

Fall 2005
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. <u> B </u> | 11. <u> C </u> |
| 2. <u> D </u> | 12. <u> D </u> |
| 3. <u> C </u> | 13. <u> C </u> |
| 4. <u> D </u> | 14. <u> D </u> |
| 5. <u> E </u> | 15. <u> B </u> |
| 6. <u> D </u> | 16. <u> B </u> |
| 7. <u> C </u> | 17. <u> C </u> |
| 8. <u> A </u> | 18. <u> C </u> |
| 9. <u> C </u> | 19. <u> A </u> |
| 10. <u> C </u> | 20. <u> C </u> |

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	40	
Problem I	20	
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. Under the perpetual inventory system, in addition to making the entry to record a sale, a company would
 - A. Make no additional entry until the end of the period.
 - B. Debit Cost of Goods Sold and credit Merchandise Inventory.**
 - C. Debit Cost of Goods Sold and credit Purchases.
 - D. Debit Merchandise Inventory and credit Cost of Goods Sold.

2. Welsh Company purchased an item for inventory that cost \$14 per unit and was marked to sell at \$16 less selling costs of \$1. It was determined that the replacement cost is \$12 per unit. No purchases in the near future are anticipated. Using the lower-of-cost-or-market rule, the per unit valuation for inventory should be
 - A. \$16.00.
 - B. \$15.00.
 - C. \$14.00.
 - D. \$12.00.**

3. Which of the following goods would *not* be included in merchandise inventory for a selling company?
 - A. Goods on hand in the showroom.
 - B. Goods shipped on consignment to another company.
 - C. Goods in transit to a customer shipped FOB shipping point.**
 - D. Goods in transit to a customer shipped FOB destination.

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. 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.**

6. Which of the following statements is **false**?
- A. The Inventory account is updated after every sale and purchase of merchandise under the perpetual inventory system.
 - B. The Inventory account is updated only at the end of the accounting period under the periodic inventory system.
 - C. A Cost of Goods Sold account is updated after each sale of merchandise under the perpetual inventory system.
 - D. A Purchases account is used under both the periodic and perpetual inventory systems.**
7. 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 |
| | | |
| C. Cash | 784 | |
| Sales Returns and Allowances | 400 | |
| Sales Discounts | 16 | |
| Accounts Receivable | | 1,200 |
| | | |
| D. Cash | 1,176 | |
| Sales Discounts | 24 | |
| Sales Returns and Allowances | | 400 |
| Accounts Receivable | | 800 |
8. An automobile dealer probably would use which of the following inventory methods?
- A. Specific identification.**
 - B. Average-cost.
 - C. FIFO.
 - D. LIFO.
9. Which inventory method generally best follows the matching principle?
- A. Average-cost.
 - B. Whichever method is used for tax purposes.
 - C. LIFO.**
 - D. FIFO.
10. In a period of rising prices, which inventory method is best to use for tax purposes?
- A. Specific identification.
 - B. Average-cost.
 - C. LIFO.**
 - D. FIFO.

Use the following information to answer questions 11 through 13

The trial balance for Houley Corporation appears as follows:

Houley Corporation Trial Balance December 31, 2005		
Cash	\$ 300	
Accounts Receivable	500	
Prepaid Insurance	50	
Supplies	150	
Office Equipment	4,000	
Accumulated Depreciation, Office Equipment		\$ 800
Accounts Payable		300
Common Stock		1,000
Retained Earnings		1,400
Service Revenue		3,000
Salaries Expense	1,000	
Rent Expense	<u>500</u>	
	<u>\$ 6,500</u>	<u>\$ 6,500</u>

11. If on December 31, 2005, the insurance still unexpired amounted to \$20, the adjusting entry would contain a
- A. Debit to Prepaid Insurance for \$30.
 - B. Credit to Prepaid Insurance for \$20.
 - C. Debit to Insurance Expense for \$30.**
 - D. Credit to Prepaid Insurance for \$20.
12. If as of December 31, 2005, rent of \$100 for December had not been recorded or paid, the adjusting entry would include a
- A. Credit to Accumulated Rent for \$100.
 - B. Credit to Cash for \$100.
 - C. Debit to Rent Payable for \$100.
 - D. Debit to Rent Expense for \$100.**
13. If service for \$125 had been performed but not billed, the adjusting entry to record this would include a
- A. Debit to Service Revenue for \$125.
 - B. Credit to Unearned Service Revenue for \$125.
 - C. Credit for Service Revenue for \$125.**
 - D. Debit to Unearned Revenue for \$125.

14. The multiple-step income statement for a merchandiser shows each of the following features *except*:
- A. Gross profit.
 - B. Operating expenses.
 - C. Net sales.
 - D. Investing activities.**
15. Which of the following activities occurs last in the accounting cycle?
- A. Preparing the financial statements.
 - B. Journalizing and posting closing entries.**
 - C. Preparing an adjusted trial balance.
 - D. Preparing a worksheet.
16. ABC Toys received an order from a customer on March 1. The toys were shipped on March 18. The customer sent a check for full payment on April 10. ABC received the check on April 12 and deposited it in the bank account. ABC should record sales revenue related to this series of transaction on
- A. March 1.
 - B. March 18.**
 - C. April 10.
 - D. April 12.
 - E. None of the above is correct.
17. Timberland's gross profit percentage has been increasing in the three years from 1996 through 1998 from 36.5% to 39.8%. This change has most likely been caused by
- A. Higher product costs.
 - B. Selling products with lower margins.
 - C. Selling products for higher prices.**
 - D. None of the above.
 - E. All of the above.
18. Which of the following is ***NOT*** a reason for closing entries:
- A. They are required to reduce the balances in the temporary accounts to zero at the end of each period.
 - B. They transfer the components of net income to a stockholders' equity account each period.
 - C. They establish a zero balance in all assets and liabilities accounts at the end of each period.**
 - D. They are required so that the income statement accounts will be prepared to collect revenue and expense amounts for the subsequent period.

