<u>3,650,000</u>		

Problem 3-26 (Functional method)

**Karla Company
Income Statement
Year ended December 31, 2008**

	Note		
Net sales revenue	(1)		
7,700,000			
Cost of sales	(2)		
<u>(5,000,000)</u>			
Gross income			
2,700,000			
Other income	(3)		
<u>400,000</u>			
Total income			
3,100,000			
Expenses:			
Selling expenses	(4)	950,000	
Administrative expenses	(5)	800,000	
Other expenses	(6)	<u>100,000</u>	<u>1,850,000</u>
Income before tax			1,250,000
Income tax			
<u>(250,000)</u>			
Net income			<u>1,000,000</u>

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Note 1 - Net sales revenue

Gross sales	
7,850,000	
Sales returns and allowances	
(140,000)	
Sales discounts	
(<u>10,000</u>)	
Net sales revenue	
<u>7,700,000</u>	

Note 2 - Cost of sales

Inventory, January 1		
1,000,000		
Purchases		5,250,000
Freight in		500,000
Purchase returns and allowances		(150,000)
Purchase discounts		(<u>100,000</u>)
Net purchases		
<u>5,500,000</u>		
Goods available for sale		
6,500,000		
Inventory, December 31		
(<u>1,500,000</u>)		
Cost of sales		
<u>5,000,000</u>		

Note 3 - Other income

Rental income	
250,000	
Dividend revenue	
<u>150,000</u>	
Total other income	
<u>400,000</u>	

Note 4 - Selling expenses

Freight out	
175,000	
Salesmen's commission	
650,000	
Depreciation - store equipment	
<u>125,000</u>	
Total selling expenses	
<u>950,000</u>	

Note 5 - Administrative expenses

Officers' salaries
500,000
Depreciation - office equipment
300,000
Total administrative expenses
800,000

Note 6 - Other expenses

Loss on sale of equipment
50,000
Loss on sale of investment
50,000
Total other expenses
100,000

37
Natural method
Karla Company
Income Statement
Year ended December 31, 2008

	Note	
Net sales revenue	(1)	
7,700,000		
Other income	(2)	
400,000		
Increase in inventory	(3)	
<u>500,000</u>		
Total		
8,600,000		
Expenses:		
Net purchases	(4)	5,500,000
Freight out		175,000
Salesmen's commission		650,000
Depreciation	(5)	425,000
Officers' salaries		500,000
Other expenses	(6)	<u>100,000</u>
<u>7,350,000</u>		
Income before tax		
1,250,000		
Income tax		
(<u>250,000</u>)		
Net income		
<u>1,000,000</u>		

Note 1 - Net sales revenue

Gross sales
7,850,000
Sales returns and allowances
(140,000)
Sales discounts
(10,000)
Net sales revenue
7,700,000

Note 2 - Other income

Rental income
250,000
Dividend revenue
150,000
Total other income
400,000

Note 3 - Increase in inventory

Inventory, December 31
1,500,000
Inventory, January 1
1,000,000
Increase in inventory
500,000

Note 4 - Net purchases

Purchases
5,250,000
Freight in
500,000
Purchase returns and allowances
150,000)
Purchase discounts
(100,000)
Net purchases
5,500,000

38**Note 5 - Depreciation**

Depreciation - store equipment
125,000

Depreciation - office equipment	
	<u>300,000</u>
Total	<u>425,000</u>

Note 6 - Other expenses

Loss on sale of equipment	
	50,000
Loss on sale of investment	
	<u>50,000</u>
Total	
	<u>100,000</u>

Problem 3-27

**Masay Company
Statement of Cost of Goods Manufactured
Year Ended December 31, 2008**

Raw materials - January 1		
	200,000	
Purchases		
	<u>3,000,000</u>	
Raw materials available for use		
	3,200,000	
Less: Raw materials - December 31		
	<u>280,000</u>	
Raw materials used		
	2,920,000	
Direct labor		
	950,000	
Factory overhead:		
Indirect labor		250,000
Superintendence		210,000
Light, heat and power		320,000
Rent - factory building		120,000
Repair and maintenance - machinery		50,000
Factory supplies used		110,000
Depreciation - machinery		<u>60,000</u>
	<u>1,120,000</u>	
Total manufacturing cost		
	4,990,000	
Goods in process - January 1		
	<u>240,000</u>	
Total Cost of goods in process		
	5,230,000	
Less: Goods in process - December 31		
	<u>170,000</u>	

Cost of goods manufactured
5,060,000

39
Cost of sales method

Masay Company
Income Statement
Year ended December 31, 2008

	Note	
Net sales revenue	(1)	
7,450,000		
Cost of goods sold	(2)	
<u>(5,120,000)</u>		
Gross income		
2,330,000		
Other income	(3)	
<u>210,000</u>		
Total income		
2,540,000		
Expenses:		
Selling expenses	(4)	830,000
Administrative expenses	(5)	590,000
Other expense	(6)	<u>300,000</u>
<u>1,720,000</u>		
Income before tax		
820,000		
Income tax expense		
<u>(320,000)</u>		
Net income		
<u>500,000</u>		

Note 1 - Net sales revenue

Sales
7,500,000
Sales returns and allowances
(50,000)
Net sales revenue
7,450,000

Note 2 - Cost of goods sold

Finished goods - January 1
360,000

Cost of goods manufactured
5,060,000
Goods available for sale
5,420,000
Finished goods - December 31
(300,000)
Cost of goods sold
5,120,000

Note 3 - Other income

Gain from expropriation
100,000
Interest income
10,000
Gain on sale of equipment
100,000

210,000

Note 4 - Selling expenses

Sales salaries
400,000
Advertising
160,000
Depreciation - store equipment
70,000
Delivery expenses
200,000
Total
830,000

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Note 5 - Administrative expenses

Office salaries
150,000
Depreciation - office equipment
40,000
Accounting and legal fees
150,000
Office expenses
250,000
Total
590,000

Note 6 - Other expense

Earthquake loss
300,000

Nature of expense method
Masay Company
Income Statement
Year Ended December 31, 2008

	Note	
Net sales revenue	(1)	
7,450,000		
Other income	(2)	
<u>210,000</u>		
Total income		
7,660,000		
Expenses:		
Decrease in finished goods and goods in process	(3)	130,000
Raw materials used	(4)	2,920,000
Direct labor		950,000
Factory overhead	(5)	1,120,000
Salaries	(6)	550,000
Advertising		160,000
Depreciation	(7)	110,000
Delivery expenses		200,000
Accounting and legal fees		150,000
Office expenses		250,000
Other expense	(8)	<u>300,000</u>
<u>6,840,000</u>		
Income before tax		
820,000		
Income tax expense		
<u>(320,000)</u>		
Net income		
<u>500,000</u>		

Note 1 - Net sales revenue

Sales
7,500,000
Sales returns and allowances
(50,000)
Net sales revenue
7,450,000

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Note 2 - Other income

Gain from expropriation	
100,000	
Interest income	
10,000	
Gain on sale of equipment	
<u>100,000</u>	
<u>210,000</u>	

Note 3 - Decrease in finished goods and goods in process

	January 1	December 31
Decrease		
Finished goods	360,000	300,000
60,000		
Goods in process	<u>240,000</u>	<u>170,000</u>
<u>70,000</u>		
Total	<u>600,000</u>	<u>470,000</u>
<u>130,000</u>		

Note 4 - Raw materials used

Raw materials - January 1	
200,000	
Purchases	
<u>3,000,000</u>	
Raw materials available for use	
3,200,000	
Raw materials - December 31	
<u>280,000</u>	
Raw materials used	
<u>2,920,000</u>	

Note 5 - Factory overhead

Indirect labor	
250,000	
Superintendence	
210,000	
Light, heat and power	
320,000	
Rent - factory building	
120,000	
Repair and maintenance - machinery	
50,000	

Factory supplies used
 110,000
 Depreciation - machinery
60,000
 Total
1,120,000

Note 6 - Salaries

Sales salaries
 400,000
 Office salaries
150,000
 Total
550,000

Note 7 - Depreciation

Depreciation - store equipment
 70,000
 Depreciation - office equipment
40,000
 Total
110,000

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Note 8 - Other expense

Earthquake loss
300,000

Problem 3-28

Youth Company
Income Statement
Year ended December 31, 2008

	Note	
Net sales revenue	(1)	
8,870,000		
Cost of goods sold	(2)	
<u>(5,900,000)</u>		
Gross income		
2,970,000		
Expenses:		
Selling expenses	(3)	690,000
Administrative expenses	(4)	580,000
Other expense	(5)	<u>340,000</u>
<u>1,610,000</u>		

Income before tax
1,360,000
Income tax expense
(360,000)
Net income
1,000,000

Note 1 - Net sales revenue

Sales
9,070,000
Sales returns and allowances
(200,000)
Net sales revenue
8,870,000

Note 2 - Cost of goods sold

Beginning inventory		
1,500,000		
Purchases	5,750,000	
Transportation in	150,000	
Purchase discounts	(<u>100,000</u>)	
<u>5,800,000</u>		
Goods available for sale		
7,300,000		
Ending inventory		
(<u>1,400,000</u>)		
Cost of goods sold		
<u>5,900,000</u>		

Note 3 - Selling expenses

Depreciation - store equipment
110,000
Store supplies
80,000
Sales salaries
500,000
Total
690,000

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Note 4 - Administrative expenses

Officers' salaries
 400,000
 Depreciation - building
 120,000
 Office supplies
60,000
 Total
580,000

Note 5 - Other expense

Uninsured flood loss
340,000

Problem 3-29

**Christian Company
 Statement of Cost of Goods Manufactured
 Year Ended December 31, 2008**

Purchases	
1,600,000	
Freight in	
<u>80,000</u>	
Total	
1,680,000	
Increase in raw materials	
(<u>100,000</u>)	
Raw materials used	
1,580,000	
Direct labor	
1,480,000	
Factory overhead:	
Indirect labor	600,000
Depreciation - machinery	50,000
Factory taxes	130,000
Factory supplies expense	120,000
Factory superintendence	480,000
Factory maintenance	150,000
Factory heat, light and power	<u>220,000</u>
<u>1,750,000</u>	
Total manufacturing cost	
4,810,000	
Decrease in goods in process	
<u>90,000</u>	
Cost of goods manufactured	
<u>4,900,000</u>	

**Christian Company
 Income Statement
 Year Ended December 31, 2008**

Note

Sales revenue			8,000,000
Cost of goods sold	(1)		
<u>(5,100,000)</u>			
Gross income			2,900,000
Expenses:			
Selling expenses	(2)	800,000	
Administrative expenses	(3)		<u>930,000</u>
<u>1,730,000</u>			
Income before tax			1,170,000
Income tax expense			
<u>(170,000)</u>			
Net income			<u>1,000,000</u>

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Note 1 - Cost of goods sold

Cost of goods manufactured	4,900,000
Decrease in finished goods	<u>200,000</u>
Cost of goods sold	<u>5,100,000</u>

Note 2 - Selling expenses

Sales salaries	520,000
Advertising	120,000
Delivery expense	<u>160,000</u>
Total	<u>800,000</u>

Note 3 - Administrative expenses

Office supplies expense	30,000
Office salaries	800,000
Doubtful accounts	<u>100,000</u>
Total	<u>930,000</u>

Problem 3-30

Ronald Company
Statement of Cost of Goods Manufactured
Year Ended December 31, 2008

Materials - January 1	
1,120,000	
Purchases	1,600,000
Freight on purchases	220,000
Purchase discounts	(<u>20,000</u>)
<u>1,800,000</u>	
Materials available for use	
2,920,000	
Less: Materials - December 31	
<u>1,560,000</u>	
Materials used	
1,360,000	
Direct labor	
2,000,000	
Factory overhead:	
Heat, light and power	600,000
Repairs and maintenance	100,000
Indirect labor	360,000
Other factory overhead	340,000
Factory supplies used (300,000 + 660,000 - 540,000)	420,000
Depreciation - factory building	<u>280,000</u>
<u>2,100,000</u>	
Total manufacturing cost	
5,460,000	
Goods in process - January 1	
<u>360,000</u>	
Total cost of goods in process	
5,820,000	
Less: Goods in process - December 31	
<u>320,000</u>	
Cost of goods manufactured	
<u>5,500,000</u>	

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**Ronald Company
Income Statement
Year Ended December 31, 2008**

	Note
Net sales revenue	(1)
6,980,000	
Cost of goods sold	(2)
(<u>5,400,000</u>)	
Gross income	
1,580,000	

Other income	(3)
<u>160,000</u>	Total income
	1,740,000
Expenses:	
Selling expenses	200,000
Administrative expenses	<u>340,000</u>
<u>540,000</u>	Income before tax
	1,200,000
Income tax expense	
(<u>200,000</u>)	
Net income	
<u>1,000,000</u>	

Note 1 - Net sales revenue

Sales	7,120,000
Sales returns and allowances	(<u>140,000</u>)
Net sales revenue	<u>6,980,000</u>

Note 2 - Cost of goods sold

Finished goods - January 1	420,000
Cost of goods manufactured	<u>5,500,000</u>
Goods available for sale	5,920,000
Finished goods - December 31	(<u>520,000</u>)
Cost of goods sold	<u>5,400,000</u>

Note 3 - Other income

Interest revenue	<u>160,000</u>
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**Endless Company
Income Statement
Year Ended December 31, 2008**

	Note	
Net sales revenue	(1)	
8,600,000		
Cost of goods sold	(2)	
<u>(4,950,000)</u>		
Gross income		
3,650,000		
Other income	(3)	
<u>80,000</u>		
Total income		
3,730,000		
Expenses:		
Selling expenses	(4)	1,260,000
Administrative expenses	(5)	1,140,000
Other expenses	(6)	<u>50,000</u>
<u>2,450,000</u>		Income before tax
		1,280,000
Income tax		
<u>(280,000)</u>		
Net income		
<u>1,000,000</u>		

Note 1 - Net sales revenue

Sales	
8,750,000	
Sales returns and allowances	
<u>(150,000)</u>	
Net sales revenue	
<u>8,600,000</u>	

Note 2 - Cost of goods sold

Merchandise inventory, January 1	
1,100,000	
Purchases	4,600,000
Freight in	145,000
Purchase discounts	<u>(45,000)</u>
<u>4,700,000</u>	
Goods available for sale	
5,800,000	
Merchandise inventory, December 31	
<u>1,000,000</u>	
Cost of goods sold before writedown	
4,800,000	

Loss from inventory writedown
150,000
Cost of goods sold after inventory writedown
4,950,000

Note 3 - Other income

Dividend revenue
50,000
Gain on sale of equipment
10,000
Interest revenue
20,000
Total
80,000

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Note 4 - Selling expenses

Delivery expense
425,000
Depreciation - delivery truck
60,000
Depreciation - store equipment
25,000
Sales salaries
600,000
Store supplies
150,000
Total
1,260,000

Note 5 - Administrative expenses

Contribution
125,000
Depreciation - office
35,000
Doubtful accounts
30,000
Office salaries
950,000
Total
1,140,000

Note 6 - Other expenses

Loss on sale of trading securities
50,000

**Endless Company
Statement of Retained Earnings
Year Ended December 31, 2008**

Retained earnings - January 1	550,000
Prior period error - underdepreciation in 2006	(<u>200,000</u>)
Corrected beginning balance	350,000
Net income	<u>1,000,000</u>
Total	1,350,000
Dividends paid	(<u>450,000</u>)
Retained earnings - December 31	<u>900,000</u>

Problem 3-32

**Berna Company
Income Statement
Year Ended December 31, 2008**

Sales (1,000,000/25%)	
4,000,000	
Cost of goods sold (45% x 4,000,000)	
(<u>1,800,000</u>)	
Gross income	2,200,000
Expenses (30% x 4,000,000)	
(<u>1,200,000</u>)	
Net income	<u>1,000,000</u>
Cost of goods sold (150% x 30%)	45%
Net income (100% - 45% - 30%)	<u>25%</u>

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Computation:

Purchases (1,500,000/75%)	
2,000,000	
Raw materials - December 31	
<u>500,000</u>	
Raw materials used (50% x 3,000,000)	
1,500,000	
Direct labor (30% x 3,000,000)	
900,000	
Factory overhead (20% x 3,000,000)	
<u>600,000</u>	
Total manufacturing cost	
3,000,000	
Goods in process - December 31 (1/3 x 2,250,000)	
<u>750,000</u>	
Cost of goods manufactured	
2,250,000	
Finished goods - December 31 (25% x 1,800,000)	
<u>450,000</u>	

Cost of goods sold	
<u>1,800,000</u>	
Cash receipts:	
Cash investment	1,000,000
Collections (90% x 4,000,000)	<u>3,600,000</u>
4,600,000	
Cash disbursements:	
Purchases (75% x 2,000,000)	1,500,000
Direct labor	900,000
Factory overhead (600,000 - 100,000)	500,000
Operating expenses	<u>1,200,000</u>
<u>4,100,000</u>	
Cash balance - December 31	
<u>500,000</u>	

**Berna Company
Balance Sheet
December 31, 2008**

ASSETS

	Note	
Current assets:		
Cash		500,000
Accounts receivable (10% x 4,000,000)		400,000
Inventories	(1)	<u>1,700,000</u>
Total current assets		2,600,000
Noncurrent assets:		
Property, plant and equipment	(2)	<u>2,900,000</u>
Total assets		<u>5,500,000</u>

LIABILITIES AND EQUITY

Current liability:		
Accounts payable (25% x 2,000,000)		500,000
Equity:		
Common stock, P100 par		2,500,000
Additional paid in capital		1,500,000
Retained earnings		<u>1,000,000</u>
Total equity		<u>5,000,000</u>
Total liabilities and equity		<u>5,500,000</u>

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Note 1 - Inventories

Raw materials - December 31	
500,000	
Goods in process - December 31 (1/3 x 2,250,000)	
750,000	
Finished goods - December 31 (25% x 1,800,000)	
<u>450,000</u>	
Total	
	<u>1,700,000</u>

Note 2 - Property, plant and equipment

Total cost	
3,000,000	
Accumulated depreciation	
(<u>100,000</u>)	
Book value	
	<u>2,900,000</u>

CHAPTER 4

Problem 4-1

1. D
2. C
3. C
4. B
5. D

Problem 4-2

1. B
2. C
3. B
4. C
5. C

Problem 4-3 Answer A

Total revenues		Total expenses
2,200,000		(2,900,000)
Impairment loss (2,000,000 - 1,800,000)		
(200,000)		
Employee termination cost		
(100,000)		
Loss from discontinued operations		
<u>(1,000,000)</u>		

Problem 4-4 Answer C

Income	
3,000,000	
Impairment loss	
(500,000)	
Income before tax	
2,500,000	
Income tax - 35%	
(875,000)	
Net income	
<u>1,625,000</u>	

Problem 4-5 Answer D

Revenue	
50,000,000	
Expenses	
(32,000,000)	

Impairment loss
(20,000,000)
Loss from discontinued operation
(2,000,000)

Carrying amount of net assets
90,000,000
Recoverable amount
70,000,000
Impairment loss
20,000,000

Problem 4-6 Answer D

Revenue - January 1 to December 31
50,000,000
Expenses - January 1 to December 31
(37,000,000)
Termination cost
(4,000,000)
Income before tax
9,000,000
Income tax (35% x 9,000,000)
3,150,000
Income from discontinued operation
5,850,000

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Recoverable amount
56,500,000
Carrying amount of net assets
56,000,000
Expected gain - not recognized
500,000

Problem 4-7 Answer D

Sales - South
3,500,000
Expenses - South
3,900,000
Operating loss
(400,000)
Loss on disposal
(2,000,000)
Total loss
(2,400,000)

Tax saving (35% x 2,400,000)
840,000
Loss from discontinued operations
(1,560,000)

Problem 4-8 Answer D

Sales - Dakak
23,000
Cost of goods sold - Dakak
(14,000)
Other expenses - Dakak
(17,000)
Gain on disposal
15,000
Income before tax
7,000
Income tax (35% x 7,000)
(2,450)
Income from discontinued operations 4,550

Problem 4-9 Answer B

Operating loss for the year
8,000,000
Loss on disposal in 2008
500,000
Pretax loss from discontinued operations
8,500,000

The expected operating loss in 2009 and expected gain on disposal in 2009 are **not recognized in 2008**.

Problem 4-10 Answer D

Carrying value
15,000,000

Fair value
9,000,000
Cost to sell
(500,000)
Fair value less cost to sell
8,500,000

PFRS 5, paragraph 15, provides that an entity shall measure a noncurrent asset or disposal group classified as held for sale at the **lower of carrying amount and fair value less cost to sell**.

