

**Fall 2004**  
Financial Accounting 201  
EXAM #2

NAME \_\_\_\_\_  
SECTION TIME (Circle one) 10:00 12:00 1:00

Answer all multiple choice questions below; there is only one BEST answer (2 points each)

1.   C  

2.   A  

3.   D  

4.   D  

5.   A  

6.   D  

7.   B  

8.   D  

9.   A  

10.   B  

11.   E  

12.   C  

13.   B  

14.   C  

15.   D  

**Note:** Put answers to problems on Pages provided. Turn in all pages of exam.

Put answer sheets in front of exam.

**SCORE**

	Possible	Actual
Multiple Choice	30	
Problem I	30	
Problem II	30	
Short Answer	<u>10</u>	
Total	<u>100</u>	

**Multiple Choice** (2 points each) There is only **ONE BEST** answer.

**MULTIPLE CHOICE**

1. If **accounts receivable** has debit postings of \$19,000, credit postings of \$10,000, and a beginning normal balance of \$11,000, its ending balance is
  - a. \$2,000
  - b. \$9,000
  - c. \$20,000**
  - d. \$21,000
  
2. Revenue from the sale of merchandise normally is recognized (i.e., recorded)
  - a. on the date of sale.**
  - b. when the customer pays for the merchandise.
  - c. at the earlier of two dates i.e., the date on which the sale occurs, or the date on which the customer pays.
  - d. when the merchandise is sold, if sold for cash, or when payment is received, if sold on credit.
  
3. Closing entries result in net income being calculated in the income summary account and then transferred to the
  - a. Revenue account.
  - b. Common Stock account.
  - c. Dividends account.
  - d. Retained Earnings account.**
  
4. Customers often return merchandise to the store where they bought the merchandise. In order to capture information on returned merchandise, stores should record the dollar amount of merchandise returned by customers
  - a. as a reduction in the Sales account.
  - b. as an addition to the Purchases account.
  - c. in a special inventory account called purchase returns and allowances
  - d. in a contra-revenue account called sales returns and allowances**

5. Flies Corp. sold merchandise to a customer on credit. The invoice amount was \$1,500; the invoice date was December 10; credit terms were 1/10, n/30. Which of the following statements is true?
- The customer can take a \$15 discount if the invoice is paid by Dec. 20.**
  - The customer should pay \$1,485 if the invoice is paid by January 9.
  - The customer must pay a \$15 penalty if payment is made after Jan. 9.
  - The customer must pay \$1,515 if payment is made after December 20.
6. Which of the following statements is **false**?
- The Inventory account is updated after every sale and purchase of merchandise under the perpetual inventory system.
  - The Inventory account is updated only at the end of the accounting period under the periodic inventory system.
  - A Cost of Goods Sold account is updated after each sale of merchandise under the perpetual inventory system.
  - A Purchases account is used under both the periodic and perpetual inventory systems.**
7. Which of the following is a **not** an advantage of the perpetual inventory system over the periodic inventory system?
- Inventory losses can be identified and controlled better under the perpetual system.
  - The equipment and personnel cost of implementing the perpetual inventory system is likely to be less than under periodic.**
  - The perpetual system is suitable for businesses with a relatively small volume of high unit price merchandise.
  - The perpetual system provides more timely information to management than does periodic.
8. The accounting cycle is
- the time period from using cash to purchase merchandise through the collection of cash from sales of merchandise.
  - the calendar year.
  - the 12-month time period which an entity uses for its accounting period.
  - the series of steps performed for a time period beginning with collection and analysis of data from source documents and ending with preparation of financial statements.**
9. Failure to make an adjusting entry to recognize rent receivable would cause:
- an understatement of assets and an understatement of income and owners' equity.**
  - an overstatement of assets and owners' equity and an understatement of net income.
  - no effect on assets, liabilities, net income, and owners' equity.
  - an overstatement of assets, net income, and owners' equity.
  - None of the above is correct.

10. A company has appropriately applied the matching principle in 2004 in each case described below **EXCEPT**:
- a. Sales commissions are charged to expense in 2004 on all sales revenue realized in 2004 even though some of the commissions have not been paid.
  - b. Insurance expense is recognized for the total cost of a 1-year policy purchased in August, 2004.**
  - c. A loss is recognized in 2004 on land that is sold below its cost.
  - d. Utility expenses (e.g., for electricity and water used) are recognized in 2004 even though the last bill received in 2004 has not been paid.

11. A list of all accounts and their balances which is used to prove the equality of debits and credits as of a specific date:
- a. Account
  - b. General journal
  - c. General ledger
  - d. Chart of accounts
  - e. Trial balance**

12. Ellis Company sells merchandise on account for \$1,200 to Thomas Company with credit terms of 2/10, n/30. Thomas Company returns \$400 of merchandise that was damaged, along with a check to settle the account within the discount period. What entry does Ellis Company make upon receipt of the check?

a. Cash .....	800	
Accounts Receivable .....		800
b. Cash .....	784	
Sales Returns and Allowances .....	416	
Accounts Receivable .....		1,200
<b>c. Cash .....</b>	<b>784</b>	
<b>Sales Returns and Allowances .....</b>	<b>400</b>	
<b>Sales Discounts .....</b>	<b>16</b>	
<b>Accounts Receivable .....</b>		<b>1,200</b>
d. Cash .....	1,176	
Sales Discounts .....	24	
Sales Returns and Allowances .....		400
Accounts Receivable .....		800

Use the following information to answer questions 13 through 15

Financial information is presented below:

Operating Expenses	\$ 55,000
Sales Returns and Allowances	13,000
Sales Discount	6,000
Sales	160,000
Costs of Goods Sold	77,000

13. The amount of net sales on the income statement would be
- a. \$154,000.
  - b. \$141,000.**
  - c. \$160,000.
  - d. \$166,000.
14. Gross Profit would be
- a. \$77,000.
  - b. \$70,000.
  - c. \$64,000.**
  - d. \$83,000.
15. The profit margin rate would be
- a. .454.
  - b. .546.
  - c. .500.
  - d. .538.**

**Problem I** (30 points)

Journalize the following business events in general journal form. Identify each transaction by number.

