

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

NAME \_\_\_\_\_  
SECTION TIME (Circle one) 8:00 9:00 10:00

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

1.      **B**
2.      **A**
3.      **B**
4.      **A**
5.      **A**
6.      **D**
7.      **B**
8.      **B**
9.      **C**
10.     **C**
11.     **C**
12.     **D**
13.     **B**
14.     **A**
15.     **B**
16.     **B**
17.     **B**
18.     **C**
19.     **D**
20.     **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	40	
Problem I	25	
Problem II	25	
Short Answer	<u>10</u>	
Total	<u>100</u>	

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

1. A flower shop makes a large sale for \$1,000 on November 30 and delivers the flowers on December 1. The customer is sent a statement on December 5 and a check is received on December 10. The flower shop follows GAAP and applies the revenue recognition principle. When is the \$1,000 considered to be earned?
  - A. November 30
  - B. December 1**
  - C. December 5
  - D. December 10
  
2. Using accrual accounting, expenses are recorded and reported only
  - A. when they are incurred whether or not cash is paid.**
  - B. when they are incurred and paid at the same time.
  - C. if they are paid before they are incurred.
  - D. if they are paid after they are incurred.
  
3. Which of the following would not result in unearned revenue?
  - A. Rent collected in advance from tenants
  - B. Services performed on account**
  - C. Sale of season tickets to football games
  - D. Sale of two-year magazine subscriptions
  
4. Which of the following is a true statement about closing the books of a corporation?
  - A. Expenses are closed to the Expense Summary account.
  - B. Only revenues are closed to the Income Summary account.
  - C. Revenues and expenses are closed to the Income Summary account.**
  - D. Revenues, expenses, and the Dividends account are closed to the Income Summary account.
  
5. Gross profit equals the difference between
  - A. net income and operating expenses.
  - B. net sales revenues and cost of goods sold.**
  - C. net sales revenues and operating expenses.
  - D. net sales revenues and cost of goods sold plus operating expenses.
  
6. Under a perpetual inventory system
  - A. accounting records continuously disclose the amount of inventory.**
  - B. increases in inventory resulting from purchases are debited to purchases.
  - C. there is no need for a year-end physical count.
  - D. accounting procedures and systems are simplified.
  
7. A perpetual inventory system would most likely be used by a(n)
  - A. automobile dealership.**
  - B. hardware store.
  - C. drugstore.
  - D. convenience store.

8. The primary difference between a periodic and perpetual inventory system is that a periodic system
- A. keeps a record showing the inventory on hand at all time.
  - B. provides better control over inventories.
  - C. records the cost of the sale on the date the sale is made.
  - D. **determines the inventory on hand only at the end of the accounting period.**
9. The credit terms offered to a customer by a business firm were 2/10, n/30, which means
- A. the customer must pay the bill within 10 days.
  - B. the customer can deduct a 2% discount if the bill is paid between the 10th and 30th day from the invoice date.
  - C. **the customer can deduct a 2% discount if the bill is paid within 10 days of the invoice date.**
  - D. two sales returns can be made within 10 days of the invoice date and no returns thereafter.
10. If the beginning balance in accounts payable was a normal balance of \$100 and the total of the debit entries to the accounts payable account amounted to \$900 and the total of the credit entries during the month amounted to \$500. The ending balance of the account was
- A. \$1,400 credit balance.
  - B. \$1,400 debit balance.
  - C. \$600 debit balance.
  - D. **\$600 credit balance.**
11. The shareholders of a retailer interested in evaluating how much of a sales dollar increases their equity would monitor
- A. Gross profit percentage
  - B. **Profit margin percentage**
  - C. Inventory turnover
  - D. Days in inventory
12. Which of the following describes the conservatism constraint?
- A. **Avoid overstating assets and revenues and avoid understating expenses and liabilities.**
  - B. The benefits of accounting for and reporting information should outweigh the costs.
  - C. Amounts that are large enough to influence a user's decisions.
  - D. Differences due to long-standing and accepted accounting and reporting in a particular industry.
  - E. None of the above is correct.

Use the following information to answer questions 13 and 14:

Financial information is presented below:

Operating Expenses	\$ 45,000
Sales Returns and Allowances	13,000
Sales Discount	6,000
Sales	150,000
Beginning inventory	77,000
Ending inventory, per count	85,000
Purchases	90,000

