

Chapter 37
 Accrual Basis
 Comprehensive Problem

Problem 37-1

Calapan Company provided the following data:

| | 12/31/2014 | 12/31/2015 |
|-----------------------------|------------|------------|
| Physical inventory, at cost | 600,000 | 1,000,000 |
| Sales | 4,000,000 | |
| Cost of sales | 2,400,000 | |
| Accounts receivable-trade | 1,200,000 | 1,350,000 |
| Accounts payable-trade | 1,500,000 | 1,850,000 |

In 2015, accounts written off amounted to P100,000. Sales returns with credit memo amounted to P150,000 and purchase returns, P50,000. Cash receipts from customers after P200,000 discounts totalled P6,000,000 while cash payments to trade creditors amounted to P4,000,000 after discounts of P300,000. Cash paid to customers for goods returned was P50,000. On this transaction, accounts receivable was debited.

- Under accrual basis, what amount should be reported as gross sales for the current year?
 - 6,600,000
 - 6,550,000
 - 6,650,000
 - 6,350,000
- Under accrual basis, what amount should be reported as gross purchases for the current year?
 - 4,700,000
 - 4,350,000
 - 4,300,000
 - 4,000,000

Solution 37-1

Question 1- Answer b

| | |
|--|------------------|
| Accounts receivable- December 31, 2015 | 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- December 31,2014 | (1,200,000) |
| Erroneous debit to accounts receivable | <u>(50,000)</u> |
| Gross sales | <u>6,550,000</u> |

Question 2- Answer a

| | |
|-------------------------------------|--------------------|
| Accounts payable- December 31, 2015 | 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- December 31, 2014 | <u>(1,500,000)</u> |
| Gross purchases | <u>4,700,000</u> |

Problem 37-2

Emmyrelle Company provided the following selected accounts, cash receipts and disbursements for 2015:

| | December 31 | January 1 |
|---------------------|-------------|-----------|
| Accounts receivable | 250,000 | 300,000 |
| Notes receivable | 150,000 | 100,000 |
| Accounts payable | 120,000 | 160,000 |
| Notes payable | 200,000 | 150,000 |
| Prepaid insurance | 30,000 | 10,000 |

Cash receipts for 2015

| | |
|---|-----------|
| Cash sales | 500,000 |
| Collections of accounts, net discounts of P40,000 | 1,800,000 |
| Collections of notes receivable | 80,000 |
| Bank loan- one year, dated December 31, 2015 | |
| 100,000 | |
| Purchase returns and allowances | 60,000 |

Cash disbursements for 2015

| | |
|---|-----------|
| Cash purchases | 130,000 |
| Payments of accounts payable, net of discounts of P20,000 | 1,500,000 |
| Payments of notes payable | 400,000 |
| Insurance | 220,000 |
| Other expenses | 650,000 |
| Sales returns and allowances | 50,000 |

- Under accrual basis, what amount should be reported as gross sales?
 - 2,420,000
 - 2,470,000
 - 2,370,000
 - 2,380,000
- Under accrual basis, what amount should be reported as gross purchases?
 - 1,960,000
 - 2,060,000
 - 2,140,000
 - 1,830,000

Solution 37-2

Question 1- Answer a

| | |
|------------------------------------|-------------------|
| Accounts receivable- December 31 | 250,000 |
| Notes receivable- December 31 | 150,000 |
| Collections of accounts receivable | 1,800,000 |
| Sales discounts | 40,000 |
| Collections of notes receivables | <u>80,000</u> |
| Total | 2,320,000 |
| Accounts receivable- January 1 | (300,000) |
| Notes receivable- January 1 | <u>(100,000)</u> |
| Sales on account | 1,920,000 |
| Cash sales | <u>500,000</u> |
| Gross sales | <u>2,420,000</u> |