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Problem 4-11 Answer D

Cost

1,000,000

Accumulated depreciation

750,000

Book value - 4/1/2008

250,000

Fair value less cost to sell - 4/1/2008 (100,000 - 10,000)

90,000

Impairment loss - 4/1/2008

60,000

Impairment loss

60,000

Accumulated depreciation

60,000

Fair value less cost to sell - 12/31/2008 (150,000 - 20,000)

130,000

Fair value less cost to sell - 4/1/2008

90,000

Gain on impairment recovery

40,000

Accumulated depreciation

40,000

Gain on impairment recovery

40,000

IFRS 5, paragraph 25, provides that an entity shall **not depreciate** a noncurrent asset while it is classified as held for sale or while it is part of a disposal group classified as held for sale.

Problem 4-12 Answer C

Carrying amount

30,000,000

Fair value less cost to sell

22,000,000

Impairment loss

8,000,000

Allocated to goodwill

5,000,000

Balance allocated to **noncurrent assets**

3,000,000

Loss	Carrying amount	Fraction
PPE 2,400,000	16,000,000	16/20
Patent <u>600,000</u>	<u>4,000,000</u>	4/20
<u>3,000,000</u>	<u>20,000,000</u>	

Observe that the impairment loss is allocated first to goodwill and the remainder to the “noncurrent assets” in the disposal group. PFRS 5, paragraph 23, provides that the impairment loss for a disposal group classified as held for sale shall reduce the carrying amount of the **noncurrent assets** only. Thus, no loss is allocated to accounts receivable and inventory.

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CHAPTER 5

Problem 5-1

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

Problem 5-2

Problem 5-3

- | |
|------|
| 1. C |
| 2. C |
| 3. A |
| 4. B |
| 5. A |

Problem 5-4 Answer A

Cost	
	3,000,000
Accumulated depreciation (3,000,000 / 6 x 3)	
	<u>1,500,000</u>
Book value - January 1, 2008	
	<u>1,500,000</u>

Depreciation for 2008 $(1,500,000/5)$
300,000

Problem 5-5 Answer A

Cost
2,640,000
Accumulated depreciation $(2,640,000 / 8 \times 3)$
990,000
Book value - January 1, 2008
1,650,000

Accumulated depreciation - January 1, 2008
990,000
Depreciation for 2008 $(1,650,000 - 240,000 / 3)$
470,000
Balance - December 31, 2008
1,460,000

Problem 5-6 Answer D

Straight line depreciation for year 2008 $(1,536,000 / 8)$
192,000

Problem 5-7 Answer C

Cost - 1/1/2006
6,000,000
Accumulated depreciation - 1/1/2008 $(6,000,000 - 600,000 \times 20 \times 2)$
540,000
Book value - 1/1/2008
5,460,000

Depreciation for 2008 $(5,460,000 - 800,000 / 10)$
466,000

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Problem 5-8 Answer A

Patents - 1/1/2003
3,000,000
Accumulated amortization $(3,000,000 / 10 \times 5)$
1,500,000

Book value - 1/1/2008	<u>1,500,000</u>
Amortization of patents for 2008 (1,500,000 / 3)	500,000
Depreciation for 2008 (4,600,000 - 200,000 / 10)	<u>440,000</u>
Total charge against 2008 income	<u>940,000</u>

Problem 5-9 Answer D

Inventory	600,000
Retained earnings	600,000

Problem 5-10 Answer A

Inventory - January 1, 2008:	
Weighted average	7,700,000
FIFO	<u>7,200,000</u>
Effect of change - increase in inventory	<u>500,000</u>

Problem 5-11 Answer C

Percentage of completion	9,000,000
Cost recovery method	<u>7,000,000</u>
Cumulative effect - understatement of income	2,000,000
Tax (35% x 2,000,000)	(<u>700,000</u>)
Net cumulative effect	<u>1,300,000</u>

The change from cost recovery method to percentage of completion is a change in accounting policy. Accordingly, the cumulative effect is an adjustment of retained earnings.

Problem 5-12 Answer A

	Percentage of completion	Cost
recovery method		

2005		15,000,000
	7,000,000	
2006		16,000,000
	13,000,000	
2007		<u>7,000,000</u>
	<u>12,000,000</u>	
Total		<u>38,000,000</u>
	<u>32,000,000</u>	
Cumulative effect (38,000,000 - 32,000,000)		
		<u>6,000,000</u>

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Problem 5-13 Answer A

Only the unrecorded warranty cost of P100,000 on December 31, 2007 should be accounted for as a prior period error. The change from straight line to accelerated depreciation is a change in estimate and therefore should be treated currently and prospectively.

Problem 5-14 Answer B

Retained earnings (2,000,000 / 5)	
	400,000
Depreciation	
	400,000
Accumulated depreciation	
	800,000

Problem 5-15 Answer A

Retained earnings - January 1, 2008	
	850,000
Prior period errors - underdepreciation:	
2006	
	(25,000)
2007	
	<u>(25,000)</u>
Corrected beginning balance	
	800,000
Net income for 2008	
	<u>500,000</u>
Retained earnings - December 31, 2008	
	<u>1,300,000</u>

Problem 5-16 Answer B

Net income	
	3,500,000
Unrealized gain on available for sale securities	250,000
Foreign currency translation loss	(50,000)
Revaluation surplus	<u>1,000,000</u>
Net amount	<u>4,700,000</u>

Problem 5-17 Answer C

Income from continuing operations	
	10,000,000
Unrealized loss on available for sale securities	(2,000,000)
Casualty loss	(500,000)
Foreign currency translation gain	<u>1,000,000</u>
Comprehensive income	<u>8,500,000</u>

Comprehensive income as an **American term** and this is the same as the concept of recognized gains and losses. The dividend paid is a deduction from retained earnings.

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Problem 5-18

Building	
	15,000,000
Accumulated depreciation (15,000,000 / 15 x 3)	<u>3,000,000</u>
Book value - December 31, 2007	<u>12,000,000</u>
Machinery	
	10,000,000
Accumulated depreciation (10,000,000 / 10 x 3)	<u>3,000,000</u>
Book value - December 31, 2007	<u>7,000,000</u>

Furniture and fixtures	
	3,500,000
Accumulated depreciation (3,500,000 / 7 x 3)	
	<u>1,500,000</u>
Book value - December 31, 2007	
	<u>2,000,000</u>

Depreciation for 2008:	
Building (12,000,000 / 10)	
	1,200,000
Machinery (7,000,000 / 7)	
	1,000,000
Furniture and fixtures (2,000,000 / 5)	
	<u>400,000</u>
Total depreciation	
	<u>2,600,000</u>

Problem 5-19

Equipment - January 1, 2004	
	4,000,000
Accumulated depreciation (4,000,000 - 400,000 / 10 x 4)	
	<u>1,440,000</u>
Book value - December 31, 2007	
	<u>2,560,000</u>

Revised annual depreciation (2,560,000 - 460,000 / 7)	
	<u>300,000</u>

Problem 5-20

1. A change in accounting policy made voluntarily is accounted for retrospectively.
2. A change in accounting policy required by an accounting standard is accounted for as required by the transitional provisions. If there are no transitional provisions, the change is recognized retrospectively.
3. A change in residual value is a change in estimate and therefore accounted for currently and prospectively.
4. An immaterial error can be ignored or corrected in the current year as a component of income of the current year.
5. A material error is accounted for retrospectively. Undue cost and effort would not be an acceptable excuse for retrospective application.

Problem 5-21

Reliable Company
Statement of Retained Earnings
Year Ended December 31, 2008

Retained earnings - January 1		200,000
Prior period error - overdepreciation in 2007		100,000
Change in accounting policy from FIFO to weighted average method - credit adjustment		<u>150,000</u>
Corrected beginning balance		450,000
Net income		1,300,000
Decrease in appropriation for treasury share		<u>200,000</u>
Total		1,950,000
Cash dividends paid to shareholders		(500,000)
Current appropriation for contingencies		<u>(100,000)</u>
Retained earnings - December 31		<u>1,350,000</u>

Problem 5-22

Net income		3,000,000
Loss from fire		(50,000)
Goodwill impairment		(250,000)
Loss on sale of equipment		(200,000)
Gain on retirement of bonds payable		100,000
Gain on life insurance settlement		<u>450,000</u>
Adjusted net income		<u>3,050,000</u>

Gondola Company
Statement of Retained Earnings
Year ended December 31, 2008

Balance - January 1	2,600,000
Compensation of prior period not accrued	(500,000)
Correction of prior period error - credit	<u>400,000</u>
Adjusted beginning balance	2,500,000
Net income - adjusted	3,050,000
Stock dividend	(700,000)
Loss on retirement of preference share	(350,000)
Appropriated for treasury share	<u>(1,000,000)</u>
Balance - December 31	<u>3,500,000</u>

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Problem 5-23

Angola Company
Comparative Income Statement
Years ended December 31, 2008 and 2007

	2008	2007
Sales	6,000,000	4,500,000
Cost of goods sold	<u>(2,900,000)</u>	<u>(2,300,000)</u>
Gross income	3,100,000	2,200,000
Expenses	<u>(1,490,000)</u>	<u>(1,800,000)</u>
Net income	<u>1,610,000</u>	<u>400,000</u>

Angola Company**Comparative Statement of Retained Earnings
Years ended December 31, 2008 and 2007**

	2008	2007
Retained earnings - January 1	1,250,000	1,000,000
Net income	1,610,000	400,000
Dividends paid	(500,000)	(150,000)
Retained earnings - December 31	<u>2,360,000</u>	<u>1,250,000</u>

Problem 5-24**Martha Company****Statement of Changes in Equity
Year ended December 31, 2008**

	Share				
	RE	TS	Ordinary	Preference	premium
Balances - January 1	3,250,000	10,000,000			7,500,000
Issuance of preference 400,000				5,000,000	
Purchase of treasury - ordinary				320,000	
Issuance of ordinary		2,500,000			3,500,000
Dividend to ordinary	(2,480,000)				
Reissuance of TS	50,000		(160,000)		
Dividend to preference	(450,000)				
Overstatement of 2007 ending inventory	(130,000)				
Net income					<u>2,250,000</u>
Balances - December 31	<u>2,440,000</u>	<u>160,000</u>	<u>12,500,000</u>	<u>5,000,000</u>	<u>11,450,000</u>

Problem 5-25

Carr Company

Statement of Changes in Equity
Year ended December 31, 2008

	Share		Ordinary	Preference	premium
	RE	TS			
Balances - January 1		5,150,000	1,800,000	3,590,000	4,000,000
Retirement of TS		(150,000)		(120,000)	
		(270,000)			
Property dividend		(750,000)			
Dividend to preference		(180,000)			
Error		(325,000)			
Net income					2,600,000
<u>Balances - December 31</u>		<u>5,000,000</u>	<u>1,800,000</u>	<u>3,470,000</u>	<u>5,345,000</u>
		<u>-</u>			

CHAPTER 6

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

Problem 6-4 Answer B

Property taxes (180,000 / 4)	
	45,000
Repairs - allocated to second, third and fourth quarters (300,000 / 3)	
	<u>100,000</u>
The expense for second quarter	
	<u>145,000</u>

Problem 6-5 Answer D

Depreciation	250,000	
Bonuses		<u>600,000</u> Total
	<u>850,000</u>	

Problem 6-6 Answer A

The casualty loss is reported in the period in which it is incurred. In this case, the loss is incurred in the third quarter.

Problem 6-7 Answer D

Net income per book	
	950,000
Gain from expropriation incorrectly allocated (600,000 / 3)	
	(200,000)
Change in accounting policy incorrectly deducted from income	
	<u>150,000</u>
Corrected net income	
	<u>900,000</u>

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Problem 6-8 Answer C

Advertising and bonuses are reported in the interim period when incurred.

PAS 34, paragraph 39, provides that cost incurred **unevenly** during a financial year shall be anticipated or deferred for interim purposes only if it is also appropriate to anticipate or defer such cost at the end of the financial year.

Problem 6-9 Answer A

Total warranty (10% x P25 million)	
	2,500,000
Warranty recognition in first quarter (5% x P10 million)	
	<u>500,000</u>
Warranty expense for second quarter	
	<u>2,000,000</u>

Problem 6-10 Answer B

First quarter - Gross income	
	5,000,000
Percentage of completion	
	<u>10%</u>

Income earned
500,000

Second quarter - No work done
0

Third quarter - Gross income 800,000
Percentage of completion
25%
Cumulative income 200,000
Income earned - FQ
(500,000)
Loss in TQ
(300,000)

Fourth quarter
0

Problem 6-11 Answer B

Problem 6-12 Answer B

Bad debt expense for the **entire year**
450,000

Bad debt expense:

First quarter (5% x 2,000,000)
100,000

Second quarter (5% x 1,500,000)
75,000

Third quarter (5% x 2,500,000)
125,000 300,000

Bad debt expense for fourth quarter
150,000

Problem 6-13 Answer A

First quarter:

Property taxes (600,000 / 4)
150,000

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Second, third and fourth quarter:
Property taxes

150,000

Major repairs, (2,400,000 / 3)	
	<u>800,000</u>
Total	<u>950,000</u>

Problem 6-14

Question 1 - Answer B

Using just the annual sales data, it appears that the annual sales are increasing by P10,000. Accordingly, the 2008 sales would be P60,000. A reasonable forecast of the fourth quarter sales would be P60,000 divided by 4 or P15,000.

Question 2 - Answer A

Using the quarterly sales data, it appears that the fourth quarter sales are increasing by P4,000. The best guess of the fourth quarter sales for 2008 would be P20,000 plus P4,000 or P24,000.

Question 3 - Answer C

Using the quarterly sales data, the first quarter sales appear to increase by P2,000. However, the actual increase in 2008 is twice as much from P10,000 to P14,000. If this trend continues, sales for the fourth quarter of 2008 would also be twice as much. Under this assumption, the best guess of the fourth quarter sales for 2008 would be P20,000 plus P8,000 or P28,000.

Problem 6-15 Answer A

Sales (30% x 6,000,000)	1,800,000
Cost of goods sold (60% x 1,800,000)	<u>(1,080,000)</u>
Gross income	720,000
Variable expense (30% x 400,000)	(120,000)
Fixed expenses (100,000 / 4)	(25,000)
Casualty loss	<u>(300,000)</u>
Income before tax	<u>275,000</u>

The gain on sale of equipment is reported in the **second quarter**, not in the third quarter, because the equipment is sold on June 1, 2008.

Problem 6-16

Chairmaine Company

Income Statement Three-month ended March 31, 2008

Sales		25,000,000
Cost of sales (60%)		
	<u>15,000,000</u>	
Gross income		10,000,000
Interest income (5,000,000 x 12% x 3/12)		
	<u>150,000</u>	
Total income		10,150,000
Selling expenses		(3,350,000)
Administrative expenses		
	<u>(3,050,000)</u>	
Income before tax		3,750,000
Income tax (35%)		
		<u>(1,312,500)</u>
Net income		<u><u>2,437,500</u></u>
Selling expenses		3,200,000
Depreciation (450,000 x 1/3)		
	<u>150,000</u>	
Total		<u><u>3,350,000</u></u>
Administrative expenses		2,400,000
Depreciation (450,000 x 2/3)		300,000
Insurance (400,000 / 4)		100,000
Doubtful accounts (25,000,000 x 1%)		
	<u>250,000</u>	
Total		<u><u>3,050,000</u></u>

Chairmaine Company**Balance Sheet
March 31, 2008****ASSETS**

Current assets:

Cash		
	1,000,000	
Trade and other receivables		
1,900,000		
Inventory		
3,500,000		
Prepaid insurance		
<u>300,000</u>		6,700,000

Noncurrent assets:

Note receivable		
5,000,000		
Property, plant and equipment		
<u>19,050,000</u>	<u>24,050,000</u>	
Total assets		<u>30,750,000</u>

64**LIABILITIES AND EQUITY**

Current liabilities:

Accounts payable		
8,500,000		
Income tax payable		
<u>1,312,500</u>		9,812,500

Shareholders' equity:

Share capital		
5,000,000		
Share premium		
4,000,000		
Retained earnings		
<u>11,937,500</u>	<u>20,937,500</u>	
Total liabilities and equity		<u>30,750,000</u>

Accounts receivable		2,000,000
Allowance for doubtful accounts		(250,000)

Accrued interest on NR		<u>150,000</u>
Total trade and other receivables		<u>1,900,000</u>
Inventory - 1/1		
		1,500,000
Purchases		<u>17,000,000</u>
GAS		18,500,000
Cost of sales		(<u>15,000,000</u>)
Inventory - 12/31		<u>3,500,000</u>
Land		1,500,000
Buildings and equipment	18,000,000	
Accumulated depreciation		(<u>450,000</u>)
Net book value		<u>19,050,000</u>
Retained earnings - 1/1		9,500,000
Net income		<u>2,437,500</u>
Balance - 12/31		<u>11,937,500</u>

Dunhill Company**Income Statement
Six-month ended June 30, 2008**

Sales	20,000,000
Cost of sales	<u>(11,500,000)</u>
Gross income	8,500,000
Interest revenue	250,000
Dividend revenue	<u>500,000</u>
Total income	9,250,000
Selling expenses	(2,500,000)
General expenses	(1,100,000)
Depreciation	(700,000)
Interest expense	<u>(300,000)</u>
Income before tax	4,650,000
Income tax expense	<u>(1,300,000)</u>
Net income	<u>3,350,000</u>

Dunhill Company**Income Statement
Three-month ended June 30, 2008**

Sales	12,500,000
Cost of sales	<u>(7,000,000)</u>
Gross income	5,500,000
Interest revenue	250,000
Dividend revenue	<u>200,000</u>
Total income	5,950,000
Selling expenses	(1,600,000)
General expenses	(600,000)

Depreciation	(300,000)
Interest expense	(200,000)
Income before tax	3,250,000
Income tax expense	(900,000)
Net income	<u>2,350,000</u>

Problem 6-18

First quarter (70% x 10,000,000)	7,000,000
Loss on inventory writedown	<u>100,000</u>
Cost of goods sold after inventory writedown	<u>7,100,000</u>

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First and second quarters (65% x 18,000,000)	11,700,000
Cost of goods sold for first quarter before inventory writedown	(7,000,000)
Cost of goods sold before reversal of writedown - second quarter	4,700,000
Gain on reversal of writedown	(100,000)
Cost of goods sold after reversal of writedown	<u>4,600,000</u>

Third quarter (70% x 7,000,000)	4,900,000
Loss on inventory writedown	<u>150,000</u>
Cost of goods sold after inventory writedown	<u>5,050,000</u>

Cost of goods sold for entire year (75% x 40,000,000)	30,000,000
Cost of goods sold before writedown and reversal:	

First quarter	(7,000,000)
Second quarter	(4,700,000)
Third quarter	(<u>4,900,000</u>)
Cost of goods sold before reversal of writedown - fourth quarter	13,400,000
Gain on reversal of writedown	(<u>150,000</u>)
Cost of goods sold after reversal of writedown - fourth quarter	<u>13,250,000</u>

sold	Gross income	Sales	Cost of goods
First quarter	10,000,000	7,100,000	
	2,900,000		
Second quarter	8,000,000	4,600,000	
	3,400,000		
Third quarter	7,000,000	5,050,000	
	1,950,000		
Fourth quarter	<u>15,000,000</u>	<u>13,250,000</u>	
	<u>1,750,000</u>		
Total	<u>40,000,000</u>	<u>30,000,000</u>	
	<u>10,000,000</u>		

Problem 7-1

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

Problem 7-3

- 1. C 6. D
- 2. B
- 3. B 8. D
- 4. B 9. C
- 5. B 10. C

Problem 7-2

- 1. D
- 2. B
- 7. B
- 3. D
- 4. C
- 5. B
- 6. C

Problem 7-4 Answer B

Sales to unaffiliated customers	20,000,000
Intersegment sales	<u>6,000,000</u>
Total segment revenue	<u>26,000,000</u>
Revenue criterion (10% x 26,000,000)	<u>2,600,000</u>

Problem 7-5 Answer B

	Total revenue	Percent
Alo	8,000	9.64%
Bix	12,000	14.46%
Cee	4,000	4.82%
Dil	<u>59,000</u>	<u>71.08%</u>
	<u>83,000</u>	<u>100.00%</u>

Only Bix and Dil have a revenue of 10% or more of the combined revenue. It is to be noted that the revenue includes both *sales to unaffiliated customers* and *intersegment sales*.

