

ACG 201
TEST IA
Spring 2007

NAME MASTER

Class Time
Circle one: 8:00 11:00

MULTIPLE CHOICE: There is only one BEST answer. 2 points each.

1. C

2. A

3. C

4. B

5. D

6. C

7. D

8. C

9. B

10. B

11. D

12. A

13. B

14. D

15. C

16. C

17. A

18. D

19. C

20. B

Multiple Choice 40

Problem I 30

Problem II 20

Problem III 10

100

Multiple Choice – (2 points each) select *the ONE best answer*

1. Three college professors at MIT formed a business to speed transactions over the internet. They each put in an equal amount and will share all profits equally. They are concerned with not having personal legal liability for their business activities and want to raise capital to take the entity public. What business form should they use?
 - a. Sole proprietorship.
 - b. Partnership.
 - c. **Corporation.**
 - d. Division.

2. Finley Company recorded the following cash transactions for the year:
Paid \$90,000 for salaries
Paid \$40,000 to purchase office equipment
Paid \$10,000 for utilities
Paid \$4,000 in dividends
Received \$15,000 on a loan
Collected \$150,000 from customers

What was Finley's net cash (used) or provided by financing activities?
 - a. **\$11,000 provided**
 - b. \$15,000 provided
 - c. \$60,000 provided
 - d. \$40,000 (used)

3. The company's policy toward dividends and growth could best be determined by examining the
 - a. Balance sheet.
 - b. Income statement.
 - c. **Retained earnings statement.**
 - d. Statement of cash flows.

4. If total assets increased by \$14,000 during a period of time and stockholders' equity decreased by \$6,000 during the same period, then the amount and direction (increase or decrease) of the period's change in total liabilities is a(n)
 - a. \$14,000 increase.
 - b. **\$20,000 increase.**
 - c. \$8,000 decrease.
 - d. \$8,000 increase.

5. Notes to the financial statements are principally an application of
 - a. cost.
 - b. materiality.
 - c. conservatism.
 - d. **full disclosure.**

6. On a classified balance sheet, companies usually list current assets
 - a. in alphabetical order.
 - b. with the largest dollar amounts first.
 - c. in the order in which they are expected to be converted into cash.**
 - d. in the order of acquisition.

7. The relationship between total liabilities and total assets is important in evaluating a company's
 - a. profitability.
 - b. liquidity.
 - c. market value.
 - d. solvency.**

8. Which of the following is least useful in evaluating liquidity?
 - a. amount of working capital.
 - b. current ratio.
 - c. net income per share.**
 - d. cash flow from operating activities.

9. M Corporation has a debt to total assets ratio of 73%. This tells the user of M's financial statements
 - a. M is getting a 27% return on its assets.
 - b. There is a risk that M cannot pay its debts as they come due.**
 - c. 73% of the assets are financed by the stockholders.
 - d. Based on this measure, the user should not invest in M.

10. Which of the following statements is **NOT** consistent with generally accepted accounting principles related to asset valuation?
 - a. Many assets are originally recorded in accounting records at their cost to the business entity.
 - b. Subtracting total liabilities from total assets indicates what the owners' equity in the business is worth under current market conditions.**
 - c. Accountants assume that assets such as office supplies, land, and buildings will be used in business operations rather than sold at current market prices.
 - d. Accountants prefer to base the valuation of assets upon objective, verifiable evidence rather than upon appraisals or personal opinion.

11. What organization is primarily responsible for establishing U.S. accounting standards?
 - a. Security Exchange Commission (SEC).
 - b. International Accounting Standards Committee (IASC).
 - c. American Institute of Certified Public Accountants (AICPA).
 - d. Financial Accounting Standards Board (FASB).**

12. Which of the following is not a key assumption in developing accounting standards
 - a. Profitability.**
 - b. Monetary Unit.
 - c. Time period.
 - d. Going concern.

13. What constraint in accounting would permit a company to not follow GAAP in reporting a particular transaction (best answer)
- a. consistency.
 - b. materiality.**
 - c. full disclosure.
 - d. conservatism.
14. Which accounting assumption says that an enterprise will continue in operation long enough to carry out its existing objectives and commitments?
- a. Monetary unit assumption
 - b. Economic entity assumption
 - c. Time period assumption
 - d. Going concern assumption**
15. A high price earnings ratio indicates
- a. high net income and optimism by management .
 - b. high debt and pessimism by the bank.
 - c. net income and optimism by Wall Street.**
 - d. high liquidity for paying bills.
16. Which of the following is not an activity of accounting as included in the definition of accounting?
- a. interpreting.
 - b. classifying.
 - c. auditing.**
 - d. reporting.
17. The usual sequence of steps in the recording process is to
- a. analyze each transaction, enter the transaction in the journal, and transfer the information to the ledger accounts.**
 - b. analyze each transaction, enter the transaction in the ledger, and transfer the information to the journal.
 - c. analyze each transaction, enter the transaction in the book of accounts, and transfer the information to the journal.
 - d. analyze each transaction, enter the transaction in the book of original entry, and transfer the information to the journal.
18. A list of accounts to be used in accounting for transactions is called a
- a. trial balance.
 - b. general journal.
 - c. general ledger.
 - d. chart of accounts.**

19. Accounts receivable has a normal balance of \$9,000 on August 1, debit posting of \$12,000 and credit posting of \$7,000 during the month. The ending balance is
- \$14,000 CR
 - \$4,000 CR
 - \$14,000 DR**
 - \$28,000 CR
20. The best absolute measure of a company's ability to pay obligations due within the next year is the
- current ratio
 - working capital amount**
 - Total cash balance
 - total current asset balance

Problem I – Financial Statements (30 points)

Use the following accounts and information to prepare, in good form, an income statement, a retained earning statement, and a balance sheet for Minor Industries for the month ended January 31, 2007 on pages which follow. Average shares outstanding are 1,000.