19. Which of the following statements about a periodic inventory system is true?
- A. **Cost of goods sold is determined only at the end of the accounting period.**
 - B. Detailed records of the cost of each inventory purchase and sale are maintained continuously.
 - C. The periodic system provides better control over inventories than a perpetual system.
 - D. The increased use of computerized systems has increased the use of the periodic system.
20. According to the article "Fuzzy Numbers" in the November, 2004, Business Week,
- A. As a result of Sarbanes Oxley reforms, corporate profits are no longer distorted or confusing and management no longer plays any games with earnings.
 - B. Accounting rules allow some management latitude in manipulating net income but no latitude in manipulating the cash flow statement.
 - C. **Estimates of pension fund profits, unpaid receivables and old inventory are easy to manipulate.**
 - D. Extensive use of accounting estimated tends to increase stock prices in the long run.

Problem I (20 points)

Inventory records indicate the following at October 31:

Oct.	1	Beginning inventory	10 units @	\$93	=	930
	8	Purchase	55 units @	\$150	=	8,250
	15	Purchase	25 units @	\$181	=	4,525
	19	Purchase.....	35 units @	\$185	=	6,475
	26	Purchase	<u>55</u> units @	<u>\$196</u>	=	<u>10,780</u>
			180			30,960

One hundred and twenty units were sold for \$240 each. The Physical count of inventory at October 31 indicates that 60 units are on hand, and the company owns them.

Required: Complete the comparative income statements below under the various inventory-costing methods.

Hint: Determine sales, then compute ending inventory and cost of goods sold and finally gross profit using each of the following methods (show your calculations in the space provided):

1. Specific identification of unit cost, where the warehouse determines 55 units @ \$150 and 5 @ \$196 are on hand at October 31.
2. Weighted-average cost
3. First in, first out
4. Last in, first out

		<u>Specific ID</u>	<u>Weighted Average Cost</u>	<u>FIFO</u>	<u>LIFO</u>
Sales	(120 x 240)	<u>28,800</u>	<u>28,800</u>	<u>28,800</u>	<u>28,800</u>
Beginning Inventory		930	930	930	930
Purchases		<u>30,030</u>	<u>30,030</u>	<u>30,030</u>	<u>30,030</u>
Good available		30,960	30,960	30,960	30,960
Less: Ending Inventory		<u>(9,230)</u>	<u>(10,320)</u>	<u>(11,705)</u>	<u>(8,430)</u>
Cost of Sales		<u>21,730</u>	<u>20,640</u>	<u>19,255</u>	<u>22,530</u>
Gross Profit		<u>7,070</u>	<u>8,160</u>	<u>9,545</u>	<u>6,270</u>
		55x150=8,250 <u>5x196= 980</u> 60 9,230	<u>172x60</u> 10,320	55x196=10,780 <u>5x185= 925</u> 11,705	10x93= 930 <u>50x150=7,500</u> 8,430

Problem II (30 points)

PART A

On September 1, 2004, Hale Company purchased a new computer for \$1,200. It is expected to be used for 24 months and then will be discarded for zero salvage

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

General Journal

Entry	Description	Debit	Credit
12-31-04	Depreciation Expense Accumulated Depreciation	200	200

$$\frac{1,200}{24} = 50/\text{month} \times 4 \text{ months} = 200$$

PART B

UNC-Chapel Hill sells 55,000 season tickets for home games for \$200 each. Two games are held in September, two in October and one in November. Assuming that \$11,000,000 is credited to unearned season tickets when the tickets are sold, what adjustment is needed for monthly financial statements at the end of September?

General Journal

Entry	Description	Debit	Credit
9-30	Unearned season tickets Revenue	4,400,000	4,400,000

$$\begin{array}{r} \frac{11,000,000}{5 \text{ games}} = \frac{2,200,000}{\times 2} \\ 4,400,000 \end{array}$$

PART C

Coastal Beverage started the year with \$2,500 in packing supplies, during the year it purchased \$12,000 more packing supplies. Based on a count at year end packing supplies on hand was \$8,000. Record the adjustment for packing supplies at year end.

General Journal

Entry	Description	Debit	Credit
12-31	Supply Expense Supplies	6,500	6,500

<u>Supplies</u>	
2,500	14,520
<u>12,000</u>	<u>(8,000)</u>
14,500	6,500 used

PART D

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

General Journal

Entry	Description	Debit	Credit
12-31	Salary Expense Salary Payable	1,800	1,800

$$5 \times 600 \times \frac{3}{5} = 1,800$$

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
12-31	Interest Expense Interest Payable	60	60

$$8,000 \times 9\% \times 1/12 = 60$$

Short Answer – Question III (10 points)

Aai Pharma sells Darvacet, a pain medicine to pharmacies such as Eckards and CVS. On December 28, 2003, the company shipped 100,000 cases of its products to Walgreens. Walgreens returned 90,000 cases on January 5, 2004.

Required: Indicate whether Aai Pharma should record net sales revenue on the 100,000 cases of product at December 31, 2003 and why. (hint: consider revenue recognition principle)

Should record sale for 10,000 cases, although 100,000 were delivered, they only expected/actually were paid for 10,000 since 90,000 were returned. Under revenue recognition must both deliver (earn) and expect to be paid.