Problem 7-6 Answer C

	revenue	Profit	Assets	Total
A	30.53%	30.17%	29.63%	
B	24.14%	25.93%		24.43%
C	20.69%	18.52%		18.32%
D	9.48%	11.11%		9.16%
E	11.64%	10.37%		12.98%
F	<u>3.88%</u>	<u>4.44%</u>		<u>4.58%</u>
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>

A, B, C, D and E are reportable segments because their revenue or operating profit or asset is at least 10% of the combined amount.

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Problem 7-7 Answer B

	Profit	Operating loss	
V	3,400,000		
W	1,000,000		
X		2,000,000	
Y	400,000		
Z		<u>200,000</u>	
	<u>2,200,000</u>		<u>4,800,000</u>

The total profit figure is the basis for identifying the reportable segments because it is higher than the total loss figure. Accordingly, those segments with profit or loss of at least 10% of P4,800,000 or P480,000 are reportable. Thus, V, W and X are reportable.

Problem 7-8 Answer C

Sales - Segment Z
600,000

Segment expenses:

Traceable operating expenses	
350,000	
Allocated indirect operating expenses	
(600,000/2,400,000 x 360,000)	
<u>90,000</u>	<u>440,000</u>
Profit	
	<u>160,000</u>

Segment expense does not include administrative expenses, head office expenses and other expenses that arise at the enterprise level and relate to the enterprise as a whole.

Problem 7-9 Answer D

	Segment 1	Total revenue
Sales		
	3,000,000	7,500,000
Traceable costs		
	(1,750,000)	(5,000,000)
Profit before common cost		
	1,250,000	2,500,000
Common cost (1,250,000/2,500,000 x 1,500,000)		(750,000)
	<u>(1,500,000)</u>	
Segment profit		
	<u>500,000</u>	<u>1,000,000</u>

Problem 7-10 Answer C

Sales - Segment A		3,000,000
Expenses:		
Traceable operating costs		
1,900,000		
Allocated indirect costs (25% x 500,000)		<u>250,000</u>
	<u>2,025,000</u>	
Segment profit		
		<u>975,000</u>

Segment expense does not include interest expense, unless the segment's operations are primarily of a financial nature.

Problem 7-11

Question 1 - Answer A

10% x 50,000,000

5,000,000

AICPA FASB Statement No. 30, paragraph 6, provides that a *major customer disclosure* is required if an enterprise derives 10% or more of its revenue from a single customer or group of enterprises under common control.

Question 2 - Answer A

75% x 30,000,000

22,500,000

Problem 7-12 Answer D

Sales - Segment 1 (25% x 14,000,000)
3,500,000

Specific costs - Segment 1
(1,100,000)

Allocated common costs (25% x 6,500,000)
(1,625,000)

Operating profit
775,000

Problem 7-13

(Amounts in millions)

	Segment B	Others	Segment A Total
Sales	5,000 45,000	25,000	15,000
Segment expenses	(31,000)	(18,000)	(9,000) (4,000)
Segment result	<u>1,000</u> 14,000	<u>7,000</u>	<u>6,000</u>
General corporate expenses	(1,500)		
Interest expense		(500)	
Income before tax		12,000	
Income tax expense		(3,800)	
Net income		<u>8,200</u>	

Segment assets		<u>35,000</u>	<u>18,000</u>
<u>7,000</u>	60,000		
General corporate assets			
	<u>5,000</u>		
Total assets			<u>65,000</u>

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Problem 7-14

(Amounts in millions)

	Segment B	Others	Segment A Total
Sales		24,000	
27,000	9,000		60,000
Cost of goods sold		(9,800)	(14,000)
(4,200)	(28,000)		
Gross income		14,200	13,000
	4,800		32,000
Segment expenses		(4,800)	4,800)
(2,400)	(12,000)		
Depreciation		(1,200)	(1,350)
(450)	(3,000)		
Segment result		<u>8,200</u>	<u>6,850</u>
	<u>1,950</u>		17,000
General corporate expenses			
(2,000 + 1,000)			(3,000)
Income before tax			14,000
			14,000
Income tax expense			(4,000)
			<u>10,000</u>

Problem 7-15

	Computer	Others	Furniture Total	Stationery
External sales			800,000	500,000
	400,000	100,000	1,800,000	

Intersegment sales		<u>200,000</u>	<u>150,000</u>
<u>80,000</u>	<u>-</u>	<u>430,000</u>	
Total revenue		2,230,000	
Elimination of intersegment sales		(<u>430,000</u>)	
Enterprise revenue		1,800,000	
Cost of sales		(1,200,000)	
Distribution cost		(200,000)	
Administrative expenses		(<u>100,000</u>)	
Segment result		<u>150,000</u>	<u>75,000</u>
<u>60,000</u>	<u>15,000</u>	<u>300,000</u>	
Other income		60,000	
Other expenses		(50,000)	
Finance cost		(60,000)	
Share of profit of associate		<u>10,000</u>	
Income before tax		260,000	
Income tax		(<u>90,000</u>)	
Net income		<u>170,000</u>	
Segment assets		<u>440,000</u>	<u>170,000</u>
<u>100,000</u>	<u>5,000</u>	<u>715,000</u>	
Investment in associate		70,000	
General corporate assets		<u>15,000</u>	
Total assets		<u>800,000</u>	
Segment liabilities		<u>75,000</u>	<u>50,000</u>
<u>15,000</u>	<u>3,000</u>	<u>143,000</u>	
General corporate liabilities		<u>7,000</u>	
Total liabilities		<u>150,000</u>	

Problem 7-16

Operating segment (loss)	Operating assets	Segment revenue	Segment profit
	620,000	1	200,000
2			100,000
20,000		80,000	3
	340,000		70,000
300,000			190,000
4		140,000	5
(30,000)	180,000		(25,000)
180,000			70,000
6		120,000	
10,000			120,000
7		140,000	
(20,000)			<u>380,000</u>
Others		<u>140,000</u>	
(<u>25,000</u>)			
Total		<u>2,000,000</u>	
<u>200,000</u>	<u>1,500,000</u>		

1. The information above shows that any operating segment with revenue equal to or greater than P200,000 is a reportable segment (segments 1 and 3). Any segment with identifiable assets greater than P150,000 is a reportable segment (segments 1, 3, and 5). The total operating profit for all segments with operating profit totals P300,000. As a result, any segment with an operating profit or loss equal to or greater than an absolute amount of P30,000 is a reportable segment (segments 1, 3, and 4). Thus, Segments 1, 3, 4 and 5 are reportable segments.

2. The revenue of the reportable segments is as follows:

Segment 1	620,000	
3		340,000
4		190,000
	<u>180,000</u>	
Total revenue	<u>1,330,000</u>	
Percentage (1,330,000 / 2,000,000)	<u>66.5%</u>	

If the total external revenue attributable to reportable segments constitutes less than 75% of the total enterprise revenue, additional segments shall be identified even if they do not meet the 10% threshold until at least 75% of the enterprise revenue is included in reportable segments. Moreover, reportable segments that are below the 10% threshold can be aggregated as one segment if they share a majority of the five factors in identifying a business segment, namely:

- a. Nature of product
- b. Nature of production process
- c. Class of customer
- d. Method of distributing product
- e. Regulated environment

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Since Segments 6 and 7 are similar in **four** of the five criteria, they can be aggregated as one reportable segment.

Segment 6	Segment 7	Total	
Revenue			70,000
120,000	190,000		
Profit (loss)			10,000
(20,000)	(10,000)		
Segment assets			120,000
140,000	260,000		

With Segments 6 and 7 considered as one reportable segment, the total segment revenue increases to P1,520,000 or 76% of the total. The 75% requirement has been met.

Revenue of reportable segments before aggregation	1,330,000
Revenue of additional reportable segments	<u>190,000</u>
Total	<u>1,520,000</u>

Percentage (1,520,000 / 2,000,000)
76%

3. In conclusion, Segments 1, 3, 4, 5, and Segments 6 and 7 (combined) shall be considered reportable segments.

Problem 7-17

1. Primary reporting format about product lines:

	Product A	Product B	Total
Revenue			2,500,000
	6,000,000	8,500,000	
Segment result			650,000
	700,000	1,350,000	
Depreciation			350,000
	1,300,000	1,650,000	
Property plant and equipment			1,100,000
	4,000,000	5,100,000	
Segment assets			2,600,000
	10,000,000	12,600,000	
Segment liabilities			1,300,000
	6,000,000	7,300,000	
Capital expenditures			600,000
	1,300,000	1,900,000	

Secondary reporting format or supplemental information about geographical areas:

	Philippines	Japan	Total
Revenue			5,000,000
	3,500,000	8,500,000	
Segment result			750,000
	600,000	1,350,000	
Segment assets			7,200,000
	5,400,000	12,600,000	

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2. Primary reporting format about geographical areas:

	Philippines	Japan	Total
Revenue			5,000,000
	3,500,000	8,500,000	
Segment result			750,000
	600,000	1,350,000	

Depreciation			950,000
700,000	1,650,000		
Property, plant and equipment			3,000,000
2,100,000	5,100,000		
Segment assets			7,200,000
5,400,000	12,600,000		
Segment liabilities			4,700,000
2,600,000	7,300,000		
Capital expenditures			1,200,000
700,000	1,900,000		

Supplemental information about product lines:

	Product A	Product B	Total
Revenue			2,500,000
6,000,000	8,500,000		
Segment result			650,000
700,000	1,350,000		
Segment assets			2,600,000
10,000,000	12,600,000		

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CHAPTER 8

Problem 8-1

1. Sales on account

850,000

Add: Accounts receivable, January 1	<u>250,000</u>	
Total		
	1,100,000	
Less: Accounts receivable, December 31	<u>400,000</u>	
Collections on credit sales		700,000
Cash sales		
	<u>2,500,000</u>	
Total sales - cash basis		<u>3,200,000</u>

Sales on account		
	850,000	
Cash sales		
	<u>2,500,000</u>	
Total sales - accrual		
	<u>3,350,000</u>	

2. Purchases on account		400,000
Add: Accounts payable, January 1	<u>150,000</u>	
Total		
	550,000	
Less: Accounts payable, December 31	<u>200,000</u>	
Cash payments to creditors		350,000
Add: Cash purchases		
	<u>1,700,000</u>	
Purchases - cash basis		<u>2,050,000</u>
Purchases on account		400,000
Cash purchases		
	<u>1,700,000</u>	
Total purchases - accrual		<u>2,100,000</u>

3. Depreciation -		
on beginning balance (800,000 / 10 years)		80,000
on July 1 acquisition (200,000 / 10 years x 1/2)		<u>10,000</u>
Total		
	<u>90,000</u>	
4. Expenses paid - cash basis		750,000
Add: Accrued expenses, December 31		
	<u>20,000</u>	
Total		
	770,000	
Less: Prepaid expenses, December 31		
		<u>30,000</u>
Expenses - accrual		
	<u>740,000</u>	
5. Interest received - cash basis		40,000
Less: Accrued interest receivable, January 1		
	<u>10,000</u>	
Interest income - accrual		
		<u>30,000</u>

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	Accrual	Cash
Sales		<u>3,200,000</u>
	<u>3,350,000</u>	
Cost of sales:		
Inventory - January 1	500,000	500,000
Purchases		<u>2,050,000</u>
	<u>2,100,000</u>	
Goods available for sale	2,550,000	2,600,000
Less: Inventory - December 31		
	<u>600,000</u>	<u>600,000</u>

Cost of sales		
	<u>1,950,000</u>	<u>2,000,000</u>
Gross income	1,250,000	1,350,000
Interest income	<u>40,000</u>	<u>30,000</u>
Total income	<u>1,290,000</u>	<u>1,380,000</u>
Expenses:		
Depreciation	90,000	
90,000		
Expenses	<u>750,000</u>	
<u>740,000</u>		
Total		<u>840,000</u>
<u>830,000</u>		
Net income	<u>450,000</u>	<u>550,000</u>

Problem 8-2

**Aris Marval
Income Statement
Year ended December 31, 2008**

Professional fees		
	5,250,000	
Expenses:		
Rent		1,300,000
Supplies		850,000
Depreciation	250,000	
Other expenses	750,000	
Interest expense	<u>90,000</u>	<u>3,240,000</u>
Net income		
	<u>2,010,000</u>	

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Aris Marval
Balance Sheet
December 31, 2008

Assets

Current Assets		
Cash		1,500,000
Accounts receivable	750,000	
Office supplies unused	<u>250,000</u>	2,500,000
Noncurrent assets:		
Furniture and equipment	2,500,000	
Less: Accumulated depreciation	<u>375,000</u>	<u>2,125,000</u>
Total assets		<u>4,625,000</u>

Liabilities and Equity

Current liabilities:		
Note payable	1,000,000	
Accrued interest payable	90,000	
Accrued rent payable	<u>100,000</u>	1,190,000
Equity:		
Capital, January 1	2,275,000	
Add: Net income	<u>2,010,000</u>	
Total		4,285,000
Less: Withdrawals	<u>850,000</u>	<u>3,435,000</u>

Total liabilities and equity 4,625,000

Adjusting entries:

1. Depreciation (2,500,000 / 10 years)
250,000
Capital (1/2 x 250,000) 125,000
Accumulated depreciation 375,000

2. Interest expense (1,000,000 x 12% x 9/12)
90,000
Accrued interest payable 90,000

3. Accounts receivable 750,000
Professional fees 750,000
750,000
Professional fees 500,000
Capital 500,000
500,000

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4. Rent 100,000
Accrued rent payable 100,000

5. Office supplies unused 250,000
Supplies 250,000
Supplies 300,000
Capital 300,000

Problem 8-3

1. Sales		200,000
Retained earnings		
200,000		
Accounts receivable	250,000	
Sales		
	250,000	
2. Retained earnings		40,000
Sales		
	40,000	
3. Retained earnings		350,000
Purchases		
350,000		
Purchases		
		280,000
Accounts payable		
280,000		
4. Retained earnings		70,000
Expenses		
	70,000	
Expenses		
		100,000
Accrued expenses		
100,000		
5. Merchandise inventory, January 1, 2008		
150,000		
Retained earnings		
150,000		

	4,090,000	
Cost of sales:		
Merchandise inventory, January 1	150,000	
Purchases		<u>1,830,000</u>
Goods available for sale	1,980,000	
Less: Merchandise inventory, December 31	<u>210,000</u>	<u>1,770,000</u>
Gross income		2,320,000
Expenses:		
Expenses		1,530,000
Depreciation - equipment	20,000	
Depreciation - building	300,000	
Doubtful accounts		25,000
Interest expense		<u>36,000</u>
Net income		<u>1,911,000</u>
	<u>409,000</u>	

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Zamboanga Company Balance Sheet December 31, 2008

Assets

Current assets:		
Cash		1,500,000
Accounts receivable, net of allowance of P25,000		225,000
Advances to supplier	100,000	

Merchandise inventory			
	<u>210,000</u>		2,035,000
Noncurrent assets:			
Land			800,000
Building			
	1,500,000		
Less: Accumulated depreciation		<u>600,000</u>	
900,000			
Furniture and equipment			200,000
Less: Accumulated depreciation		<u>30,000</u>	
<u>170,000</u>	<u>1,870,000</u>		
Total assets			
	<u>3,905,000</u>		

Liabilities and Equity

Current liabilities:			
Accounts payable		280,000	
Accrued expenses		100,000	
Accrued interest payable			
	<u>36,000</u>		416,000
Noncurrent liability:			
Mortgage payable			900,000
Equity:			
Share capital			2,000,000
Retained earnings (Note 1)		<u>589,000</u>	<u>2,589,000</u>
Total liabilities and equity			<u>3,905,000</u>

Note 1 - Retained earnings

Adjusted retained earnings - January 1		180,000
Net income		
	<u>409,000</u>	
Retained earnings - December 31		<u>589,000</u>

Problem 8-4

1. Inventory - December 31, 2008		230,000
Income summary		

230,000

2. Accounts receivable

40,000

Sales

40,000

80

3. Doubtful accounts

15,000

Allowance for doubtful accounts

15,000

4. Depreciation

90,000

Accumulated depreciation - building

50,000

Accumulated depreciation - equipment

40,000

5. Purchases

30,000

Accounts payable

30,000

6. Retained earnings

5,000

Rent

5,000

7. Rent

10,000

Accrued rent payable

10,000

8. Insurance

7,000

Retained earnings

7,000

9. Prepaid insurance		12,000
Insurance		
	12,000	

Income Statement
Year ended December 31, 2008

Sales

		2,040,000	
Cost of sales:			
Inventory - January 1		150,000	
Purchases			<u>1,230,000</u>
Goods available for sale			1,380,000
Less: Inventory - December 31			<u>230,000</u>
Gross income		<u>1,150,000</u>	
	890,000		
Expenses:			
Office expenses		255,000	
Rent			245,000
Insurance			45,000
Supplies			140,000
Doubtful accounts			15,000
Depreciation			<u>90,000</u>
Net income			<u><u>790,000</u></u>
			<u><u>100,000</u></u>

Assets	
Current assets:	
Cash	200,000
Accounts receivable, net of allowance of P15,000	275,000
Inventory	230,000
Prepaid insurance	12,000
	<u>717,000</u>
Noncurrent assets:	
Land	300,000
Building	1,000,000
Less: Accumulated depreciation	<u>250,000</u>
750,000	
Equipment	400,000
Less: Accumulated depreciation	<u>80,000</u>
<u>320,000</u>	<u>1,370,000</u>
Total assets	<u><u>2,087,000</u></u>

Liabilities and Equity	
Current liabilities:	
Accounts payable	130,000
Accrued rent payable	10,000
	<u>140,000</u>
Equity:	
Share capital	1,500,000
Retained earnings (Note 1)	447,000
	<u>1,947,000</u>
Total liabilities and equity	<u><u>2,087,000</u></u>

Note 1 - Retained earnings

Retained earnings per book	345,000
Unrecorded accrued rent - December 31, 2007	
(5,000)	
Unrecorded prepaid insurance - December 31, 2007	
<u>7,000</u>	
Corrected beginning balance	347,000
Net income for 2008	

100,000

Retained earnings - December 31, 2008

447,000

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Problem 8-5

1. Merchandise inventory - December 31

500,000

Income summary

500,000

2. Accounts receivable

100,000

Sales

100,000

Purchases

80,000

Accounts payable

80,000

3. Expenses

20,000

Accrued expenses

20,000

4. Receivable from officer

10,000

Purchases

10,000

5. Sales

25,000

Advances from customer

	25,000	
6. Doubtful accounts (5% x 100,000)		
	5,000	
Allowance for doubtful accounts		5,000
7. Office supplies unused		
	5,000	
Expenses		
	5,000	
Equipment		100,000
Expenses		
	100,000	
Depreciation (100,000 / 10 x 6/12)		
	5,000	
Accumulated depreciation		5,000
Prepaid insurance (20,000 x 9/12)		
	15,000	
Expenses		
	15,000	
8. Interest expense		
	4,000	
Accrued interest payable (100,000 x 12% x 4/12)		
	4,000	

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**Civic Company
Income Statement
Year ended December 31, 2008**

Sales

	4,475,000	
Cost of sales:		
Purchases		4,270,000
Less: Inventory - December 31		
	<u>500,000</u>	<u>3,770,000</u>
Gross income	705,000	
Expenses:		
Expenses		460,000
Doubtful accounts		5,000
Depreciation		5,000
Interest expense		<u>4,000</u>
Net income		<u>474,000</u>
	<u>231,000</u>	

**Civic Company
Balance Sheet
December 31, 2008**

Assets

Current assets:		
Cash		840,000
Accounts receivable (Note 1)	95,000	
Receivable from officer	10,000	
Inventory		500,000
Prepaid expenses (Note 2)	<u>20,000</u>	1,465,000
Noncurrent asset:		
Equipment		100,000
Less: Accumulated depreciation	<u>5,000</u>	<u>95,000</u>
Total assets		<u>1,560,000</u>

Liabilities and Equity

Current liabilities:

Accounts payable		
	80,000	
Notes payable		200,000
Accrued expenses	20,000	
Advances from customer		
	25,000	
Accrued interest payable		
	<u>4,000</u>	329,000
Equity:		
Share capital		1,000,000
Retained earnings		
	<u>231,000</u>	<u>1,231,000</u>
Total liabilities and equity		<u>1,560,000</u>

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Note 1 - Accounts receivable