Question 2 Answer a

| | | |
|-------------------------------|------------------|-------------------|
| Accounts payable- December 31 | | 120,000 |
| Notes payable-trade | | |
| Notes payable- December 31 | 200,000 | |
| Bank loan on December 31 | <u>(100,000)</u> | 100,000 |
| Payments of accounts payable | | 1,500,000 |
| Purchase discounts | | 20,000 |
| Payments on notes payable | | <u>400,000</u> |
| Total | | 2,140,000 |
| Accounts payable- January 1 | | (160,000) |
| Note payable- January 1 | | <u>(150,000)</u> |
| Purchases on account | | 1,830,000 |
| Cash purchases | | <u>130,000</u> |
| Gross purchases | | <u>1,960,000</u> |

Problem 37-3

Merill Company has not prepared financial statements for three years since December 31, 2012

During the three year period, the cash receipts and cash disbursements were maintained and sales on account were entered directly into an accounts receivable ledger.

However no general postings have been made since the December 31, 2012 closing.

The examination of the records disclosed balances at the beginning and end of the three year period as follows:

| | 12/31/2012 | 12/31/2015 |
|----------------------|------------|------------|
| Less than 1 year old | 77,000 | 141,000 |
| 1 to 2 years old | 6,000 | 9,000 |
| 2 to 3 years old | | 4,000 |

| | | |
|---------------------------|---------------|----------------|
| Over 3 years old | | <u>11,000</u> |
| Total accounts receivable | <u>83,000</u> | <u>165,000</u> |
| Inventory | 58,000 | 94,000 |
| Accounts payable | 25,000 | 55,000 |

No account balances have been written off during the three-year period. The ratio of gross profit to sales remains constant from year to year.

Other data available are as follows:

| | 2013 | 2014 | 2015 |
|-----------------------------|----------------|----------------|------------------|
| Cash received applied to | | | |
| Current year | 744,000 | 809,000 | 1,044,000 |
| Accounts of prior year | 67,000 | 75,000 | 84,000 |
| Accounts of two years prior | <u>3,000</u> | <u>2,000</u> | <u>10,000</u> |
| Total collections | <u>814,000</u> | <u>886,000</u> | <u>1,138,000</u> |
| Cash sales | 85,000 | 130,000 | 156,000 |
| Payment of accounts payable | 625,000 | 706,000 | 869,000 |

- What is the amount of total sales for 2013, 2014, and 2015?
 - 1,341,000
 - 3,291,000
 - 2,920,000
 - 1,032,000
- What is the amount of total purchases for 2013, 2014, and 2015?
 - 2,170,000
 - 2,200,000
 - 2,230,000
 - 2,255,000
- What is the amount of cost of sales for 2013, 2014, and 2015?
 - 2,266,000
 - 2,230,000
 - 2,288,000
 - 2,194,000

Solution 37-3

Question 1- Answer b

| | 2013 | 2014 | 2015 |
|---------------------------|---------|---------|-----------|
| AR- December 31, 2015 | 4,000 | 9,000 | 141,000 |
| Cash received applied to: | | | |
| Current year | 744,000 | 809,000 | 1,404,000 |

| | | | |
|-----------------------------|----------------|------------------|------------------|
| Accounts of prior year | 75,000 | 84,000 | |
| Accounts of two years prior | <u>10,000</u> | | |
| Sales on account | 833,000 | 902,000 | 1,185,000 |
| Cash sales | <u>85,000</u> | <u>130,000</u> | <u>156,000</u> |
| Total sales | <u>918,000</u> | <u>1,032,000</u> | <u>1,314,000</u> |
| Total amount | | | <u>3,291,000</u> |

Question 2 Answer c

| | |
|-------------------------------------|------------------|
| Accounts payable- December 31, 2015 | 55,000 |
| Payments of accounts payable: | |
| 2013 | 625,000 |
| 2014 | 706,000 |
| 2015 | <u>869,000</u> |
| Total | 2,255,000 |
| Accounts payable- December 31, 2012 | <u>(25,000)</u> |
| Purchases- 2013, 2014, 2015 | <u>2,230,000</u> |