1. Stockholders invest \$325,000 in cash in starting a clothing store operating as a corporation.
2. Purchased \$150,000 of clothes for resale on credit.
3. Purchased store equipment for \$16,000, paying \$3,500 in cash and signed a 60-day, \$12,500, note payable.
4. Signed a contract to deliver \$75,000 of clothes to the UNCW athletic department, the gross profit rate is 20%.
5. Shipped \$40,000 of monogrammed shirts to a customer on account. The cost of merchandise was \$25,000 (assume perpetual inventory)
6. Paid \$7,000 in cash for the current month's rent.
7. Paid \$28,000 cash on account for purchase in transaction 2.
8. Received a bill for \$500 for advertising used during the current month.
9. Paid \$2,500 cash for sales salaries.
10. Received a bill from the electric company for the monthly electricity of \$75.
11. Paid \$1,200 cash dividends to stockholders.
12. Received a check for \$40,000 from the customer in payment on account for the merchandise shipped in transaction 5.
13. Recorded depreciation expense for the month of \$400.

### General Journal

Entry	Description	Debit	Credit
1.	Cash Common Stock	\$325,000	\$325,000
2.	Inventory Accounts payable	150,000	150,000
3.	Store Equipment Cash Notes payable	16,000	3,500 12,500
4.	Not a Transaction		
5.	Accounts Receivable Sales Cost of Sales Inventory	40,000 25,000	40,000 25,000
6.	Rent Expense Cash	7,000	7,000
7.	Accounts Payable Cash	28,000	28,000
8.	Advertising Expense Accounts Payable	500	500
9.	Sales Salary Expense Cash	2,500	2,500
10.	Electricity Expense Accounts Payable	75	75
11.	Dividends or Returned Earnings Cash	1,200	1,200
12.	Cash Account Receivable	40,000	40,000
13.	Depreciation Expense Accumulated Depreciation	400	400

**Problem I** (30 points)

**PART A**

On June 1, 2004, Hale Company paid for a three-year insurance premium. On that date the following journal entry was made:

Prepaid insurance .....7,200  
 Cash..... 7,200

The annual accounting period ends on December 31. Give the adjusting entry that should be made on December 31, 2004.

$$7,200 \div 36 = 200/\text{month} \times 7 \text{ months} = 1,400 \text{ used}$$

**General Journal**

Entry	Description	Debit	Credit
12-31-04	Insurance Expense Prepaid Insurance	1,400	1,400

**PART B**

Accounting Today, a monthly newsletter, collects annual subscriptions of \$60 from each subscription. In November, 2004 it collected 1,000 subscriptions and in December it collected 5,000 more. Calculate the revenue earned on these subscriptions by December 31, 2004 and record the adjustment entry required.

$$60 \div 12 = \$5/\text{mnthly}$$

$$\text{Nov} = 1,000 \times 2 \text{ months} \times \$5 = 10,000$$

$$\text{Dec} = 5,000 \times 1 \text{ month} \times \$5 = 5,000$$

$$10,000 + 5,000 = 15,000$$

**General Journal**

Entry	Description	Debit	Credit
12-31-04	Unearned Subscriptions Subscription Revenue	1,500	1,500

PART C

Coastal Beverage started the year with \$6,500 in packing supplies, during the year it purchased \$18,000 more packing supplies. Based on a count at year end packing supplies on hand was \$14,000. Record the adjustment for packing supplies at year end.

**General Journal**

Entry	Description	Debit	Credit
12-31-04	Supply Expenses Packing Supplies	10,500	10,500

					Supplies	
Beg.		6,500		24,500		
Purchases	+	<u>18,000</u>		<u>(14,000)</u>	on hand	
		<u>24,500</u>		<u>10,500</u>	used	

PART D

An employer has 5 employees who are each paid \$600 on Friday's. If the accounting period ends on Tuesday, December 31, what adjusting entry is required?

**General Journal**

Entry	Description	Debit	Credit
12-31-04	Salary Expense Salary Payable	1,200	1,200

$$5 \times 600 \times \frac{2}{5} = 1,200$$

PART E

A corporation borrows \$8,000 from a bank on December 1, at a 9% annual interest. What adjustment entry is needed at December 31 to record the interest owed the bank.

General Journal

Entry	Description	Debit	Credit
11-31-04	Interest Expense Interest Payable	60	60

$$8,000 \times .09 \times \frac{1}{12} = 60$$

**Short Answer – Question III** (10 points)

You own Hot Mouth, Inc., a company which manufactures BBQ sauce in Mexico where all wages and supplies are paid in cash. Your major customer is Walmart which buys your product by the truckload. Walmart pays its bills under terms of net 75.

Required: Indicate whether Hot Mouth, Inc., should use the cash or accrual method of accounting for its financial reporting and briefly explain why.

Accrual, this results in better matching of revenues & expenses. Your major customer pays slowly (Walmart) so earnings would be distributed under the cash basis.