Accounts receivable	
	100,000
Allowance for doubtful accounts	(<u>5,000</u>)
Net realizable value	
	<u>95,000</u>

Note 2 - Prepaid expenses

Office supplies unused	
	5,000
Prepaid insurance	
	<u>15,000</u>
Total prepaid expenses	
	<u>20,000</u>

Problem 8-6 Answer B

Accounts receivable - January 1		
	400,000	
Revenue - accrual basis		<u>3,000,000</u>

Total		
	3,400,000	
Less: Accounts receivable - December 31	500,000	
Accounts written off		<u>20,000</u>
		<u>520,000</u>
Collections - revenue under cash basis		<u>2,880,000</u>

Problem 8-7 Answer A

Accounts receivable - December 31		
		650,000
Notes receivable - December 31		200,000
Collections from customers (cash basis)		2,300,000
Accounts written off		
	10,000	
Note discounted		
	<u>100,000</u>	
Total		

	3,260,000	
Less: Accounts receivable - January 1	500,000	
Notes receivable - January 1		<u>650,000</u>
	<u>150,000</u>	
Sales revenue - accrual basis		<u>2,610,000</u>

Problem 8-8 Answer B

Accounts receivable - December 31, 2008		
		300,000
Add: Sales in 2008 under cash basis		
		<u>1,750,000</u>
Total		

	2,050,000	
Less: Accounts receivable - December 31, 2007	<u>500,000</u>	
Sales - accrual basis		
	<u>1,550,000</u>	

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Problem 8-9 Answer C

Accounts receivable - December 31, 2008	600,000	
Collections from clients		<u>2,000,000</u>
Total		
	2,600,000	
Less: Accounts receivable - December 31, 2007	400,000	
	Unearned fees - December 31, 2008	
	<u>50,000</u>	<u>450,000</u>
Service revenue		
	<u>2,150,000</u>	

Problem 8-10 Answer D

Accounts receivable - December 31, 2007	1,000,000	
Add: Sales 2008		
	<u>4,600,000</u>	
Total		
	5,600,000	
Less: Accounts receivable - December 31, 2008	1,300,000	
	Writeoff	
		<u>20,000</u>
	<u>1,320,000</u>	
Collections - cash basis sales revenue		
	<u>4,280,000</u>	

Problem 8-11 Answer C

Accounts receivable - December 31, 2007	400,000	
Credit sales		
	<u>3,000,000</u>	

Total		
	3,400,000	
Less: Accounts receivable - December 31, 2008	<u>485,000</u>	
Collections		
	2,915,000	
Cash sales		
	<u>200,000</u>	
Total sales - cash basis		<u>3,115,000</u>

Problem 8-12 Answer A

Accounts receivable - January 1		
	200,000	
Add: Credit sales		
	<u>600,000</u>	
Total		
	800,000	
Less: Accounts receivable - December 31		
	150,000	
Sales discount		
	<u>30,000</u>	<u>180,000</u>
Collections		
	620,000	
Cash sales - net (400,000 - 20,000)		
	<u>380,000</u>	
Total sales - cash basis		<u>1,000,000</u>

Problem 8-13 Answer B

Accounts payable - 2008		
		700,000
Notes payable - 2008 (800,000 less 200,000 note payable to bank)		
	600,000	
Payment to suppliers		

2,200,000
Purchase discounts

50,000
Purchase returns

100,000
Total

3,650,000
Less: Accounts payable - 2007
500,000
Notes payable - 2007

300,000

800,000

Gross purchases

2,850,000

Problem 8-14 Answer D

Cash basis income

6,000,000
Add: Accounts receivable - 2008
4,000,000
payable - 2007
3,000,000 7,000,000
Total

Accounts

13,000,000
Less: Accounts receivable - 2007
2,000,000
Accounts payable - 2008
1,500,000 3,500,000

Accrual basis income

9,500,000

Problem 8-15 Answer C

Capital - February 1

200,000
Cash basis income for February and March
500,000

Total

700,000

Less: Withdrawals during March		
Capital - March 31	<u>100,000</u>	<u>600,000</u>

Problem 8-16 Answer D

Interest paid		
100,000		
Add: Prepaid interest - 2007		23,500
Interest payable - 2008		
<u>53,500</u>		
Total		
	177,000	
Less: Prepaid interest - 2008		
Interest payable - 2007	18,000	
	<u>45,000</u>	<u>63,000</u>
Interest expense		
<u>114,000</u>		

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Problem 8-17 Answer D

Insurance premium paid (squeeze)		460,000
Add: Prepaid insurance - January 1		<u>100,000</u>
Total		
	560,000	
Less: Prepaid insurance - December 31		<u>120,000</u>
Insurance expense		
<u>440,000</u>		

Problem 8-18 Answer C

Accrued salaries payable - January 1		
	40,000	
Add: Salaries expense		<u>420,000</u>
Total		
	460,000	
Less: Salaries paid		
<u>390,000</u>		
Accrued salaries payable - December 31	<u>70,000</u>	

Problem 8-19 Answer A

Interest paid		
	800,000	
Decrease in prepaid interest		100,000
Increase in accrued interest payable		<u>30,000</u>
Interest expense		
<u>930,000</u>		

Problem 8-20 Answer C

Royalties received		
	2,500,000	
Royalties receivable - 2008		800,000
Unearned royalties - 2007		<u>450,000</u>
Total		
	3,750,000	
Less: Royalties receivable - 2007		
	750,000	
Unearned royalties - 2008		
	<u>650,000</u>	<u>1,400,000</u>
Royalty revenue		
<u>2,350,000</u>		

Problem 8-21 Answer D

Rent received		
2,210,000		
Rent receivable - December 31		1,060,000
Rent receivable written off		
<u> 30,000</u>		
Total		
3,300,000		
Less: Rent receivable - January 1		<u> 800,000</u>
Accrual basis rental revenue		<u> 2,500,000</u>

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Problem 8-22 Answer B

Prepaid insurance (32,000 x 6/12)		16,000
Prepaid rent		
<u> 20,000</u>		
Total prepaid expenses - December 31, 2008		<u> 36,000</u>

Problem 8-23 Answer B

Balance per book		
990,000		
Add: Radio advertising accrued on December 31		
<u> 50,000</u>		
Total		
1,040,000		
Less: Prepaid newspaper advertising		<u> 60,000</u>
Advertising expense		
<u> 980,000</u>		

Problem 8-24 Answer A

Royalty expense (earned by artist in 2008)
500,000

Problem 8-25 Answer B

Prepaid insurance - March 31, 2008 (72,000 x 35/36)
70,000

Insurance expense per book 72,000

Prepaid insurance before adjustment 3,000

Total

75,000
Less: Prepaid insurance - March 31, 2008 70,000

Insurance expense
5,000

Problem 8-26 Answer C

December 1, 2007 - May 31, 2008 4,000,000

December 1, 2007 - December 31, 2007 (500,000)

Sales - January 1 to May 31, 2008 3,500,000

June 1, 2008 - November 30, 2008 3,250,000

December 1, 2008 - December 31, 2008 700,000

Total sales in 2008
7,450,000

Royalty revenue for 2008 (20% x 7,450,000)
1,490,000

Problem 8-27 Answer A

Cash received from tenants		8,000,000
Rentals receivable - 2008		1,240,000
Unearned rentals - 2007		<u>3,200,000</u>
Total		
	12,440,000	
Less: Rentals receivable - 2007	960,000	
Unearned rentals - 2008	<u>2,400,000</u>	<u>3,360,000</u>
Rental revenue for 2008		<u>9,080,000</u>

Problem 8-28 Answer A

Compensation expense per book		490,000
Add: Accrued salaries		18,000
Accrued bonus		
	<u>175,000</u>	
Total compensation expense		<u>683,000</u>

Problem 8-29 Answer D

Problem 8-30

Question 1 Answer D

Question 2 Answer D

Problem 8-31 Answer B

AR - 1/1		
	670,000	
Sales on account		
	<u>7,980,000</u>	
Total		
	8,650,000	
AR - 12/31		
	(<u>900,000</u>)	

Collections of AR

7,750,000

Inventory - 1/1

860,000

Purchases (**squeeze**)

5,750,000

Goods available

6,610,000

Inventory - 12/31

(780,000)

Cost of goods sold

5,830,000

90

Accounts payable - 1/1

530,000

Purchases

5,750,000

Total

6,280,000

Accounts payable - 12/31

(480,000)

Payment of AP

5,800,000

Cash - 1/1

620,000

Collections of AR

7,750,000

Total

	8,370,000	
Less: Payment of AP		
	5,800,000	
Payment of expenses		
	<u>1,070,000</u>	<u>6,870,000</u>
Cash - 12/31		
	<u>1,500,000</u>	

Problem 8-32 Answer A

Accrual sales

	5,000,000	
AR - January 1		
	800,000	
Advances from customer - December 31		
	<u>400,000</u>	
Total		

	6,200,000	
Less: AR - December 31		
	500,000	
Advances from customers - January 1		
	<u>300,000</u>	<u>800,000</u>
Cash received from customers		
		<u>5,400,000</u>

Problem 8-33

Question 1 - Answer B

Accounts receivable - 12/31/2008		1,350,000
Accounts written off		
	100,000	
Sales returns		
	150,000	
Cash receipts from customers		
		6,000,000
Sales discounts		
	<u>200,000</u>	
Total		

	7,800,000	
Accounts receivable - 12/31/2007		(1,200,000)
Erroneous debit to AR		(_____
<u>50,000)</u>		
Gross sales		
	<u>6,550,000</u>	

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Question 2 - Answer A

Accounts payable - 12/31/2008		1,850,000
Purchase returns		
50,000		
Payments to trade creditors		4,000,000
Purchase discounts		<u>300,000</u>
Total		
	6,200,000	
Accounts payable - 12/31/2007		(<u>1,500,000</u>)
Gross purchases		
	<u>4,700,000</u>	

Problem 8-34 Answer A

Net income - cash basis		1,101,000
Accrued revenue		
2007		
(91,000)	
2008		

	73,000	
Unearned revenue		
2007		66,000
2008		
	(108,000)	
Accrued expenses		
2007		49,000
2008		
	(65,000)	
Prepaid expenses		
2007		
	(46,000)	
	2008	
	<u>56,000</u>	
Net income - accrual basis		<u>1,035,000</u>

Problem 8-35

Question 1 - Answer C

Cash dividend from Kar

10,000

The cash dividend from AUB is a reduction of investment because the investment is 30%.

Question 2 - Answer D

Royalty revenue from January to June 2008 paid on
September 1, 2008

700,000

Royalty revenue from July to December 2008 (10% x 2,000,000)
200,000
Total royalty revenue
900,000

Question 3 - Answer C

Rent for 2008
480,000
Amortization of nonrefundable deposit (500,000 / 10)
50,000
Total rental revenue
530,000

	January 1	December 31
Total assets		6,000,000
	6,880,000	
Total liabilities		6,000,000
	<u>1,600,000</u>	
Capital	<u>2,120,000</u>	
	<u>3,880,000</u>	<u>5,280,000</u>
Capital - December 31		5,280,000
Add: Withdrawals		400,000
		<u>400,000</u>
Total		5,680,000
	5,680,000	
Less: Capital - January 1		3,880,000
	3,880,000	
Investment		<u>600,000</u>
Net income		<u>4,480,000</u>
	<u>1,200,000</u>	
Notes receivable - December 31		1,200,000
Accounts receivable - December 31		2,000,000
Collections of accounts receivable		3,000,000
Collections of notes receivable		960,000
Sales discount		100,000
	100,000	
Bad debts (accounts written off)		120,000
Sales returns		320,000
	<u>320,000</u>	
Total		7,700,000
	7,700,000	
Less: Notes receivable - January 1		400,000
	400,000	
Accounts receivable - January 1		<u>2,000,000</u>
	<u>1,600,000</u>	

Sales on account

5,700,000

Cash sales

800,000

Total sales

6,500,000

Notes payable - December 31

480,000

Accounts payable - December 31

1,040,000

Payment of accounts payable

1,520,000

Payments of notes payable

1,280,000

Purchase allowances

80,000

Total

4,400,000

Less: Notes payable - January 1

720,000

Accounts payable - January 1

1,200,000

1,920,000

Purchases on account

2,480,000

Cash purchases

600,000

Total purchases

3,080,000

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Rent received

80,000

Add: Unearned rent income - January 1

120,000

Total

200,000
Less: Unearned rent income - December 31
40,000

Rent income

160,000

Sales price

120,000
Less: Book value of equipment sold

100,000

Gain on sale of equipment

20,000

Equipment - January 1

1,200,000

Add: Acquisition

400,000

Total

1,600,000
Less: Equipment - December 31

1,120,000

Book value of equipment sold

100,000

1,220,000

Depreciation

380,000

Interest paid

160,000

Add: Accrued interest payable - December 31

40,000

Total

200,000

Less: Accrued interest payable - January 1

80,000

Interest expense

120,000

Lancer Store

**Income Statement
Year ended December 31, 2008**

Net sales revenue (Note 1)		6,080,000
Cost of sales (Note 2)		
	<u>3,640,000</u>	
Gross income		
	2,440,000	
Other income (Note 3)		<u>180,000</u>
Total income		
	2,620,000	
Expenses:		
Expenses		800,000
Bad debts		120,000
Depreciation		380,000
Interest expense	<u>120,000</u>	<u>1,420,000</u>
Net income		
	<u>1,200,000</u>	

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Note 1 - Net sales revenue

Sales		
	6,500,000	
Sales discount		
(100,000)		
Sales return		
(<u>320,000</u>)		
Net sales revenue		
	<u>6,080,000</u>	

Note 2 - Cost of sales

Inventory - January 1

1,600,000

Purchases

3,080,000

Purchase allowances

(80,000)3,000,000

Goods available for sale

4,600,000

Less: Inventory - December 31

960,000

Cost of sales

3,640,000**Note 3 - Other income**

Rent income

160,000

Gain on sale of equipment

20,000

Total

180,000**Problem 9-2**

Retained earnings - December 31

600,000

Add: Dividends

400,000

Total

1,000,000

Less: Retained earnings - January 1

500,000

Net income

500,000

Notes receivable - December 31

210,000

Accounts receivable - December 31

950,000

Collection of notes and accounts

2,950,000

Note receivable discounted		<u>200,000</u>
Total		
	4,310,000	
Less: Notes receivable - January 1	200,000	
	Accounts receivable - January 1	
	<u>740,000</u>	<u>940,000</u>
Sales on account		<u>3,370,000</u>
Interest on note discounted (200,000 - 190,000)		
	10,000	
Interest accrued on note issued to bank (300,000 x 12% x 10/12)		
	<u>30,000</u>	
Interest expense		
	<u>40,000</u>	

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Sales price		
	250,000	
Less: Cost of investment sold		<u>300,000</u>
Loss on sale of investment		
	(<u>50,000</u>)	
Notes payable - December 31		580,000
Less: Note payable - bank		<u>300,000</u>
Notes payable - trade		280,000
Accounts payable - December 31		750,000
Payment of notes and accounts		<u>2,100,000</u>
Total		
	3,130,000	
Less: Notes payable - January 1	750,000	

Accounts payable - January 1			
	<u>600,000</u>	<u>1,350,000</u>	
Purchases on account			<u>1,780,000</u>
Expenses paid			
	790,000		
Add: Prepaid expenses - January 1			
		120,000	
Accrued expenses - December 31			
			<u>50,000</u>
Total			
	960,000		
Less: Prepaid expenses - December 31			
	100,000		
Accrued expenses - January 1			
	<u>40,000</u>	<u>140,000</u>	
Expenses			
	<u>820,000</u>		
Equipment - January 1			1,000,000
Add: Acquisition			
	<u>280,000</u>		
Total			
	1,280,000		
Less: Equipment - December 31			
		<u>1,200,000</u>	
Depreciation			
	<u>80,000</u>		

Corolla Company
Income Statement
Year ended December 31, 2008

Sales			
	3,370,000		
Cost of sales:			
Inventory - January 1		1,600,000	
Purchases			<u>1,780,000</u>
Goods available for sale			
		3,380,000	

	Less: Inventory - December 31		
		<u>1,500,000</u>	<u>1,880,000</u>
Gross income			
1,490,000			
Expenses:			
Expenses			820,000
Depreciation			80,000
Loss on sale of investment			
Interest expense		50,000	
		<u>40,000</u>	<u>990,000</u>
Net income			
<u>500,000</u>			

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Problem 9-3

Total assets

1,590,000

Less: Total liabilities

460,000

Capital - January 1

1,130,000

Cash balance - January 1

200,000

Add: Deposits

3,930,000

Total

4,130,000

Less: Checks drawn

3,360,000

Bank service charge

10,000

3,370,000

Cash balance - December 31

760,000

Accounts payable - January 1

250,000

Add: Purchases

Total	<u>2,280,000</u>	
	2,530,000	
Less: Purchase returns		70,000
Payments		<u>2,200,000</u>
	<u>2,270,000</u>	
Accounts payable - December 31		<u>260,000</u>
Salaries paid		
	400,000	
Accrued salaries - December 31		<u>15,000</u>
Total		
	415,000	
Less: Accrued salaries - January 1		<u>10,000</u>
Salaries expense		
	<u>405,000</u>	
Supplies paid		
	75,000	
Add: Prepaid supplies - January 1		<u>40,000</u>
Total		
	115,000	
Less: Prepaid supplies - December 31		<u>20,000</u>
Supplies expense		
	<u>95,000</u>	
Taxes paid		
	<u>45,000</u>	
Miscellaneous expense paid		<u>35,000</u>
Other expenses paid		

245,000

Note payable - January 1

200,000

Less: Payment

120,000

Note payable - December 31

80,000

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Accounts receivable - December 31

450,000

Accounts collected

1,720,000

Accounts written off

30,000

Total

2,200,000

Less: Accounts receivable - January 1

420,000

Sales on account

1,780,000

Allowance for doubtful accounts - January 1

20,000

Add: Doubtful accounts expense (squeeze)

60,000

Total

80,000

Less: Accounts written off

30,000

Allowance for doubtful accounts - December 31

50,000

Total deposits

3,930,000

Less: Accounts receivable collected		
Cash sales		<u>1,720,000</u>
	2,210,000	
Add: Sales on account		<u>1,780,000</u>
Total sales		
	<u>3,990,000</u>	
Depreciation (350,000 x 10%)		<u>35,000</u>

Income Statement
Year ended December 31, 2008

Sales		
	3,990,000	
Cost of sales:		
Merchandise inventory - January 1	700,000	
Purchases	2,280,000	
Less: Purchase returns	<u>70,000</u>	<u>2,210,000</u>
Goods available for sale		2,910,000
Less: Merchandise inventory - December 31	<u>650,000</u>	<u>2,260,000</u>
Gross income		1,730,000
Expenses:		
Salaries		405,000
Supplies		
95,000		
Taxes		45,000
Other expenses		245,000
Doubtful accounts		60,000
Depreciation		35,000
Bank service charge		10,000

Miscellaneous expense		
	<u>35,000</u>	<u>930,000</u>
Net income		
	<u>800,000</u>	

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Balance Sheet
December 31, 2008

Assets

Current assets:		
Cash		760,000
Accounts receivable, net of allowance of P50,000		400,000
Merchandise inventory	650,000	
Prepaid supplies		
	<u>20,000</u>	1,830,000
Noncurrent assets:		
Equipment		350,000
Less: Accumulated depreciation		
	<u>135,000</u>	<u>215,000</u>
Total assets		
		<u>2,045,000</u>

Liabilities and Equity

Current liabilities:		
Accounts payable		260,000
Note payable		80,000
Accrued salaries payable		
	<u>15,000</u>	355,000
Equity:		
Capital - January 1	1,130,000	
Add: Net income		
	<u>800,000</u>	
Total		1,930,000
Less: Drawings		
	<u>240,000</u>	<u>1,690,000</u>

Total liabilities and equity 2,045,000

Problem 9-4

Collections on accounts receivable	3,000,000	
Collections on notes receivable		240,000
Sales returns and allowances (120,000 - 40,000)	80,000	
Increase in accounts receivable		<u>140,000</u>
Total		
	3,460,000	
Less: Decrease in notes receivable		<u>60,000</u>
Sales on account		
3,400,000		
Cash sales		
	<u>300,000</u>	
Total sales		
	<u>3,700,000</u>	

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Payments on accounts payable	1,650,000	
Purchase returns and allowances (80,000- 50,000)	30,000	
Increase in accounts payable		<u>40,000</u>
Purchases on account		
		1,720,000
Cash purchases		
	<u>100,000</u>	
Total purchases		

	<u>1,820,000</u>	
Insurance paid		
	70,000	
Less: Increase in prepaid insurance		<u>20,000</u>
Insurance expense		
	<u>50,000</u>	
New equipment acquired		80,000
Add: Decrease in equipment		<u>10,000</u>
Depreciation		
	<u>90,000</u>	
Salaries paid		
	1,000,000	
Less: Decrease in accrued salaries payable		<u>30,000</u>
Salaries expense		
	<u>970,000</u>	

**Ronald Company
Income Statement
Year ended December 31, 2008**

Net sales revenue (Note 1)	3,580,000
Cost of sales (Note 2)	
	<u>1,840,000</u>
Gross income	
	1,740,000
Interest income	
	<u>20,000</u>
Total income	
	1,760,000
Expenses:	

Insurance		50,000
Salaries		970,000
Depreciation	90,000	
Other expenses	<u>150,000</u>	<u>1,260,000</u>
Net income		
	<u>500,000</u>	

Note 1 - Net sales revenue

Sales		
	3,700,000	
Sales returns and allowances		(<u>120,000</u>)
Net sales revenue		
	<u>3,580,000</u>	

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Note 2 - Cost of sales

Purchases		
	1,820,000	
Purchase returns and allowances		(<u>80,000</u>)
Net purchases		
	1,740,000	
Decrease in inventory		<u>100,000</u>
Cost of sales		
	<u>1,840,000</u>	

on net assets	Effect
Decrease	Increase

Increase in cash	420,000	
Increase in accounts receivable		140,000
Increase in accounts payable		40,000
Increase in prepaid insurance		20,000
Decrease in inventory		100,000
Decrease in equipment		10,000
Decrease in notes receivable		60,000
Decrease in accrued salaries payable		<u>30,000</u>
	<u>210,000</u>	<u>610,000</u>

Net increase in net assets (610,000 - 210,000)
400,000

Add: Dividends

100,000

Net income

500,000

Problem 9-5

Balance per bank

250,000

Less: Outstanding checks

50,000

Adjusted bank balance

200,000

Cash investment

500,000

Proceeds of bank loan

500,000

Collection of accounts receivable (squeeze)

2,500,000

Total deposits

3,500,000

Less: Disbursements in check:		
Payment of loan	125,000	
Interest on loan		25,000
Equipment	400,000	
Interest on equipment	45,000	
Payment of accounts payable (squeeze)		
<u>2,705,000</u>	<u>3,300,000</u>	
Cash in bank - December 31		<u>200,000</u>

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The collection of accounts receivable and payment of accounts payable are "squeezed" by working back from the cash in bank.