Question 3 Answer d

| | |
|---------------------------------|------------------|
| Inventory- December 31, 2012 | 58,000 |
| Purchases- 2013, 2014, 2015 | <u>2,230,000</u> |
| Goods available for sale | 2,288,000 |
| Inventory- December 31, 2015 | <u>(94,000)</u> |
| Cost of sales- 2013, 2014, 2015 | <u>2,194,000</u> |
| Sales- 2013, 2014, 2015 | 3,291,000 |
| Cost of sales- 2013, 2014, 2015 | <u>2,194,000</u> |
| Gross profit | <u>1,097,000</u> |

Average gross profit rate (1,097,000/3,291,000) 33 1/3%

Problem 37-4

Eros Company kept the records on a cash basis. The entity reported the following cash basis income statement for 2015:

| | |
|------------|------------------|
| Revenue | 1,910,000 |
| Expenses | <u>809,000</u> |
| Net income | <u>1,101,000</u> |

The following amounts of accrued, prepaid and unearned items were ignored at the end of 2014 and 2015:

| | | |
|------------------|--------|---------|
| | 2014 | 2015 |
| Accrued revenue | 91,000 | 73,000 |
| Unearned revenue | 66,000 | 108,000 |
| Accrued expenses | 49,000 | 65,000 |

Prepaid expenses 46,000 56,000
 What is the net income under accrual basis?
 a. 1,035,000
 b. 1,051,000
 c. 1,201,000
 d. 1,135,000

Solution 37-4 Answer a

| | |
|---------------------------|------------------|
| Net income cash basis | 1,101,000 |
| Accrued revenue | |
| 2014 | (91,000) |
| 2015 | 73,000 |
| Unearned revenue | |
| 2014 | 66,000 |
| 2015 | (108,000) |
| Accrued expenses | |
| 2014 | 49,000 |
| 2015 | (65,000) |
| Prepaid expenses | |
| 2014 | (46,000) |
| 2015 | <u>56,000</u> |
| Net income- accrual basis | <u>1,305,000</u> |

Problem 37-5

Rice Company's salaried employees are paid biweekly. Advances made to employees are paid back by payroll deductions.

| | 12/31/2014 | 12/31/2015 |
|---------------------------------------|------------|------------|
| Employee advances | 240,000 | 360,000 |
| Accrued salaries payable | 400,000 | ? |
| Salaries expense during the year | | 4,200,000 |
| Salaries paid during the year (gross) | | 3,900,000 |

On December 31, 2015, what amount should be reported as accrued salaries payable?

- a. 940,000
- b. 820,000
- c. 700,000
- d. 300,000

Solution Answer c

| | |
|---|------------------|
| Accrued salaries payable- December 31, 2014 | 400,000 |
| Add: salaries expense | <u>4,200,000</u> |

| | |
|---|------------------|
| Total | 4,600,000 |
| Less: Salaries paid | <u>3,900,000</u> |
| Accrued salaries payable- December 31, 2015 | <u>700,000</u> |

Problem 37-6

Karen Company reported in the income statement for 2015 P1,100,000 of wages expense. The previous year's statement of financial position reported P100,000 of wages payable. An analysis of the payroll records showed wage payments during the year of P950,000. The previous year's adjusting entry for unpaid wages was reversed on January 1, 2015.

What is the amount of the adjusting entry for accrued wages payable on December 31, 2015?

- a. 250,000
- b. 400,000
- c. 150,000
- d. 850,000

Solution 37-6 Answer a

| | |
|-------------------------------|-------------------|
| Wages payable – January 1 | 100,000 |
| Wages expense | <u>1,100,000</u> |
| Total | 1,200,000 |
| Wage payments during the year | <u>(950,000)</u> |
| Wage payable- December 31 | <u>250,000</u> |

Adjusting entry on December 31

| | | |
|-----------------------|---------|---------|
| Wages expense | 250,000 | |
| Accrued wages payable | | 250,000 |

Problem 37-7

Doren Company had a balance of P490,000 in the compensation expense account on December 31, 2015 before year-end adjustment for the following:

- No salary accrual was made for the week of December 25-31, 2015. Salaries for this period totalled P18,000 and were paid on January 5, 2016.
- Bonus for 2015 was paid on January 31, 2016 in the total amount of P175,000.

What is the adjusted balance of compensation expense for 2015?