Accumulated depreciation	\$ 3,000	Dividends	\$ 3,000
Accounts payable	1,100	Insurance expense	1,200
Accounts receivable	1,500	Supplies	1,400
Buildings	20,400	Bonds payable due in 2010	3,300
Cash	18,600	Rent expense	3,400
Sales revenue	33,700	Salaries expense	10,000
Common stock	10,000	Marketable securities	3,000
Retained earnings (beginning)	25,900	Copyright	2,000
Cost of sales	9,000		
Inventory	3,500		

Financial Statements
 Minor Industries
Income Statement
For the Month Ended January 31, 2007

Sales revenue	<u>33,700</u>
Less: Cost of sales	(9,000)
Insurance expense	(1,200)
Rent expense	(3,400)
Salary expense	<u>(10,000)</u>
	(23,600)

10,100
1,000

Net Income	<u>10,100</u>	_____
Earnings per share	\$ <u>10.10</u>	_____

Retained Earnings Statement
For the Month Ended January 31, 2007

<u>Beginning RE</u>	25,900
<u>Net Income</u>	10,100
<u>Less: Dividends</u>	(3,000)
Retained earnings	<u>33,000</u>

Minor Industries
Classified Balance Sheet
As of January 31, 2007

ASSETS

Current Assets	
Cash	18,600
Marketable securities	3,000
Accounts receivable	1,500
Inventory	3,500
Supplies	<u>1,400</u>
Total Current Assets	<u>28,000</u>
Building	20,400
Less: Accumulated depreciation	<u>(3,000)</u>
	<u>17,400</u>
Copyright	<u>2,000</u>
Total Assets	<u>47,400</u>

LIABILITIES & EQUITY

Current Liabilities	
Accounts payable	<u>1,100</u>
Long Term Liabilities	
Bonds payable due in 2010	<u>3,300</u>
Total Current Liabilities	<u>4,400</u>
Stockholder's Equity	
Common stock	10,000
Retained earnings	<u>33,000</u>
Total Stockholder's Equity	<u>43,000</u>
Total Liabilities and Equity	<u>47,400</u>

Problem II (20 points)

In January, 2007, Wendy Winger organized a corporation to provide aerial photography services. The company is called Aerial Views, Inc and started immediately after formation.

Journalize the following business transactions for January, 2007 on the general journal form on the following page. Identify each transaction by date. You may omit explanations of the transactions.

- January 1. The corporation issued 60,000 shares of capital stock to Wendy Winger and received \$60,000 cash from her.
2. Purchased a plane from Utility Aircraft for \$220,000. Made a \$40,000 cash down payment and issued a note payable for the remaining balance.
 3. Paid Woodrow Airport \$2,500 to rent office and hangar space for the month.
 4. Billed customers \$8,320 for aerial photographs taken.
 5. Paid \$5,000 in cash to employees for work done.
 6. Paid \$1900 to Hannigan's Hanger for maintenance and repair services on the company plane.
 7. Received a bill for \$500 for advertising the current month.
 8. Collected the \$8,320 billed to customers on the 4th.
 9. Paid \$1,200 cash dividends to Wendy Winger.
 10. Received an order for photographs to be taken in February estimated at \$4000.

Chart of Accounts:

Cash
Investment
Accounts Receivable
Office Supplies
Aircraft
Accounts Payable
Notes Payable
Capital Stock
Photography Revenue
Advertising Expense
Maintenance Expense
Rent Expense
Salary Expense
Dividends
Retained Earnings

General Journal

Entry	Description	Debit	Credit
1	Cash Capital stock	60,000	60,000
2	Aircraft Notes payable Cash	220,000	180,000 40,000
3	Rent expense Cash	2,500	2,500
4	Accounts receivable Photography revenue	8,320	8,320
5	Salary expense Cash	5,000	5,000
6	Maintenance expense Cash	1,900	1,900
7	Advertising expense Accounts payable	500	500
8	Cash Accounts receivable	8,320	8,320
9	Dividends (or retained earnings) Cash	1,200	1,200
10	No entry required		

Problem III – Short Answer (10 points)

The following information is determined from the annual reports of Lucky Company and Broke Company.

	Lucky		Broke	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
1. Current ratio	1.47:1	1.65:1	1.90:1	1.60:1
2. Debt to total assets ratio	73%	85%	86%	95%
3. Earnings per share	\$4.52	\$3.52	\$4.30	\$5.30
4. Cash balance	\$1,000,000	\$900,000	\$900,000	\$1,000,000
5. Price Earnings ratio	15:1	18:1	18:1	15:1

Required: Indicate which company has greatest solvency and why.

Lucky has lowest debt to total asset ratio of 73% in 2006, which indicates less risk of meeting long term obligations or solvency.