Customers' deposit

75,000	Collections of accounts receivable (squeeze)	
		<u>600,000</u>

Total

	675,000	
Less: Disbursements in cash		<u>550,000</u>

Cash on hand - December 31

125,000

Accounts receivable - December 31

900,000

Collections deposited

2,500,000

Collections not deposited

600,000

Total sales

4,000,000

Accounts payable - December 31

350,000

Payments of accounts payable

2,705,000

Total purchases
3,055,000

Income Statement
Year ended December 31, 2008

Sales

4,000,000

Cost of sales:

Purchases

3,055,000

Less: Inventory - December 31

755,000 2,300,000

Gross income

1,700,000

Expenses:

Utilities

100,000

Salaries

100,000

Supplies

175,000

Taxes

25,000

Doubtful accounts

50,000

Depreciation - building (4,500,000 / 15)
300,000

Depreciation - equipment (400,000 / 5)
80,000

Interest expense (25,000 + 45,000)

70,000 900,000

Net income

800,000

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Balance Sheet
December 31, 2008

Assets	
Current assets:	
Cash (Note 1)	325,000
Accounts receivable (Note 2)	850,000
Inventory	<u>755,000</u>
1,930,000	
Noncurrent assets:	
Land	1,500,000
Building	4,500,000
Less: Accumulated depreciation	<u>300,000</u>
4,200,000	
Equipment	400,000
Less: Accumulated depreciation	<u>80,000</u>
<u>320,000</u>	<u>6,020,000</u>
Total assets	<u>7,950,000</u>

Liabilities and Equity	
Current liabilities:	
Accounts payable	350,000
Loan payable - bank	375,000
Customers' deposit	<u>75,000</u>
	800,000
Equity:	
Share capital	6,000,000
Share premium	500,000
Retained earnings (Note 3)	<u>650,000</u>
	<u>7,150,000</u>
Total liabilities and equity	<u>7,950,000</u>

Note 1 - Cash

Cash in bank
 200,000
Cash on hand

125,000
Total cash

325,000

Note 2 - Accounts receivable

Accounts receivable

900,000

Allowance for doubtful accounts

(50,000)

Net realizable value

850,000

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Note 3 - Retained earnings

Net income

800,000

Dividends

(150,000)

Total

650,000

Problem 9-6

Accounts receivable - December 31

200,000

Cash sales, collections and advances

3,030,000

Advances from customers - January 1

90,000

Total

3,320,000

Less: Accounts receivable - January 1

120,000

	Advances from customers - December 31	
	<u>50,000</u>	<u>170,000</u>
Sales		
	<u>3,150,000</u>	
Sales price		
	45,000	
Less: Book value of equipment sold		<u>20,000</u>
Gain on sale of equipment		
	<u>25,000</u>	
Accounts payable - December 31		
		100,000
Cash purchases and payments		<u>1,640,000</u>
Total		
	1,740,000	
Less: Accounts payable - January 1		<u>170,000</u>
Purchases		
	<u>1,570,000</u>	
Insurance paid		
	80,000	
Prepaid insurance - January 1		<u>35,000</u>
Total		
	115,000	
Less: Prepaid insurance - December 31		<u>25,000</u>
Insurance expense		
	<u>90,000</u>	
Depreciation:		
Building (2,000,000 x 10%)		200,000
Equipment (800,000 x 10%)		
80,000		
Equipment - new (200,000 x 10% x 3/12)		<u>5,000</u>

Total

285,000

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Salaries paid

390,000

Accrued salaries - December 31

30,000

Total

420,000

Less: Accrued salaries - January 1

20,000

Salaries expense

400,000

Doubtful accounts (5% x 200,000)

10,000

Income Statement
Year ended December 31, 2008

Sales

3,150,000

Cost of sales:

Inventory - January 1

230,000

Purchases

1,570,000

Goods available for sale

1,800,000

Less: Inventory - December 31

245,000

1,555,000

Gross income

1,595,000

Gain on sale of equipment

25,000

Total income

1,620,000

Expenses:

Insurance

90,000

Depreciation

285,000

Salaries

400,000

Doubtful accounts

10,000

Other expenses

135,000

920,000

Net income

700,000

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Balance Sheet December 31, 2008

Assets

Current assets:

Cash

905,000

Accounts receivable, net of allowance of P10,000

190,000

Inventory

245,000

Prepaid insurance

25,000

1,365,000

Noncurrent assets:

Land		500,000
Building	2,000,000	
Less: Accumulated depreciation		<u>900,000</u>
1,100,000		
Equipment	950,000	
Less: Accumulated depreciation		<u>295,000</u>
<u>655,000</u>	<u>2,255,000</u>	
Total assets		
	<u>3,620,000</u>	

Liabilities and Equity

Current liabilities:		
Accounts payable		100,000
Accrued salaries		30,000
Advances from customers	50,000	
Dividends payable		
	<u>125,000</u>	305,000
Equity:		
Share capital		2,500,000
Retained earnings		
	<u>815,000</u>	<u>3,315,000</u>
Total liabilities and equity		<u>3,620,000</u>
Accumulated depreciation - January 1	240,000	
Add: Depreciation for 2000		<u>85,000</u>
Total		
	325,000	
Less: Accumulated depreciation on equipment sold		<u>30,000</u>
Accumulated depreciation - December 31		<u>295,000</u>
Retained earnings - January 1		365,000
Net income		
	<u>700,000</u>	
Total		

	1,065,000	
Less: Dividends - June 30 (5% x 2,500,000)	125,000	
	Dividends - December 31	
	<u>125,000</u>	<u>250,000</u>
Retained earnings - December 31		<u>815,000</u>

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Problem 9-7 Answer B

Capital - December 31		2,400,000
Add: Withdrawals - merchandise at cost		
	<u>100,000</u>	
Total		
	2,500,000	
Less: Capital - January 1	1,700,000	
	Additional investment	
	<u>1,060,000</u>	<u>2,760,000</u>
Net loss		
	<u>(260,000)</u>	

The additional investment is determined as follows:

Payment of note payable out of <i>personal</i> checking account		
	1,000,000	
Interest (1,000,000 x 12% x 6/12)		
		<u>60,000</u>
Total		
	<u>1,060,000</u>	

Problem 9-8 Answer A

Stockholders' equity - December 31		4,000,000
Less: Contributed capital (2,000,000 + 1,200,000)		
	<u>3,200,000</u>	
Retained earnings - December 31		800,000
Add: Dividends		

Total	<u>800,000</u>	
	1,600,000	
Less: Retained earnings - January 1		<u>1,000,000</u>
Net income		
	<u>600,000</u>	

Problem 9-9 Answer D

on capital		Effect
Decrease		Increase
Decrease in cash		
480,000		
Increase in accounts receivable		
300,000		
Increase in inventory		
	3,100,000	
Increase in accounts payable		420,000
Increase in notes payable (4,000,000 - 3,000,000)		
	1,000,000	
Increase in accrued interest payable		
	<u>100,000</u>	
		<u>3,400,000</u>
	<u>2,000,000</u>	
Net increase in capital		1,400,000
Add: Withdrawals (10,000 x 52 weeks)		
	<u>520,000</u>	
Total		
	1,920,000	
Less: Additional investment (sale of marketable securities)		
	<u>1,500,000</u>	
Net income		
	<u>420,000</u>	

Problem 9-10 Answer C

Increase in assets

3,560,000

Increase in liabilities

1,080,000

Net increase

2,480,000

Add: Dividends

520,000

Total

3,000,000

Less: Increase in capital:

Common stock

2,400,000

Additional paid in capital

240,0002,640,000

Net income

360,000**Problem 9-11 Answer B**

Retained earnings - January 1 (squeeze)

900,000

Prior period adjustment:

Overstatement of 2007 inventory

(200,000)

Corrected beginning balance

700,000

Add: Net income

700,000

Total

1,400,000

Less: Dividends declared

400,000

Retained earnings - December 31 (4,000,000 - 3,000,000)

1,000,000**Problem 9-12 Answer A**

Retained earnings - January 1 (squeeze)		
	1,400,000	
Add: Net income	800,000	
	Prior period error of 2007 overdepreciation	
	<u>100,000</u>	<u>900,000</u>
Total		
	2,300,000	
Less: Dividend declared		<u>600,000</u>
Retained earnings - December 31		<u>1,700,000</u>

The beginning balance of retained earnings is “squeezed” by working back from the ending balance.

Total shareholders' equity - December 31		
	5,000,000	
Less: Share capital	3,000,000	
	Share premium from treasury shares	
	<u>300,000</u>	<u>3,300,000</u>
Retained earnings - December 31		<u>1,700,000</u>

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Problem 9-13 Answer A

Effect on equity		
Increase in assets		
	520,000	
Decrease in liabilities		
	<u>820,000</u>	
Net increase in equity		1,340,000
Shareholders' equity - beginning		
	<u>2,080,000</u>	

Shareholders' equity - ending	<u>3,420,000</u>
-------------------------------	------------------

Problem 9-14 Answer C

Total assets - December 31	880,000
Total liabilities - December 31	<u>390,000</u>
Shareholders' equity - December 31	490,000
Shareholders' equity - January 1	<u>380,000</u>
Net income	<u>110,000</u>

Since there are no dividends declared and issuance of share capital during the year, the net increase in shareholders' equity is already the net income for the year.

Problem 9-15 Answer B

Shareholders' equity (3,000,000 / 150%)	2,000,000
Contributed capital (1,000,000 + 500,000)	<u>(1,500,000)</u>
Retained earnings - December 31	<u>500,000</u>
Retained earnings - January 1 (squeeze)	1,300,000
Net loss	(100,000)
Dividends declared	<u>(700,000)</u>
Retained earnings - December 31	<u>500,000</u>

Problem 9-16 Answer A

Liabilities	1,200,000
Share capital	7,500,000
Retained earnings:	

Net income	1,000,000
Dividends	(<u>300,000</u>)
<u>700,000</u>	
Total liabilities and equity	<u>9,400,000</u>

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Problem 9-17 Answer A

Net increase in net assets	1,750,000
Dividend paid	
<u>1,500,000</u>	
Total	
3,250,000	
Increase in share capital	
	(700,000)
Increase in share premium	
Error	(300,000)
(<u>250,000</u>)	
Net income	
<u>2,000,000</u>	

Problem 9-18 Answer C

	Effect on equity
Increase in cash	
790,000	
Increase in AR	
240,000	
Increase in inventory	
1,270,000	
Decrease in investments	(470,000)

Decrease in accounts payable		380,000
Increase in bonds payable		(820,000)
Net increase in equity		1,390,000
Add: Dividend declared		<u>190,000</u>
Total		
	1,580,000	
Less: Increase in share capital	1,250,000	
	Increase in share premium	
	<u>130,000</u>	<u>1,380,000</u>
Net income		
	<u>200,000</u>	

Problem 9-19 Answer C

	Effect on equity	
Increase in cash		
	1,500,000	
Increase in AR		
	3,500,000	
Increase in inventory		
	3,900,000	
Decrease in investments		(1,000,000)
Increase in equipment		3,000,000
Decrease in accounts payable		800,000
Increase in bonds payable		(2,000,000)
Increase in bank loan payable		(4,000,000)
Increase in accrued interest payable		(<u>300,000</u>)
Net increase in equity		5,400,000
Add: Dividend paid		<u>4,500,000</u>
Total		

	9,900,000	
Less: Increase in share capital (100,000 x 30)	3,000,000	
	Increase in donated capital	
	<u>2,000,000</u>	<u>5,000,000</u>
Net income		
	<u>4,900,000</u>	

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Problem 9-20

Question 1 - Answer B

Accounts payable - December 31		750,000
Payments to trade creditors		<u>2,000,000</u>
Total purchases		
	2,750,000	
Less: Unadjusted debit balance of merchandise account	<u>700,000</u>	
Sales		
	<u>2,050,000</u>	

Question 2 - Answer A

Cash - 1/1 (Investment)		
	2,000,000	
Collections of AR (2,050,000 - 600,000)		<u>1,450,000</u>
Total		
	3,450,000	
Less: Payment of AP		
		2,000,000
	Payment of expenses	
		<u>100,000</u>
Cash - 12/31		<u>2,100,000</u>
	<u>1,350,000</u>	

Question 3 - Answer B

Sales

2,050,000

Cost of Sales:

Purchases

2,750,000

Merchandise inventory - 12/31 **(squeeze)**

(450,000)

2,300,000

Gross loss

(250,000)

Expenses

(100,000)

Net loss

(350,000)

The ending merchandise inventory is "squeezed" by working back from the net loss of P350,000.

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CHAPTER 10

Problem 10-1

Problem 10-2

1. C

6. B

1. C

2. B

7. C

2. B

3. B

8. C

3. C

4. A

9. D

4. D

5. A

10. A

5. A

Problem 10-3

2008

2007

Net income

1,500,000

1,600,000

Overstatement of inventory:

2007		(130,000)
130,000		
2008	(110,000)	
Understatement of accrued advertising:		
2007		(60,000)
60,000		
2008	(30,000)	
Understatement of accrued interest income:		
2007		40,000
(40,000)		
2008	60,000	
Omission of depreciation:		
2007		(80,000)
2008		
(<u>100,000</u>)		
Corrected net income	<u>1,270,000</u>	<u>1,570,000</u>

Adjusting entries - Books not closed

1. Retained earnings		
Inventory - January 1, 2008	130,000	
		130,000
Income summary		
Inventory - December 31, 2008	110,000	
		110,000
2. Retained earnings		
Advertising	60,000	
60,000		
Advertising		30,000

Accrued expenses

30,000

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3. Interest income

40,000

Retained earnings

40,000

Accrued interest receivable

60,000

Interest income

60,000

4. Retained earnings

80,000

Depreciation

100,000

Accumulated depreciation

180,000

Adjusting entries - Books closed

1. Retained earnings

110,000

Inventory - December 31, 2008

110,000

2. Retained earnings

30,000

Accrued expenses

30,000

3. Accrued interest receivable

60,000

Retained earnings

60,000

4. Retained earnings

180,000

Accumulated depreciation

180,000

Problem 10-4

	2008	2007
Net income		
	1,750,000	2,000,000
Salary accrued omitted:		
2007		(100,000)
100,000		
2008		
	(140,000)	
Inventory - December 31, 2007 overstated		(
190,000)	190,000	
Prepaid insurance unrecorded on December 31, 2008		
	120,000	
Interest receivable unrecorded on December 31, 2008		
	20,000	
Other income overstated		(160,000)
Depreciation overstated		
	<u>40,000</u>	
Corrected net income	<u>1,460,000</u>	<u>2,170,000</u>

Adjusting entries - December 31, 2008 - Book open

1. Retained earnings

100,000

Salaries

100,000

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Salaries

140,000

Accrued salaries payable

140,000

2. Retained earnings

190,000

Inventory – January 1, 2007		190,000
3. Prepaid insurance	120,000	
Insurance		
120,000		
4. Accrued interest receivable	20,000	
Interest income		
20,000		
5. Miscellaneous income	220,000	
Accumulated depreciation	240,000	
Equipment		
400,000		
Gain on sale of equipment		60,000
Accumulated depreciation	40,000	
Depreciation		
40,000		

Adjusting entries - December 31, 2008 - Books closed

1. Retained earnings	140,000	
Accrued salaries payable		140,000
2. No adjustment		
3. Prepaid insurance	120,000	
Retained earnings		
120,000		
4. Accrued interest receivable	20,000	
Retained earnings		

20,000	
5. Retained earnings	160,000
Accumulated depreciation	240,000
Equipment	
400,000	
Accumulated depreciation	40,000
Retained earnings	
40,000	

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Problem 10-5

	2008	2007
Net income		
	3,000,000	4,000,000
December 31, 2007 inventory understated		
20,000 (20,000)		
December 31, 2008 inventory overstated		
(18,000)		
Depreciation for 2007 understated		
(4,000) -		
Prepaid insurance unrecorded on 12/31/2007		
10,000 (5,000)		
Gain on sale of machinery		32,000
Corrected net income	<u>3,026,000</u>	<u>3,989,000</u>

Adjusting entries - December 31, 2008

1. Inventory - January 1, 2008	20,000
Retained earnings	
20,000	

2. Profit and loss		
Inventory - December 31, 2008	18,000	
		18,000
3. Retained earnings		
Accumulated depreciation	4,000	
		4,000
4. Prepaid insurance		
Insurance	5,000	
Retained earnings	5,000	
10,000		
5. Cash		
Accumulated depreciation		32,000
Machinery	200,000	
200,000		
Gain on sale of machinery		32,000

Problem 10-6

	2008	2007
Net income		
Collection of December 31, 2008 recorded in 2009	4,000,000	5,000,000
Unrecorded purchase in 2008	-	
Depreciation for 2007 understated	(90,000)	(160,000)
Office supplies charged to purchases in 2008	-	
Unrecorded sales in 2008		300,000
Corrected net income	<u>3,910,000</u>	<u>5,140,000</u>

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Adjusting entries - December 31, 2008

1. Cash		100,000
Accounts receivable		100,000
2. Purchases	160,000	
Accounts payable		160,000
3. Retained earnings	90,000	
Accumulated depreciation		90,000
4. Office supplies	20,000	
Purchases		20,000
5. Accounts receivable	300,000	
Sales		300,000

Problem 10-7

Net income reported in 2008	1,550,000
Prepaid insurance - December 31, 2008	10,000
Inventory on January 1, 2008 understated	(80,000)
Inventory on December 31, 2008 understated	120,000
Accrued taxes - December 31, 2008	(60,000)
Advances from customer - December 31, 2008	(<u>100,000</u>)

Corrected net income

1,440,000

Adjusting entries - December 31, 2008

1. Prepaid insurance		
Insurance	10,000	
	10,000	
2. Inventory - January 1, 2008	80,000	
Retained earnings		
	80,000	
3. Inventory - December 31, 2008	120,000	
Profit and loss		
	120,000	
4. Taxes		
Accrued taxes payable		60,000
		60,000
5. Sales		
Advances from customer		100,000
		100,000

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Problem 10-8

	Retained earnings	Working capital	Net income
	12/31/2008	2007	12/31/2008
1		(35,000)	35,000
2			
10,000		10,000	
	10,000		
3		25,000	-
		25,000	
4			(8,000)
	(8,000)		

5		5,000	(5,000)
6			
4,000		4,000	4,000
7			<u>(20,000)</u>
		<u>(20,000)</u>	<u>(20,000)</u>
Net correction	(<u>5,000</u>)	<u>16,000</u>	
<u>11,000</u>		(<u>6,000</u>)	

Net effect of errors

a. Net income 2008 understated		16,000
b. Retained earnings - December 31, 2008 understated		
	11,000	
c. Working capital - December 31, 2008 overstated		
	6,000	

Adjusting entries - December 31, 2008

1. Retained earnings		35,000
Inventory - January 1, 2008		35,000
2. Inventory - December 31, 2008		
Profit and loss	10,000	
10,000		
3. Accumulated depreciation		
Retained earnings	25,000	
25,000		
4. Depreciation		
Accumulated depreciation		8,000
8,000		
5. Insurance		
Retained earnings		5,000
5,000		

6. Unearned rent income		
Rent income	4,000	
	4,000	
7. Salaries		20,000
Accrued salaries payable		20,000

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Problem 10-9 Answer D

	2008	2007
Net income		
	550,000	700,000
Overstatement of inventory:		
2007		(29,000)
2008	29,000	
	(33,000)	
Omission of depreciation	(15,000)	(15,000)
Understatement of commission receivable:		
2007		22,000
2008	(22,000)	
	18,000	
Unrecorded 2007 purchase	(60,000)	60,000
Corrected net income	<u>468,000</u>	<u>737,000</u>

Problem 10-10 Answer B

The December 31, 2008 inventory was overstated. Therefore, cost of goods sold for 2008 was understated by P60,000 (P75,000 / 125%).