- a. 683,000
- b. 665,000
- c. 508,000
- d. 490,000

Solution 37-7 Answer a

| | |
|------------------------------------|----------------|
| Compensation expense per book | 490,000 |
| Accrued salaries- December 31,2015 | 18,000 |
| Accrued bonus- December 31,2015 | <u>175,000</u> |
| Total compensation expense | <u>683,000</u> |

Problem 37-8

On December 31, 2015, Ashe Company had a P990,000 balance in the advertising expense account before any year-end adjustments.

- Radio and television advertising spots broadcast during December 2015 were billed to Ashe on January 4, 2016. The invoice cost of P50,000 was paid on January 15,2016.
- Included in the P990,000 is P60,000 for newspaper advertising for a January 2016 sales promotional campaign.

What amount should be reported as advertising expense for 2015?

- a. 930,000
- b. 980,000
- c. 1,000,000
- d. 1,040,000

Solution 37-8 Answer b

| | |
|---|------------------|
| Balance per book | 990,000 |
| Radio advertising accrued on December 31, 2015 | <u>50,000</u> |
| Total | 1,040,000 |
| Prepaid newspaper advertising- December 31,2015 | <u>(60,000)</u> |
| Advertising expense | <u>980,000</u> |

Problem 37-9

Park Company had a balance of P820,000 in the professional fees expense account on December 31, 2015 before considering year-end adjustments relating to the following:

- Consultants were hired for a special project at a total fee not to exceed P650,000. The entity had recorded P550,000 of this fee based on billings for work performed in 2015.
- The attorney's letter requested by the auditors dated January 31, 2016, indicated that legal fees of P60,000 were billed on January 15, 2016 for worked performed in November 2015, and unbilled fees for December 2015 were P70,000.

What amount should be reported for professional fees expense for the year-ended December 31, 2015?

- a. 1,050,000
- b. 950,000
- c. 880,000
- d. 820,000

Solution 37-9

| | | |
|---------------------------------|---------------|----------------|
| Balance per book | | 820,000 |
| Accrued legal fees: | | |
| November | 60,000 | |
| December | <u>70,000</u> | <u>130,000</u> |
| Total professional fees expense | | <u>950,000</u> |

Problem 37-10

Bianca Company maintained the accounting records using the cash basis of accounting. During 2015, the entity collected P5,000,000 in fees from clients. On dec 31, 2014, accounts receivable of P800,000 and unearned fees of P500,000 had been recorded. On December 31, 2015, accounts receivable increased to P1,500,000 while unearned fees increased to P990,000.

Under accrual basis, what is the service revenue for 2015?

- a. 5,000,000
- b. 4,700,000
- c. 6,100,000
- d. 5,300,000

Solution 37-10 answer d

| | | |
|--|--|-------------------|
| Collections from clients | | 5,000,000 |
| Accounts receivable- December 31, 2015 | | 1,500,000 |
| Unearned fees- December 31, 2014 | | <u>500,000</u> |
| Total | | 7,000,000 |
| Accounts receivable- December 31, 2014 | | (800,000) |
| Unearned fees- December 31, 2015 | | <u>(900,000)</u> |
| Service revenue- accrual basis | | <u>5,300,000</u> |

Problem 37-11

During 2015, Tara Company received P8,000,000 from tenants. The statement of financial position contained the following data:

| | 2014 | 2015 |
|--------------------|-----------|-----------|
| Rentals receivable | 960,000 | 1,240,000 |
| Unearned rentals | 3,200,000 | 2,400,000 |

What amount of rental revenue should be reported for 2015?