Problem 10-11 Answer C

January 1 inventory understated	26,000
December 31, inventory overstated	<u>52,000</u>
Cost of goods sold understated	<u>78,000</u>

If beginning inventory is understated, cost of goods sold is also understated.
If ending inventory is overstated, cost of goods sold is understated.

Problem 10-12 Answer B

Retained earnings - January 1, 2008	400,000
Understatement of prepaid insurance on December 31, 2007 (75,000 x 2/3)	50,000
Tax effect (30% x 50,000)	(15,000)
	<u>35,000</u>
Adjusted retained earnings - January 1, 2008	<u>435,000</u>

Problem 10-13 Answer A

Earnings per book	
5,000,000	
Prepaid insurance	
200,000	
Accrued wages	(
250,000)	
Rent revenue collected in advance	(300,000)
Interest receivable	
<u>100,000</u>	
Corrected earnings	<u>4,750,000</u>

Problem 10-14 Answer B

Retained earnings			
	2007	2008	January
1, 2009			
2007 inventory understated		200,000	(200,000)
		-	
2008 inventory overstated			
(300,000)		(300,000)	
2007 depreciation understated	(50,000)	
	(50,000)	
2008 depreciation overstated			
100,000		<u>100,000</u>	
Net decrease			
(<u>250,000</u>)			

Problem 10-15 Answer C

Retained earnings			
	2006	2007	January
1, 2008			
2006 inventory understated		60,000	
(60,000)			
2007 inventory overstated			=====
(<u>75,000</u>)	(<u>75,000</u>)		
Net correction			
<u>60,000</u>	(<u>135,000</u>)		(<u>75,000</u>)

Problem 10-16

1. **Answer A**
2. **Answer A**

capital	Net income	Working
	2007	2008
31, 2008		
2007 inventory understated		16,000
(16,000)		
2008 Inventory overstated		
(15,000)		(15,000)
		December

2007 depreciation understated	(6,000)	-
2007 prepaid insurance understated	10,000	(10,000)
2008 gain on sale of machinery		
<u>10,800</u>	<u>10,800</u>	
Net correction	(<u>30,200</u>)	(<u>4,200</u>)

Problem 10-17 Answer A

Net income per book		5,000,000
Unearned revenue		(200,000)
Loss on sale of equipment		(<u>150,000</u>)
Adjusted net income		<u>4,650,000</u>

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Problem 10-18 Answer A

Income before income tax		3,000,000
Inventory loss		
(<u>400,000</u>)		
Adjusted income before tax		<u>2,600,000</u>

Problem 10-19 Answer A

Problem 10-20 Answer B

Income per book		6,500,000
Unrecorded purchase		(1,000,000)
Understatement of ending inventory	1,500,000	

Unrecorded advertising		(500,000)
Unearned rent income (300,000 x 4/6)	(200,000)	
Prepaid insurance (200,000 x 6/12)	<u>100,000</u>	
Corrected income		<u>6,400,000</u>

Problem 10-21 Answer B

Retained earnings - 12/31/2008	1,940,000
Overstatement of 2008 ending inventory	(<u>300,000</u>)
Corrected balance - 12/31/2008	<u>1,640,000</u>

The inventory error in 2007 is counterbalanced in 2008 and therefore has no effect on retained earnings on December 31, 2008.

Problem 10-22 Answer A

	2007	2008
Income before tax		
	3,700,000	5,200,000
Ending inventory of 2007 understated (5,000 x 36)		180,000
(180,000)		
Purchase in transit in 2007, FOB shipping point, excluded from inventory	175,000	
(175,000)		
Merchandise sold in 2007 incorrectly included in inventory		
	(30,000)	
30,000		
Unrecorded purchase in 2007		
(15,000)	15,000	
Purchase on December 29, 2007, excluded from inventory		
	<u>15,000</u>	(
<u>15,000)</u>		
Corrected income	<u>4,025,000</u>	<u>4,875,000</u>

Problem 10-23

Question 1 - Answer A

	2008	2006	2007
Unrecorded commissions:			
2006		220,000	
2007	(220,000)		(140,000)
	140,000		
Ending inventory:			
2006 under		(400,000)	
400,000			
2007 over			(540,000)
	540,000		
2008 under			<u>150,000</u>
Net correction to income		<u>830,000</u>	
	<u>180,000</u>	<u>(860,000)</u>	
Net income per book for 2008			3,000,000
Net correction to income of 2008			<u>830,000</u>
Adjusted net income of 2008			<u><u>3,830,000</u></u>

Question 2 - Answer A

Net correction to income of 2006	180,000
Net correction to income of 2007	<u>(860,000)</u>
Net correction to income of prior years	<u>(680,000)</u>
Retained earnings - 1/1/2008	12,600,000
Prior period errors	(
<u>680,000)</u>	
Corrected beginning balance	11,920,000

Net income for 2008

3,830,000

Dividends declared in 2008

1,750,000)

Retained earnings - 12/31/2008

(
14,000,000)

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CHAPTER 11

Problem 11-1

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

Problem 11-2

- | |
|-------|
| 11. D |
| 6. D |
| 12. A |
| 7. A |
| 13. D |
| 8. A |
| 14. B |
| 9. B |
| 15. B |
| 10. D |

Problem 11-3

Accounts receivable - January 1

420,000

Add: Sales

4,500,000

Total

4,920,000

Less: Accounts receivable - December 31		
	<u>500,000</u>	
Collections from customers		<u>4,420,000</u>
Accounts payable - January 1		160,000
Purchases		
	<u>2,850,000</u>	
Total		
	3,010,000	
Less: Accounts payable - December 31		<u>280,000</u>
Payment to merchandise creditors		<u>2,730,000</u>
Salaries		
	600,000	
Add: Accrued salaries - January 1		<u>80,000</u>
Total		
	680,000	
Less: Accrued salaries - December 31		<u>50,000</u>
Payment for salaries		
	<u>630,000</u>	
Insurance		
	20,000	
Add: Prepaid insurance - December 31		<u>15,000</u>
Total		
	35,000	
Less: Prepaid insurance - January 1		<u>10,000</u>
Payment for insurance		
	<u>25,000</u>	

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Direct method

Cash received from customers		4,420,000
Cash payment to creditors		(2,730,000)
Salaries paid		
(630,000)		
Insurance paid		
25,000)		
Rent paid		
(250,000)		
Other expenses paid		
(<u>100,000</u>)		
Net cash provided by operating activities		<u>685,000</u>

Indirect method

Net income		
480,000		
Increase in accounts receivable		
(80,000)		
Decrease in inventory		150,000
Increase in prepaid insurance		
(5,000)		
Increase in accounts payable		120,000
Decrease in accrued salaries payable		
(30,000)		
Depreciation		
<u>50,000</u>		
Net cash provided by operating activities		<u>685,000</u>

Problem 11-4

Hill Company
Cash Flow Statement
Year ended December 31, 2008

Cash flow from operating activities:		
Net income	1,500,000	
Increase in accounts receivable (650,000)		
Increase in inventory (750,000)		
Decrease in prepaid expenses 50,000		
Increase in accounts payable 250,000		
Decrease in accrued expenses (150,000)		
Depreciation	<u>350,000</u>	600,000
Cash flow from investing activities:		
Purchase of equipment		(1,000,000)
Cash flow from financing activities:		
Issue of share capital	500,000	
Payment of cash dividend (300,000)	<u>200,000</u>	
Decrease in cash and cash equivalents (200,000)		
Cash and cash equivalents - January 1	<u>950,000</u>	
Cash and cash equivalents - December 31	<u><u>750,000</u></u>	

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Problem 11-5

Net loss		
(1,000,000)		
Purchase of trading securities	(500,000)	
Decrease in accounts receivable	400,000	
Increase in notes receivable	(100,000)	
Decrease in inventory		900,000

Decrease in prepaid expenses	200,000
Increase in accounts payable	250,000
Decrease in accrued expenses	(300,000)
Depreciation	
	<u>800,000</u>
Net cash provided by operating activities	<u>650,000</u>

Problem 11-6

Net income	
	2,120,000
Depreciation	
	240,000
Amortization of patent	
	80,000
Gain on sale of land	
(200,000)	
Decrease in accounts receivable	
	60,000
Increase in inventory	
(120,000)	
Decrease in accounts payable	
	(140,000)
Increase in accrued expenses	
	<u>160,000</u>
Net cash provided by operating activities	<u>2,200,000</u>

Problem 11-7

1. Accounts receivable - January 1	380,000
Sales	
	<u>3,850,000</u>
Total	
	4,230,000
Less: Accounts receivable - December 31	
400,000	

	Writeoff	<u>10,000</u>
	<u>410,000</u>	
	Collections from customers	<u>3,820,000</u>
2. Accounts payable - January 1		
	Purchases	240,000
	<u>2,200,000</u>	
	Total	
	2,440,000	
	Less: Accounts payable - December 31	
	<u>300,000</u>	
	Payment to creditors	<u>2,140,000</u>

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Inventory - January 1		910,000
Purchases (squeeze)		<u>2,200,000</u>
Goods available for sale		3,110,000
Less: Inventory - December 31		<u>840,000</u>
Cost of sales		
	<u>2,270,000</u>	

3. Salaries

	580,000	
Salaries payable - January 1		<u>100,000</u>
Total		
	680,000	
Less: Salaries payable - December 31		<u>70,000</u>

Salaries paid

610,000

4. Other expenses paid

290,000

Add: Prepaid expenses - December 31

50,000

Total

340,000

Less: Prepaid expenses - January 1

40,000

Other expenses paid

300,000

Original entries affecting noncurrent accounts

1. Profit and loss

460,000

Retained earnings

460,000

Retained earnings

170,000

Cash

170,000

2. Cash

60,000

Accumulated depreciation

140,000

Equipment

200,000

3. Equipment (2,550,000 - 2,000,000)

550,000

Cash

550,000

4. Note payable - bank

250,000

Cash

250,000

5. Cash		200,000
Share capital		
200,000		
6. Depreciation (100,000 + 140,000)		
240,000		
Accumulated depreciation		240,000

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Forever Company Cash Flow Statement Year ended December 31, 2008

Cash flow from operating activities:		
Collections from customers		3,820,000
Payment to creditors		
(2,140,000)		
Salaries paid		
(610,000)		
Other expenses		
(<u>300,000</u>)		
Net cash provided by operating activities		770,000
Cash flow from investing activities:		
Sale of equipment		60,000
Purchase of equipment		(550,000)
		(490,000)
Cash flow from financing activities:		
Issue of share capital		200,000
Payment of note payable - bank		(250,000)
Payment of cash dividend		(<u>170,000</u>)
		(<u>220,000</u>)
Increase in cash and cash equivalents		60,000
Cash and cash equivalents - January 1		<u>130,000</u>

Cash and cash equivalents - December 31
190,000

Indirect method

Net income		
460,000		
Increase in accounts receivable	(20,000)	
Decrease in inventory		
70,000		
Increase in prepaid expenses	(10,000)	
Increase in accounts payable		60,000
Decrease in salaries payable	(30,000)	
Depreciation		
<u>240,000</u>		
Net cash provided by operations		<u>770,000</u>

Problem 11-8

1. Accounts receivable - January 1		210,000
Sales		
	<u>4,450,000</u>	
Total		
	4,660,000	
Less: Accounts receivable - December 31		
370,000		
Writeoff		<u>20,000</u>
<u>390,000</u>		
Collections		
	<u>4,270,000</u>	

2. Accounts payable - January 1		
		345,000
Purchases		
	<u>2,630,000</u>	
Total		
	2,975,000	
Less: Accounts payable - December 31		
		<u>400,000</u>
Payment to creditors		<u>2,575,000</u>

3. Salaries		
	640,000	
Salaries payable - January 1		
		<u>40,000</u>
Total		
	680,000	
Less: Salaries payable - December 31		
		<u>70,000</u>
Salaries paid		
	<u>610,000</u>	

4. Insurance		
	100,000	
Add: Prepaid insurance - December 31		
		<u>80,000</u>
Total		
	180,000	
Less: Prepaid insurance - January 1		
		<u>90,000</u>
Insurance paid		
	<u>90,000</u>	

5. Rent paid	
	<u>350,000</u>

6. Interest expense	
	40,000
Less: Accrued interest payable - December 31	
	<u>5,000</u>

Interest paid

35,000

7. Income tax

200,000

Add: Income tax payable - January 1

15,000

Total

215,000

Less: Income tax payable - December 31

35,000

Income tax paid

180,000

Original entries

1. Retained earnings

160,000

Cash

160,000

Profit and loss

500,000

Retained earnings

500,000

2. Cash

110,000

Accumulated depreciation

140,000

Equipment

190,000

Gain on sale of equipment

60,000

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Depreciation (840,000 - 580,000)

260,000

Accumulated depreciation	260,000
3. Equipment (4,300,000 - 3,430,000)	
870,000	
Cash	
870,000	
4. Cash	600,000
Bonds payable	
600,000	
5. Treasury share	
Cash	140,000
140,000	

**Sandy Company
Cash Flow Statement
Year ended December 31, 2008**

Cash flow from operating activities:	
Collections from customers	4,270,000
Payments to creditors	(2,575,000)
Salaries paid	(610,000)
Insurance paid	(90,000)
Rent paid	(<u>350,000</u>)
Cash generated from operations	645,000
Interest paid	(35,000)
Income tax paid	(<u>180,000</u>)
Net cash provided by operating activities	430,000
Cash flow from investing activities:	
Sale of equipment	110,000
Purchase of equipment	(<u>870,000</u>)
	(760,000)
Cash flow from financing activities:	

Issue of bonds payable	600,000	
Payment of cash dividend	(160,000)	
Payment of treasury stock	(140,000)	<u>300,000</u>
Decrease in cash and cash equivalents	(30,000)	
Cash and cash equivalents - January 1		<u>150,000</u>
Cash and cash equivalents - December 31		<u>120,000</u>

129 Indirect method

Net income		
500,000		
Increase in accounts receivable	(160,000)	
Increase in inventory		(
230,000)		
Decrease in prepaid expenses		10,000
Increase in accounts payable		55,000
Decrease in salaries payable		30,000
Increase in income tax payable		20,000
Increase in accrued interest payable	5,000	
Depreciation		
260,000		
Gain on sale of equipment		(
<u>60,000)</u>		
Net cash provided by operations		<u>430,000</u>

Problem 11-9

Original entries

1. Profit and loss
Retained earnings 1,705,000
1,705,000
2. Retained earnings
Cash 1,000,000
1,000,000
3. Interest expense (100,000 / 10)
Discount on bonds payable 10,000
10,000

Bonds payable 200,000
Loss on retirement 28,000
Cash (200,000 x 105)
210,000
Discount on bonds payable (90,000 x 200/1,000)
18,000
4. Cash (4,000 x 30)
Ordinary share capital (4,000 x 20) 120,000
Share premium 80,000
40,000
5. Preference share capital (1,000 x 100)
100,000
Ordinary share capital (2,000 x 20)
Share premium 40,000
60,000

6. Trading securities		
Unrealized gain	100,000	
100,000		
	130	
7. Accounts receivable		
Sales	80,000	
80,000		
8. Inventory		
Cost of sales		60,000
60,000		
9. Depreciation		
Accumulated depreciation	100,000	
		100,000
10. Accounts payable		
Cash	310,000	
310,000		
11. Expenses		
Accrued expenses		100,000
100,000		

Financing

Operating

1. Net income	1,705,000
2. Cash dividend	
(1,000,000)	

3. Amortization of discount on bonds payable		
	10,000	
Retirement of bonds payable		(210,000)
Loss on retirement		
	28,000	
4. Issuance of ordinary share capital		120,000
5. Conversion of preference share into ordinary share - no cash effect		
6. Unrealized gain		(100,000)
7. Increase in accounts receivable		(80,000)
8. Increase in inventory		(60,000)
9. Depreciation	100,000	
10. Decrease in accounts payable	(310,000)	
11. Increase in accrued expenses	100,000	
	<u>1,393,000</u>	
Net cash provided (used)		<u>(1,090,000)</u>

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**Forest Company
Cash Flow Statement
Year ended December 31, 2008**

Cash flow from operating activities:		
Net income		1,705,000
Amortization of discount		10,000
Loss on retirement		28,000
Increase in accounts receivable		(80,000)

Increase in inventory		
Depreciation	(60,000)	
Unrealized gain		100,000
Decrease in accounts payable	(100,000)	
Increase in accrued expenses		100,000
	<u>100,000</u>	1,393,000
Cash flow from financing activities:		
Issue of ordinary share capital		120,000
Payment of cash dividend	(1,000,000)	
Bond retirement	(210,000)	(1,090,000)
Increase in cash and cash equivalents		<u>303,000</u>
Add: Cash and cash equivalents - January 1		<u>300,000</u>
Cash and cash equivalents - December 31		<u><u>603,000</u></u>

Problem 11-10

Original entries

1. Profit and loss		
Retained earnings		3,050,000
	3,050,000	
2. Retained earnings		
Cash	2,500,000	
		2,500,000
3. Cash		
Accumulated depreciation		70,000
Equipment	150,000	
Gain on sale of equipment	200,000	

20,000		
Depreciation (1,050,000 - 650,000)		
400,000		
Accumulated depreciation		400,000

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4. Cash (10,000 x 150)	1,500,000	
Share capital		
1,000,000		
Share premium		
500,000		
5. Cash		900,000
Treasury share		
700,000		
Share premium		
200,000		
6. Bonds payable		
Share capital	500,000	
	(2,500 x 100)	
250,000		
Share premium		
250,000		
7. Equipment		1,200,000
Cash		
	1,200,000	

8. Land		500,000
	Note payable - long term	500,000
9. Cash		100,000
	Accounts receivable	100,000
10. Inventory		150,000
	Cost of sales	150,000
11. Investment in Hall Company		
	200,000	
	Investment income	200,000
12. Purchases		
	Accounts payable	50,000
		50,000

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	Operating	Investing
Financing		
1. Net income	3,050,000	
2. Cash dividend		

	(2,500,000)	
3. Sale of equipment	70,000	
Gain on sale of equipment		(
20,000)		
Depreciation	400,000	
4. Issuance of share capital		1,500,000
5. Sale of treasury share		900,000
6. Conversion of bonds payable into ordinary share - no cash effect		
7. Purchase of equipment	(1,200,000)	
8. Purchase of land by issuing a note - no cash effect		
9. Decrease in accounts receivable		100,000
10. Increase in inventory		(
150,000)		
11. Investment income		(
200,000)		
12. Increase in accounts payable		<u>50,000</u>
<u>Net cash provided (used)</u>	<u>3,230,000</u>	<u>(1,130,000)</u> <u>(100,000)</u>

**Fearsome Company
Cash Flow Statement
Year ended December 31, 2008**

Cash flow from operating activities:		
Net income		3,050,000
Gain on sale of equipment	(20,000)
Depreciation		400,000
Decrease in accounts receivable		100,000
Increase in inventory	(150,000)
Investment income	(200,000)
Increase in accounts payable		<u>50,000</u>
		3,230,000
Cash flow from investing activities:		

Sale of equipment		70,000
Purchase of equipment	(1,200,000)	(1,130,000)
Cash flow from financing activities:		
Issue of share capital	1,500,000	
Sale of treasury share	900,000	
Payment of cash dividend	(2,500,000)	(100,000)
Increase in cash and cash equivalents		2,000,000
Add: Cash and cash equivalents - January 1		<u>350,000</u>
Cash and cash equivalents - December 31		<u>2,350,000</u>

134 Problem 11-11

Original entries

1. Profit and loss		1,095,000
	Retained earnings	
		1,095,000
2. Retained earnings (21,000 x 15)		
	315,000	
	Share capital (21,000 x 5)	
	Share premium	105,000
		210,000
3. Land		
	Share capital (19,000 x 5)	200,000
	Share premium	95,000
		105,000

4. Bonds payable		
	Cash	500,000
	450,000	
	Gain on bond retirement	50,000
5. Cash		95,000
	Accumulated depreciation	
	150,000	
	Loss on sale of equipment	
	Equipment	20,000
	265,000	
6. Retained earnings (250,000 x 2)		
	500,000	
	Cash	
	500,000	
7. Land		425,000
	Cash	
	425,000	
8. Accounts receivable		
	Sales	350,000
	350,000	
9. Inventory		
	Cost of sales	100,000
	100,000	
10. Depreciation (450,000 - 350,000)		
	100,000	
	Accumulated depreciation	100,000
11. Amortization of patent		
	Patent	15,000

Year ended December 31, 2008

Cash flow from operating activities:		
Net income		1,095,000
Gain on bond retirement		
(50,000)		
Loss on sale of equipment	20,000	
Increase in accounts receivable		
(350,000)		
Increase in inventory	(100,000)	
Depreciation		100,000
Amortization of patent	15,000	
Increase in accounts payable		350,000
350,000		
Increase in accrued expenses	<u>250,000</u>	1,330,000
Cash flow from investing activities:		
Sale of equipment	95,000	
Purchase of land	<u>(425,000)</u>	(330,000)
Cash flow from financing activities:		
Retirement of bonds payable	(450,000)	
Cash dividend	<u>(500,000)</u>	<u>(950,000)</u>
Increase in cash and cash equivalents	50,000	
Add: Cash and cash equivalents - January 1	<u>450,000</u>	
Cash and cash equivalents - December 31		<u>500,000</u>

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Problem 11-12

Original entries

1. Profit and loss	305,000	
Retained earnings		305,000
Retained earnings	85,000	

	Cash		
		85,000	
2.	Cash		18,000
	Accumulated depreciation		
		17,000	
	Loss on sale of equipment		
		10,000	
	Equipment		
		45,000	
3.	Cash		260,000
	Share capital		
		200,000	
	Share premium		
		60,000	
4.	Equipment		120,000
	Cash		
		120,000	
5.	Investment in Word Company		
		30,000	
	Investment income		
		30,000	
	Cash		
			20,000
	Investment in Word Company		
			20,000
6.	Accounts receivable		
		35,000	
	Sales		
		35,000	
7.	Cost of sales		80,000
	Inventory		

	80,000		
8. Depreciation		82,000	
Accumulated depreciation			82,000
Accumulated - 2008			345,000
Accumulated - 2007 (280,000 - 17,000)			
		<u>263,000</u>	
Depreciation for 2008			<u>82,000</u>

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9. Amortization		250,000	
Patent			
	250,000		
10. Accounts payable		135,000	
Cash			
	135,000		
11. Notes payable - long term		300,000	
Cash			
	300,000		
12. Income tax		20,000	
Deferred tax liability			
	20,000		

	Operating	Investing
Financing		
1. Net income		
Cash dividend		
305,000		
(85,000)		
2. Sale of equipment		
Loss on sale of equipment	18,000	10,000
3. Issue of share capital		
	260,000	
4. Purchase of equipment		
(120,000)		
5. Investment income		
(30,000)		
Cash dividend received from equity investee		
20,000		
6. Increase in accounts receivable		(35,000)
7. Decrease in inventory		80,000
8. Depreciation		
82,000		
9. Amortization of patent		
250,000		
10. Decrease in accounts payable		(135,000)
11. Payment of long term note		
	(300,000)	
12. Increase in deferred tax liability		<u>20,000</u>
Net cash provided (used)	<u> </u>	<u> </u>
<u>567,000</u>	<u>(102,000)</u>	<u>(125,000)</u>

Year ended December 31, 2008

Cash flow from operating activities:		
Net income		305,000
Loss on sale of equipment	10,000	
Investment income	(30,000)	
Cash dividend received from equity investee		
Increase in accounts receivable	(35,000)	
Decrease in inventory	80,000	
Depreciation		82,000
Amortization of patent	250,000	
Decrease in accounts payable	(135,000)	
Increase in deferred tax liability	<u>20,000</u>	567,000
Cash flow from investing activities:		
Sale of equipment		18,000
Purchase of equipment	<u>(120,000)</u>	(102,000)
Cash flow from financing activities:		
Cash dividend		(85,000)
Issue of share capital	260,000	
Payment of long term note	<u>(300,000)</u>	<u>(125,000)</u>
Increase in cash and cash equivalents		340,000
Cash and cash equivalents - January 1		<u>300,000</u>
Cash and cash equivalents - December 31		<u>640,000</u>

Problem 11-13

Original entries

1. Profit and loss	790,000
Retained earnings	

790,000		
2. Retained earnings		
	500,000	
Dividends payable		
500,000		
Dividends payable		
	340,000	
Cash (500,000 - 160,000)		
		340,000

3. Cash		350,000
Accumulated depreciation		
Equipment	250,000	
600,000		

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4. Cash		90,000
Loss on sale of investment		
Noncurrent investment	10,000	
		100,000
5. Short term investments		
Cash	200,000	
	200,000	
6. Cash		20,000
Accounts receivable		
		20,000
7. Inventory		
Cost of sales	100,000	
100,000		

8. Property, plant and equipment		
	1,300,000	
	Cash	
		1,300,000
Net increase in property, plant and equipment		700,000
Add: Cost of equipment sold		
		<u>600,000</u>
Total increase		
	<u>1,300,000</u>	
9. Depreciation		
		300,000
	Accumulated depreciation	
		300,000
Net increase in accumulated depreciation		50,000
Add: Accumulated depreciation on equipment sold		
		<u>250,000</u>
Deprecation		
	<u>300,000</u>	
10. Accounts payable		
		5,000
	Cash	
		5,000
11. Cash		
		300,000
	Short term debt	
		300,000
12. Cash		
		130,000
	Long term debt	
		130,000
13. Cash		
		225,000
	Share capital	
		150,000
		Share premium
		75,000

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	Operating	Investing	
Financing			
1. Net income			
	790,000		
2. Dividend paid (500,000 - 160,000)		(340,000)	
3. Sale of equipment			
	350,000		
4. Sale of investment			
	90,000		
Loss on sale of investment			
10,000			
5. Short term investments	(200,000)		
6. Decrease in accounts receivable		20,000	
7. Increase in inventory			
(100,000)			
8. Purchase of property, plant and equipment			
	(1,300,000)		
9. Depreciation			
300,000			
10. Decrease in accounts payable		(5,000)	
11. Proceeds from short term debt			
300,000			
12. Proceeds from long term debt			
		130,000	
13. Issue of share capital			
	225,000		
<u>Net cash provided (used)</u>			<u>1,015,000</u>
<u>(1,060,000)</u>	<u>315,000</u>		

Operating

1,015,000
Investing

(1,060,000)
Financing

315,000

Net increase in cash and cash equivalents
270,000

Problem 11-14

Original entries

1. Profit and loss

Retained earnings 2,900,000

2,900,000

Cash

3,300,000

Loss from condemnation

300,000

Land

3,600,000

2. Patent

Cash

680,000

680,000

Amortization of patent

120,000

Patent

120,000

3. Property, plant and equipment

5,800,000

Cash

5,800,000

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Net increase in property, plant and equipment

2,200,000

Add: Cost of land disposed of

3,600,000

Total increase

5,800,000

Operating	
4,250,000	
Investing	
(3,180,000)	
Financing	
(<u>870,000</u>)	
Net increase in cash and cash equivalents	<u>200,000</u>

The net increase in cash is actually the increase in working capital because all current assets and current liabilities, other than cash remained unchanged during the year.

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Problem 11-15 Answer C

Cash in checking account	
	350,000
Cash in money market account	
	250,000
Treasury bill	
<u>800,000</u>	
Total cash and cash equivalents	<u>1,400,000</u>

Problem 11-16 Answer C

Checking account No. 201	
	800,000
Checking account No. 202	
	(100,000)
Money market account	
	500,000
BSP treasury bill, 90 days due March 1, 2009	
<u>300,000</u>	
Total cash and cash equivalents	<u>1,500,000</u>

Problem 11-17 Answer A

Cash receipts:

From customers		
	5,000,000	
Rent received		100,000
Interest received		
	<u>50,000</u>	5,150,000
Cash payments:		
To suppliers and employees	3,000,000	
Taxes		200,000
Interest on long term debt		
	<u>400,000</u>	<u>3,600,000</u>
Net cash provided by operating activities		<u>1,550,000</u>

Problem 11-18 Answer D

Net income		
	750,000	
Increase in <i>net</i> accounts receivable (140,000 - 111,000)	(29,000)	
Decrease in prepaid rent expense		21,000
Increase in accounts payable		
		<u>15,000</u>
Cash provided by operating activities		<u>757,000</u>

Problem 11-19 Answer C

Net income		
	800,000	
Depreciation and amortization		200,000
Noncash sale (50,000 + 100,000)		(150,000)
Decrease in accrued salaries		(10,000)
Amortization of bond discount		5,000
Deferred tax liability		
	<u>50,000</u>	
Net cash provided by operating activities		<u>895,000</u>

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Problem 11-20 Answer D

Net income		
	5,000,000	
Purchase of trading securities		(2,500,000)
Sale of trading securities		
	1,100,000	
Loss on sale of TS		
	400,000	
Unrealized gain on TS (1,800,000 - 1,000,000)		(800,000)
Gain on sale of AFS securities (3,000,000 - 2,500,000)		(500,000)
Net cash provided - operating		<u>2,700,000</u>

Problem 11-21 Answer A

Net income		
	2,500,000	
Increase in AR		(400,000)
Net cash provided - operating		<u>2,100,000</u>

Direct method

AR - 1/1		
	1,300,000	
Sales		
	<u>8,000,000</u>	
Total		9,300,000
AR - 12/31		
	(1,900,000)	
Accounts written off		

(50,000)
Collections

7,350,000
Cash expenses

(5,250,000)
Net cash provided - operating

2,100,000

Problem 11-22 Answer C

Net profit

600,000
Gain on sale of investment (250,000 - 150,000)
(100,000)

Increase in trade receivables
(480,000)

Depreciation

150,000
Increase in trade accounts payable

Net cash provided - operating

200,000

370,000

Problem 11-23 Answer C

Net income

1,500,000
Increase in investment carried at equity, representing share in
net income of investee
(55,000)

Amortization of premium on bonds payable
(14,000)

Increase in deferred tax liability

Cash provided by operating activities

18,000

1,449,000

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Problem 11-24 Answer B

Net income

3,400,000	
Depreciation	
1,000,000	
Loss on sale of equipment	
100,000	
Decrease in accounts payable	(200,000)
Decrease in inventory	
150,000	
Increase in accounts receivable	(50,000)
Net cash flow from operating activities	<u>4,400,000</u>

Problem 11-25 Answer A

Net income	
750,000	
Depreciation	
500,000	
Amortization	
200,000	
Decrease in accounts receivable	70,000
Increase in inventory	(
50,000)	
Increase in accounts payable	45,000
Decrease in interest payable	(15,000)
Net cash flow from operating activities	<u>1,500,000</u>

Problem 11-26 Answer A

Net income (squeeze)	1,360,000
Depreciation	
400,000	
Accounts receivable increase	(120,000)

Inventory decrease		
280,000		
Accounts payable decrease		(<u>80,000</u>)
Cash flow from operations		<u>1,840,000</u>

The net income is simply “squeezed” by working back from the cash flow from operations.

Problem 11-27 Answer A

Net income (squeeze)		3,300,000
Decrease in accounts payable	(150,000)	
Increase in inventory		(
50,000)		
Decrease in accounts receivable	100,000	
Decrease in prepaid expenses	200,000	
Depreciation		
900,000		
Gain on sale of equipment		(
<u>300,000)</u>		
Cash flow from operations		<u>4,000,000</u>

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The net income is “squeezed” by working back from the cash flow from operations.

Problem 11-28 Answer A

Net income	
800,000	
Depreciation	
600,000	

Increase in accounts receivable	(500,000)
Decrease in inventory		
100,000		
Increase in prepaid expenses	(20,000)
Increase in accrued expenses		30,000
Decrease in income tax payable	(50,000)
Increase in accounts payable		<u>140,000</u>
Net cash provided by operating activities		<u>1,100,000</u>

Problem 11-29 Answer A

Inventory - January 1		
2,100,000		
Purchases (squeeze)		
<u>5,700,000</u>		
Goods available for sale		7,800,000
Inventory - December 31		<u>(2,500,000)</u>
Cost of goods sold		
<u>5,300,000</u>		
Accounts payable - January 1		1,200,000
Purchases		
<u>5,700,000</u>		
Total		
6,900,000		
Accounts payable - December 31		<u>(1,350,000)</u>
Cash paid for purchases		<u>5,550,000</u>

Problem 11-30 Answer B

Operating expenses per book		3,200,000
Depreciation		

	(1,000,000)	
Prepaid insurance - December 31		200,000
Prepaid insurance - January 1		(150,000)
Accrued salaries payable - December 31	(100,000)	
Accrued salaries payable - January 1		<u>120,000</u>
Cash paid for operating expenses		<u>2,270,000</u>

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Problem 11-31 Answer B

Acquisition of XYZ common stock	(2,250,000)	
Sale of investment securities		9,950,000
Purchase of patent		<u>(2,750,000)</u>
Net cash provided by investing activities		<u>4,950,000</u>

Incidentally, the net cash provided by *financing activities* is computed as follows:

Cash borrowed from bank		2,250,000
Issuance of bonds payable		4,900,000
Payment of short term bank loan	(1,500,000)	
Net cash provided by financing activities		<u>5,650,000</u>

The *increase in customer deposits* will be added to net income in computing cash flow from *operating activities*.

Problem 11-32 Answer B

Problem 11-33 Answer D

Purchase of investment	(260,000)
Sale of investment	
350,000	
Acquisition of 4-year certificate of deposit	(<u>500,000</u>)
Net cash used in investing activities	(<u>410,000</u>)

Alternative answer

The interest received and dividend received may be classified as investing activities:

Purchase of investment	(260,000)
Sale of investment	
350,000	
Certificate of deposit	(500,000)
Interest received	
37,500	
Dividend received	
<u>12,000</u>	
Net cash used in investing activities	(<u>360,500</u>)

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Problem 11-34 Answer D

Cash paid for purchase of building	(400,000)
Cash paid for purchase of land	(<u>350,000</u>)

Net cash used – investing	<u>(750,000)</u>
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Problem 11-35 Answer D

Sale of equipment (book value of P130,000 plus gain of P50,000)	
180,000	
Payment of equipment	<u>(200,000)</u>
Net cash used in investing activities	<u>(20,000)</u>

Incidentally, the cash flow from operating activities is determined as follows:

Net income	
3,000,000	
Gain on sale of equipment	(50,000)
Depreciation	
<u>520,000</u>	
Cash flow from operations	<u>3,470,000</u>

Problem 11-36 Answer C

Payment of bonds payable	(3,700,000)
Payment of cash dividend payable	(300,000)
Proceeds from sale of treasury share	<u>500,000</u>
Net cash used in financing activities	<u>(3,500,000)</u>

Problem 11-37 Answer D

Net increase in borrowings	1,700,000
Vendor financing of property	<u>(200,000)</u>
Net cash inflow from borrowings	1,500,000
Issuance of share capital	1,500,000
Dividend paid	
<u>(700,000)</u>	

Net cash flow - financing

2,300,000

Problem 11-38

Question 1 - Answer D

Question 2 - Answer A

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Problem 11-39

1. Accounts receivable - 2007

580,000

Credit sales - 2008

6,400,000

Total

6,980,000

Less: Accounts receivable - 2008

840,000

Collections in 2008

6,140,000 C

2. Inventory - 2007

420,000

Purchases (**squeeze**)

5,240,000

Goods available for sale

5,660,000

Less: Inventory - 2008

660,000

Cost of goods sold in 2008

5,000,000

Accounts payable - 2007

440,000

Purchases in 2008

5,240,000

Total

	5,680,000	
Less: Accounts payable - 2008		<u>530,000</u>
Payment of accounts payable		<u>5,150,000</u> D
3. Proceeds from note payable		500,000
Proceeds from issue of share capital (1,200,000 - 900,000)		
300,000		
Dividend paid (see computation)		(<u>100,000</u>)
Net cash provided by financing activities		<u>700,000</u> D
Retained earnings - 2007		330,000
Net income for 2008		
<u>400,000</u>		
Total		
	730,000	
Less: Retained earnings - 2008		<u>560,000</u>
Dividend declared in 2008		170,000
Dividend payable - 2008		<u>70,000</u>
Dividend paid		
<u>100,000</u>		
4. Purchase of long term investment		(80,000)
Purchase of property, plant and equipment (1,130,000 - 600,000)		
(<u>530,000</u>)		
Net cash used in investing activities		<u>(610,000)</u> C

Problem 11-40

1. AR - 2007

840,000			
Sales - 2008			
<u>12,000,000</u>			
Total			
12,840,000			
Less: AR -2008			
	780,000		
	Writeoff		
		<u>50,000</u>	—
<u>830,000</u>			
Cash collections in 2008			
		<u>12,010,000</u>	A

2. Inventory - 2007

1,500,000		
Purchases (squeeze)		<u>8,300,000</u>
Goods available for sale		
	9,800,000	
Less: Inventory - 2008		<u>1,400,000</u>
Cost of good sold		<u>8,400,000</u>
Accounts payable - 2007		
	950,000	
Purchases		
<u>8,300,000</u>		
Total		
9,250,000		

Less: Accounts payable - 2008	<u>980,000</u>	
Payment of accounts payable	<u>8,270,000</u>	B

3. Fixed expenses		1,000,000
Depreciation		
(350,000)		
Bad debt expense		(<u>50,000</u>)
Fixed expenses paid in 2008		600,000
Variable expenses paid 2008		
2008 (1,200,000 x 50%)		600,000
2007 (1,100,000 x 50%)		<u>550,000</u>
Total cash disbursements for expenses		
	<u>1,750,000</u>	C
Variable ratio (1,200,000/12,000,000)		
		10%
2007 variable expenses (10% x 11,000,000)		
	<u>1,100,000</u>	

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Problem 11-41

1. Net income	
	3,000,000
	Purchase of TS
(2,000,000)	
	Sale of TS

1,400,000		
Gain on sale of TS		
(400,000)		
Unrealized gain - TS		
(200,000)		
Gain on sale of equipment		
		(50,000)
Decrease in AR		
50,000		
Increase in inventory		
(200,000)		
Depreciation		
400,000		
Increase in AP		
1,000,000		
Decrease in income tax payable		
	(<u>200,000</u>)	
Net cash provided by operations		
	<u>2,800,000</u>	A
Net increase in accumulated depreciation		
	150,000	
Add: Accumulated depreciation of equipment sold		
(600,000 - 350,000)		
<u>250,000</u>		—
Depreciation		
<u>400,000</u>		==
2. Loan receivable		
		(1,000,000)
Collection of loan		
200,000		
Sale of equipment		
<u>400,000</u>		—
Net cash used - investing		
	(<u>400,000</u>)	D

PPE - 2007

	3,000,000	
Add: Acquisition (squeeze)		<u>4,000,000</u>
Total		
	7,000,000	
Less: Cost of equipment sold		<u>600,000</u>
PPE - 2008		
	<u>6,400,000</u>	

The acquisition is represented by the building acquired by finance lease. This is a noncash investing acquisition because there is no cash flow. Actually, the entry is debit building and credit lease liability for P4,000,000.