- a. 9,080,000
- b. 8,520,000
- c. 7,480,000
- d. 6,920,000

Solution 37-11 Answer a

| | | |
|--------------------------------|------------------|------------------|
| Cash received from tenants | | 8,000,000 |
| Rentals receivable- 2015 | | 1,240,000 |
| Unearned rentals -2014 | | <u>3,200,000</u> |
| Total | | 12,440,000 |
| Less: Rentals receivable- 2014 | 960,000 | |
| Unearned rentals- 2015 | <u>2,400,000</u> | <u>3,360,000</u> |
| Rental revenue for 2015 | | <u>9,080,000</u> |

Problem 37-12

Marr Company reported rental revenue of P2,210,000 in the cash basis income tax return for the year-ended November 31, 2015.

| | |
|---|-----------|
| Rent receivable- November 30, 2015 | 1,060,000 |
| Rent receivable- November 30, 2014 | 800,000 |
| Uncollectible rent written off during the fiscal year | 30,000 |

Under accrual basis, what amount should be reported as rent revenue?

- a. 1,920,000
- b. 1,980,000
- c. 2,440,000
- d. 2,500,000

Solution 37-12 Answer d

| | |
|------------------------------------|-------------------|
| Rent revenue -cash basis | 2,210,000 |
| Rent receivable- November 30, 2015 | 1,060,000 |
| Rent written off | <u>30,000</u> |
| Total | 3,300,000 |
| Rent receivable- November 30, 2014 | <u>(800,000)</u> |
| Accrual basis rent revenue | <u>2,500,000</u> |

Problem 37-13

Rill Company owned a 20% royalty interest in oil well. The entity received royalty payments on January 31 for the oil sold between the previous June 1 and November 31, and on July 31 for oil between December 1 and May 31. Production reports revealed the following sale:

| | |
|-------------------------------------|-----------|
| June 1, 2014- November 30, 2014 | 3,000,000 |
| December 1, 2014- December 31, 2014 | 500,000 |
| December 1, 2014- May 31, 2015 | 4,000,000 |
| June 1, 2015- November 30, 2015 | 3,250,000 |
| December 1, 2015- December 31, 2015 | 700,000 |

What amount should be reported as royalty revenue for 2015?

- a. 1,400,000
- b. 1,440,000
- c. 1,490,000
- d. 1,590,000

Solution 37-13 Answer c

| | |
|-------------------------------------|------------------|
| December 1, 2014- May 31, 2015 | 4,000,000 |
| December 1, 2014- December 31, 2014 | (500,000) |
| Sales- January 1- May 31, 2015 | 3,500,000 |
| June 1, 2015- November 30, 2015 | 3,250,000 |
| December 1, 2015- December 31, 2015 | <u>700,000</u> |
| Total sales in 2015 | <u>7,450,000</u> |

Royalty revenue for 2015 (20% x 7,450,000) 1,490,000

Problem 37-14

On January 1, 2015, Denver Company entered into a 4-year licensing agreement with Akins Company allowing Akins to use Denver's cartoon characters in all the lunchboxes that Akins manufactures. Akins is required to pay Denver royalties equal to 10% of annual sales. Akins guaranteed Denver a P1,200,000 minimum royalty over the life of the agreement and paid Denver the minimum amount on January 1, 2015. For the year-ended December 31, 2015, Akins sales totalled P5,000,000.

What amount of royalty income should Denver report in 2015?

- a. 300,000
- b. 500,000
- c. 800,000
- d. 1,200,000

Solution 37-14 Answer b

Royalty revenue for 2015 (10% x 5,000,000) 500,000
Since the guaranteed minimum annual royalty is P300,000 (1,200,000/4 years), the royalty revenue for 2015 is P500,000.

Problem 37-15

James Dean, an MD, keeps accounting records on a cash basis. During 2015, Dr. James collected P1,000,000 in fees from patients. On December 31, 2014, Dr. James had accounts receivable of P200,000. On December 31, 2015, Dr. James had accounts receivable of P300,000 and unearned fees of P10,000.

On an accrual basis, what amount was reported as patient service revenue for 2015?

- a. 1,110,000
- b. 1,090,000
- c. 900,000
- d. 890,000

Solution 37-15 Answer b

| | |
|--|------------------|
| Fees collected | 1,000,000 |
| Accounts receivable- December 31, 2015 | 300,000 |
| Accounts receivable- December 31, 2014 | (200,000) |
| Unearned fees- December 31, 2014 | (10,000) |
| Patient service revenue- accrual basis | <u>1,090,000</u> |