3. Principal lease payment (600,000 - 400,000)	
(200,000)	
Dividend declared in 2007 and paid in 2008	
(<u>1,500,000</u>)	
Net cash used - financing	(<u>1,700,000</u>) D

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Problem 11-42

Question 1 - Answer D

Net income (7,000,000 - 5,000,000)	2,000,000
Depreciation	
480,000	
Increase in AR	(
300,000)	
Increase in inventory	
(1,500,000)	
Amortization (325,000 - 275,000)	50,000
Increase in accrued expenses	50,000

Increase in accounts payable		<u>320,000</u>
Net cash provided – operating		<u>1,100,000</u>
Net increase in accumulated depreciation	180,000	
Add back: Accumulated depreciation of equipment thrown away	200,000	
	Accumulated depreciation of equipment sold	
	<u>100,000</u>	
Total depreciation		
		<u>480,000</u>

Question 2 - Answer B

Sale of equipment		
50,000		
Purchase of equipment		<u>(850,000)</u>
Net cash used – investing		<u>(800,000)</u>
Net increase in PPE		500,000
Add: Cost of equipment thrown away	200,000	
	Cost of equipment sold	
		<u>150,000</u>
Total acquisition		
		<u>850,000</u>
Patent acquired (25,000 shares x 13)	325,000	
Less: Increase in intangible asset		<u>275,000</u>
Amortization		
		<u>50,000</u>

The patent was acquired by issuing ordinary shares and therefore it is **noncash** investing and financing activity.

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Question 3 - Answer B

Retirement of bonds payable	(2,500,000)
Issuance of bonds payable	2,750,000
Dividend paid	(1,400,000)
Proceeds from note payable - short term debt	<u>700,000</u>
Net cash used - financing	<u>450,000</u>
Net income	
2,000,000	
Less: Increase in retained earnings	<u>600,000</u>
Dividend paid	
<u>1,400,000</u>	

Problem 11-43 Answer B

Net income	
8,000,000	
Increase in accounts receivable	(2,000,000)
Decrease in inventory	3,500,000
Increase in accounts and notes payable	4,000,000
Decrease in income tax payable	(4,500,000)
Depreciation and amortization	1,500,000
Gain on sale of equipment	(500,000)
Net cash provided - operating	<u>10,000,000</u>
Purchase of equipment for cash	(7,000,000)

Proceeds from sale of equipment		<u>2,000,000</u>
Net cash used - investing		(<u>5,000,000</u>)
Increase in long-term debt		5,000,000
Purchase of treasury shares		(1,000,000)
Proceeds from issuance of share capital	4,000,000	
Payment of dividends		(<u>2,500,000</u>)
Net cash provided - financing		<u>5,500,000</u>
Cash balance - January 1		6,000,000
Net cash provided - operating	10,000,000	
Net cash used - investing		(5,000,000)
Net cash provided - financing		<u>5,500,000</u>
Cash balance - December 31		<u><u>16,500,000</u></u>

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Problem 11-44 Answer A

Cash balance - beginning		1,300,000
Cash flow from financing activities		1,000,000
Cash flow from operating activities		400,000
Cash flow from investing activities		(<u>1,500,000</u>)
Cash balance - ending		<u><u>1,200,000</u></u>

Problem 11-45 Answer A

Cash - January 1		
1,200,000		
Cash flow from operating activities (squeeze)	4,200,000	
Cash flow from investing activities		(2,500,000)
Cash flow from financing activities		<u>(800,000)</u>
Cash - December 31		
<u>2,100,000</u>		

The cash flow from operating activities is “squeezed” by working back from the December 31 cash balance.

Problem 11-46 Answer A

Cash - January 1		
1,000,000		
Cash flow from operating activities (squeeze)	3,500,000	
Cash flow from investing activities		(4,800,000)
Cash flow from financing activities		<u>1,800,000</u>
Cash - December 31		
<u>1,500,000</u>		

CHAPTER 12

Problem 12-1
Problem 12-3

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

Problem 12-2
Problem 12-4

- | | |
|------|------|
| 1. D | 1. B |
| 6. C | |
| 2. C | 2. A |
| 7. D | |
| 3. A | 3. D |
| 8. A | |
| 4. C | 4. D |
| 9. A | |
| 5. A | 5. A |

Problem 12-5

Demand bank deposits	
3,000,000	
Net long-term receivables	2,000,000
Loans to employees	
<u>300,000</u>	
Total monetary assets	
<u>5,300,000</u>	

Problem 12-6

Land (1,000,000 x 300 / 120)	2,500,000
Investment in bonds - monetary	1,500,000
Long-term debt - monetary	2,000,000

Problem 12-7

	Restated	Historical	Fraction	
Cash	350,000			
	350,000			
Inventory	2,700,000	300 / 270		3,000,000
Property, plant and equipment	300 / 150	<u>1,800,000</u>	<u>900,000</u>	
Total assets	<u>3,950,000</u>			
	<u>5,150,000</u>			
Current liabilities	700,000			
	700,000			
Noncurrent liabilities	500,000			500,000
Share capital	400,000	300 / 100		1,200,000
Retained earnings	<u>2,350,000</u>			
	<u>2,750,000</u>			
Total liabilities and equity			<u>3,950,000</u>	
			<u>5,150,000</u>	

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Problem 12-8

	Restated	Historical	Fraction	
Cash	400,000			
	400,000			
Accounts receivable	800,000			800,000
Allowance for doubtful accounts		50,000		
		50,000		

Land	1,800,000	360 / 90	
7,200,000			
Building	7,500,000	360 / 100	
27,000,000			
Accumulated depreciation			3,000,000
360 / 100	10,800,000		
Accounts payable			600,000
600,000			
Bonds payable			
4,000,000			
4,000,000			
Depreciation - building			300,000
360 / 100		1,080,000	
Inventory - 12/31/2008			1,200,000
360 / 240		1,800,000	
Sales			
6,000,000		360 / 240	
9,000,000			
Purchases			
4,800,000	360 / 240		7,200,000

Problem 12-9

	Historical	Fraction
Restated		
Sales		
<u>5,000,000</u>		360 / 250
7,200,000		
Cost of good sold:		
Inventory - 1/1		
350,000	360 / 140	900,000
Purchases		
<u>2,500,000</u>	360 / 250	<u>3,600,000</u>
Goods available for sale		2,850,000
Inventory - 12/31		4,500,000
<u>500,000</u>	360 / 360	<u>500,000</u>
Cost of goods sold		
<u>2,350,000</u>		
4,000,000		
Gross income		
<u>2,650,000</u>		
<u>3,200,000</u>		
Expenses:		
Expenses		
2,000,000	360 / 250	2,880,000

Depreciation		
<u>2,000,000</u>	360 / 125	<u>5,760,000</u>
Total expenses		
<u>4,000,000</u>		
<u>8,640,000</u>		
Net loss		
		<u>(1,350,000)</u>
		<u>(5,440,000)</u>

Problem 12-10

	Restated	Historical	Fraction
Cash			
	2,000,000		
	2,000,000		
Trade and other receivables			2,600,000
			2,600,000
Property, plant and equipment			<u>4,600,000</u>
		<u>10,800,000</u>	
280 / 125			
Total assets			
	<u>9,200,000</u>		
	<u>14,904,000</u>		

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	Restated	Historical	Fraction
Trade and other payables			1,800,000
			1,800,000
Share capital			
	4,000,000		
		280 / 112	10,000,000
Revaluation surplus			
400,000			
-			
Retained earnings			
	<u>3,000,000</u>		
	<u>3,104,000</u>		
Total liabilities and equity			<u>9,200,000</u>
			<u>14,904,000</u>

The revaluation surplus shall be eliminated in accordance with PAS 29.

Problem 12-11

	Historical	Fraction
	Restated	
Cash	100,000	
	100,000	
Accounts receivable	1,200,000	
	1,200,000	
Inventory	800,000	
	800,000	
Land	400,000	260 / 100
	1,040,000	
Building	1,000,000	260 / 100
	2,600,000	
Accumulated depreciation		(200,000)
	260 / 100	(260,000)
Equipment	500,000	260 / 125
	1,040,000	1,040,000
Accumulated depreciation		(250,000)
	260 / 125	(520,000)
Total assets		
	<u>3,550,000</u>	
	<u>6,000,000</u>	
Accounts payable		600,000
600,000		
Share capital		
	2,000,000	260 / 100
		5,200,000
Retained earnings		
<u>950,000</u>		<u>200,000</u>
Total liabilities and equity		<u>3,550,000</u>
		<u>6,000,000</u>

Problem 12-12

	2007		2008	
				Historical
	Fraction		Restated	Historical
	Fraction		Restated	
Cash		3,000,000	200/120	
5,000,000	4,250,000	4,250,000		

Inventory		2,200,000	200/110	4,000,000
3,000,000	200/160	3,750,000		
Equipment (net)		1,500,000	200/100	3,000,000
1,400,000	200/100	2,800,000		
Land		4,500,000	200/100	9,000,000
<u>4,500,000</u>	200/100	<u>9,000,000</u>		
			<u>11,200,000</u>	
<u>21,000,000</u>	<u>13,150,000</u>		<u>19,800,000</u>	
Current liabilities		1,500,000	200/120	2,500,000
2,000,000		2,000,000		
Noncurrent liabilities	6,000,000	200/120	10,000,000	6,500,000
		6,500,000		
Share capital		3,000,000	200/100	6,000,000
3,000,000	200/100	6,000,000		
Retained earnings	<u>700,000</u>		<u>2,500,000</u>	<u>1,650,000</u>
	<u>5,300,000</u>		<u>11,200,000</u>	
<u>21,000,000</u>	<u>13,150,000</u>		<u>19,800,000</u>	

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	Historical	Fraction
Restated		
Sales		
	<u>8,000,000</u>	200 / 160
<u>10,000,000</u>		
Cost of good sold:		
Inventory - 1/1		
2,200,000	200 / 110	4,000,000
Purchases		
<u>5,200,000</u>	200 / 160	<u>6,500,000</u>
Goods available for sale		7,400,000
		10,500,000
Inventory - 12/31		
<u>3,000,000</u>	200 / 160	<u>3,750,000</u>
Cost of sales		
<u>4,400,000</u>		
<u>6,750,000</u>		
Gross income		
3,600,000		
3,250,000		
Gain on purchasing power		
-		<u>2,850,000</u>
Total income		
<u>3,600,000</u>		
<u>6,100,000</u>		

Expenses:			
Selling and administrative			1,700,000
	200 / 160	2,125,000	
Depreciation			
<u>100,000</u>	200 / 100		<u>200,000</u>
Total			
	<u>1,800,000</u>		
	<u>2,325,000</u>		
Income before tax			
1,800,000			
3,775,000			
Income tax			
<u>500,000</u>	200 / 160		<u>625,000</u>
Net income			
1,300,000			
3,150,000			
Add: Retained earnings, January 1			<u>700,000</u>
		<u>2,500,000</u>	
Total			
	2,000,000		
	5,650,000		
Less: Dividend			
<u>350,000</u>	200 / 200		<u>350,000</u>
Retained earnings, December 31			<u>1,650,000</u>
		<u>5,300,000</u>	
Net monetary liabilities - 12/31/2007, restated:			
Cash			
	5,000,000		
Current liabilities			
(2,500,000)			
Noncurrent liabilities			
(<u>10,000,000</u>)			
Net monetary liabilities - 12/31/2007			(7,500,000)
Increase in monetary assets in 2008:			
Sales (Restated)			
<u>10,000,000</u>			
Total			
	2,500,000		
Decrease in monetary assets - 2008 (Restated):			
Purchases			6,500,000
Selling and administrative			
	2,125,000		

Income tax		625,000
Dividend		<u>350,000</u>
		<u>9,600,000</u>
Net monetary liabilities - 12/31/2008, restated	(7,100,000)	
Less: Net monetary liabilities - 12/31/2008, cost:		
Cash		4,250,000
Current liabilities	(2,000,000)	
Noncurrent liabilities		
	<u>(6,500,000)</u>	<u>(4,250,000)</u>
Gain on purchasing power		
		<u>2,850,000</u>

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Problem 12-13

	Restated	Historical	Fraction
Net monetary assets - January 1			880,000
140 / 110		1,120,000	
Sales			
3,000,000			140 / 125
3,360,000			
Purchases			
(1,200,000)		140 / 125	(1,344,000)
Expenses			
(900,000)		140 / 125	(1,008,000)
Income tax			
600,000)		140 / 125	(672,000)
Cash dividends			
<u>200,000)</u>		140 / 140	<u>(200,000)</u>
Net monetary assets - December 31			<u>980,000</u>
		<u>1,256,000</u>	
Net monetary assets - December 31, at cost			980,000
Net monetary assets - December 31, as restated			<u>1,256,000</u>
Loss on purchasing power			<u>(276,000)</u>

Problem 12-14

Monetary assets - January 1		250,000
Monetary liabilities - January 1		<u>100,000</u>
Net monetary assets - January 1, at cost		<u>150,000</u>
Net monetary assets - January 1, as restated (150,000 x 150 / 125)	180,000	
Add: Increase in net monetary items as restated	<u>3,500,000</u>	
Total		
	3,680,000	
Less: Decrease in net monetary items as restated	<u>3,000,000</u>	
Net monetary assets - December 31, as restated	<u>680,000</u>	
Monetary assets - December 31		700,000
Monetary liabilities - December 31		<u>300,000</u>
Net monetary assets - December 31, at cost		400,000
Less: Net monetary assets - December 31, as restated	<u>680,000</u>	
Loss on purchasing power		(<u>280,000</u>)

Problem 12-15

1. Current cost - December 31, 2008	600,000	Historical
cost		<u>500,000</u>
Unrealized holding gain in 2008		<u>100,000</u>

2. Current cost - December 31, 2009

	750,000
Historical cost	
<u>500,000</u>	Cumulative unrealized holding gain in 2009
	250,000
Less: Unrealized holding gain recognized in 2008	
<u>100,000</u>	Unrealized holding gain
to be reported in 2009	
<u>150,000</u>	

3. Current cost

	800,000
Historical cost	
<u>500,000</u>	Realized holding gain in 2010
300,000	
Less: Unrealized holding gain in 2008 and 2009	
<u>250,000</u>	Realized holding
gain to be reported in 2010	
<u>50,000</u>	

Sales price	1,000,000
Less: Current cost	
<u>800,000</u>	Gain on sale of land
	<u>200,000</u>

The income statement for 2010 would show the following:

Other income:	
Realized holding gain	
50,000	Gain on sale of land
200,000	

The actual gain from the sale of the land is P500,000 (1,000,000 - 500,000). Only the net amount of P250,000 is reported in 2010 because the balance was already reported in 2008, P100,000 and 2009, P150,000.

Problem 12-16

1. Current cost (5,000,000 x 225/150)

	7,500,000
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Average current cost $(5,000,000 + 7,500,000 / 2)$
6,250,000

Depreciation on average current cost $(6,250,000 / 5)$
 1,250,000

Depreciation on historical cost $(5,000,000 / 5)$
1,000,000 Realized holding gain
250,000

2. Current cost

7,500,000
 Accumulated depreciation $(7,500,000 / 5)$
1,500,000 Net current cost
6,000,000

Historical cost

5,000,000
 Accumulated depreciation $(5,000,000 / 5)$
1,000,000 Book value
4,000,000

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Net current cost

6,000,000
 Book value

4,000,000
 Unrealized holding gain

2,000,000

Problem 12-17

a. Historical cost income statement

Sales

7,200,000

Cost of sales:

Purchases

5,000,000

	Less: Inventory - 12/31	
	<u>1,000,000</u>	<u>4,000,000</u>
Gross income		
3,200,000		
Operating expenses		
<u>700,000</u>		
Net income		
	<u>2,500,000</u>	

b. Current cost income statement

Sales		
	7,200,000	
Cost of sales (40,000 x 125)		<u>5,000,000</u>
Gross income		
2,200,000		
Other income:		
Realized holding gain		
	1,000,000	
Unrealized holding gain		
	<u>500,000</u>	<u>1,500,000</u>
Total income		
	3,700,000	
Operating expenses		
<u>700,000</u>		
Net income		
	<u>3,000,000</u>	
Cost of sales at average current cost		5,000,000
Historical cost		
<u>4,000,000</u>		
Realized holding gain		<u>1,000,000</u>
Inventory - 12/31 at current cost (10,000 x 150)		
	1,500,000	
Inventory - 12/31 at cost		
		<u>1,000,000</u>
Unrealized holding gain		

500,000

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Problem 12-18

**Legaspi Company
Income Statement
Year ended December 31, 2008**

Sales

5,000,000

Cost of sales

3,500,000

Gross income

1,500,000

Other income:

Realized holding gain (300,000 + 30,000)

330,000

Unrealized holding gain (100,000 + 700,000 + 540,000) 1,340,000

1,670,000

Total income

3,170,000

Operating expenses:

Expenses

700,000

Depreciation

130,000

830,000

Income before income tax

2,340,000

Less: Income tax

350,000

Net income

1,990,000

**Legaspi Company
Balance Sheet
December 31, 2008**

Assets

Current assets:		
Cash		500,000
Accounts receivable		
Inventory	600,000	
		<u>1,000,000</u>
	2,100,000	
Noncurrent assets:		
Land		1,500,000
Equipment		
1,600,000		
Less: Accumulated depreciation		<u>160,000</u>
<u>1,440,000</u>	<u>2,940,000</u>	
Total assets		
		<u>5,040,000</u>

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Liabilities and Shareholders' Equity

Current liabilities:		
Accounts payable		500,000
Notes payable		400,000
Income tax payable		
	<u>350,000</u>	1,250,000
Shareholders' equity:		
Share capital		2,000,000
Retained earnings:		

Net income		
1,990,000		
Dividends		
(____ 200,000)	1,790,000	3,790,000
Total liabilities and shareholders' equity		
	<u>5,040,000</u>	

Computations

1. Cost of sales:			
Average current cost			
3,500,000			
Historical cost			
<u>3,200,000</u>			
Realized holding gain			<u>300,000</u>
2. Inventory - December 31:			
Current cost			
1,000,000			
Historical cost			
<u>900,000</u>			
Unrealized holding gain			<u>100,000</u>
3. Land:			
Current cost			
1,500,000			
Historical cost			
<u>800,000</u>			
Unrealized holding gain			<u>700,000</u>
4. Depreciation on average current cost			
(1,000,000 + 1,600,000 / 2 = 1,300,000 / 10)			
130,000			
Depreciation on historical cost			
<u>100,000</u>			
Realized holding gain			<u>30,000</u>
5. Net current cost:			
Current cost			
1,600,000			

Accumulated depreciation			
(<u>160,000</u>)		1,440,000	
Book value:			
	Historical cost		
		1,000,000	
	Accumulated depreciation		
	(<u>100,000</u>)		<u>900,000</u>
Unrealized holding gain			
			<u>540,000</u>

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Problem 12-19 Answer C

2006 (1,400,000 x 70%)

980,000

2007 (380,000 x 80%)

304,000

2008 (440,000 x 90%)

396,000

1,680,000

Problem 12-20 Answer A

Cost of sales:

Average current cost (40,000 x 65)

2,600,000

Historical cost

2,375,000

Realized holding gain

225,000

Average unit cost (58 + 72 = 130 / 2)

65

Problem 12-21

1. Answer D

Inventory - December 31 (9,000 x 71)

639,000

2. Answer A

Cost of sales - average current cost (30,000 x 64)
1,920,000

Average unit cost (57 + 71 = 128 / 2)

64

Problem 12-22 Answer A

Equipment

95,000

Inventory

80,000

Total

175,000

AICPA FASB SFAS No. 89 requires that current cost for inventories and equipment should be measured at the lower of current cost or recoverable amount.

Problem 12-23 Answer C

Historical cost - January 1

1,150,000

Current cost - December 31

1,250,000

Total

2,400,000

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Average current cost (2,400,000 / 2)

1,200,000

Depreciation (1,200,000 / 5)

240,000

Problem 12-24 Answer B

Current cost per unit - January 1

58

Current cost per unit - December 31

72

Total

130

Average current cost (130 / 2)

65

Cost of goods sold at average current cost (70,000 x 65)

4,550,000

Problem 12-25 Answer D

Replacement cost

10

Historical cost

8

Holding gain

2