13. The amount of net sales on the income statement would be
- A. \$137,000.
  - B. \$131,000.**
  - C. \$150,000.
  - D. \$144,000.
14. Cost of sales would be
- A. \$90,000.
  - B. \$98,000.
  - C. \$82,000.**
  - D. \$88,000.
15. In a period of rising prices, which of the following inventory methods generally results in the lowest net income figure?
- A. Average Cost Method
  - B. LIFO method**
  - C. FIFO method
  - D. Need more information to answer
16. M Corporation borrowed \$100,000 at 6% from First Bank on November 1, 2003. The note is to be paid back with interest on October 31, 2004. Which of the following is true?
- A. On December 31, 2004, interest expense of \$6,000 must be accrued.
  - B. On December 31, 2003 (M's year end), M will have to accrue interest expense of \$1,000.**
  - C. If M does not accrue interest expense at year end it will cause net income for 2003 to be understated.
  - D. When M pays the loan and interest off on October 31, 2004, M will record interest expense of \$6,000.
17. Which of the following costs is most likely to be the largest expense item on the income statement of a merchandising chain such as Wal-Mart?
- A. Wage, salary and benefits expense
  - B. Cost of Sales**
  - C. Advertising
  - D. Income tax expense

18. Which of the following sequence of events is correct relative to the accounting cycle?
- A. post, journalize, trial balance, statements
  - B. post, trial balance, journalize
  - C. journalize, post, trial balance, statements**
  - D. journalize, statements, post, trial balance
19. All of the following are required steps in the accounting cycle *except*:
- A. journalizing and posting closing entries.
  - B. preparing an adjusted trial balance.
  - C. preparing a post-closing trial balance.
  - D. preparing a work sheet.**
20. Each of the following is a major type (category) of adjusting entry *except*:
- A. prepaid expenses.
  - B. accrued revenues.
  - C. accrued expenses.
  - D. earned expenses.

**Problem I** (25 points)

PART A

On July 1, 2003, Hale Company paid for a two-year insurance premium. On that date the following journal entry was made:

Prepaid insurance .....2,400  
 Cash.....2,400

The annual accounting period ends on December 31. Give the adjusting entry that should be made on December 31, 2003.

**General Journal**

Entry	Description	Debit	Credit
12-30-03	Insurance Expense Prepaid Insurance	1,200	1,200

PART B

On October 1, 2003, Zany Company (land lord) leased some of its office space to Fox Company and immediately collected **six months** rent in advance of \$12,000. Zany debited cash and credited unearned rent liability for \$12,000. At the end of 2003 (end of the annual accounting period), give the adjusting entry Zany should make in respect to the rent.

**General Journal**

Entry	Description	Debit	Credit
12-31-03	Unearned Rent liability Rent Revenue	6,000	6,000

PART C

On January 1, 2003, Mildred Corporation purchased a new computer for \$3,100. It had an estimated useful life of three years and a residual value of \$400. At the end of its accounting period, at December 31, 2003, Mildred's computer consultant says the computer could be replaced for \$800. What is the appropriate adjusting entry at December 31, 2003?

**General Journal**

<b>Entry</b>	<b>Description</b>	<b>Debit</b>	<b>Credit</b>
12/31/03	Depreciation Expense Accumulated Deprecation	900	900

PART D

Model Company keeps a small inventory of supplies used for cleaning and maintenance purposes. On January 1, 2003, the inventory of supplies on hand was \$1,740. During the year, supplies purchased, which amounted to \$1,620, were debited to the supplies inventory account. On December 31, 2003, the inventory count of supplies in the storeroom showed \$1,280. give the adjusting entry required at December 31, 2003.

**General Journal**

<b>Entry</b>	<b>Description</b>	<b>Debit</b>	<b>Credit</b>
12/31/03	Supply Expense Supplies	2,080	2,080

PART E

The employees for Fuqua Corporation work Monday through Friday, and earn \$6,000 a week. Payday is Friday.

What is the required adjusting entry for payroll at December 31, 2003 if the last payroll paid was Friday, December 26, 2003 and year end is Wednesday, December 31.

**General Journal**

<b>Entry</b>	<b>Description</b>	<b>Debit</b>	<b>Credit</b>
12/31/03	Wages Expense Wages Payable	3600	3600

**Problem II** (25 points)

Inventory records indicate the following at October 31:

Oct.	1	Beginning inventory.....	20 units @	\$145	=	2,900
	8	Purchase .....	55 units @	\$150	=	8,250
	15	Purchase .....	25 units @	\$130	=	3,250
	19	Purchase.....	5 units @	\$195	=	975
	26	Purchase .....	<u>20</u> units @	\$200	=	<u>4,000</u>
			125			19,375

One hundred ten units were sold for \$200 each. The Physical count of inventory at October 31 indicates that 15 units are on hand, and the company owns them. 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 15 units @ \$150 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	<u>20,000</u>	<u>20,000</u>	<u>20,000</u>	<u>20,000</u>
Beginning Inventory	2,900	2,900	2,900	2,900
Purchases	<u>16,475</u>	<u>16,475</u>	<u>16,475</u>	<u>16,475</u>
Good available	19,375	19,375	19,375	19,375
Less: Ending Inventory	<u>(3750)</u>	<u>(3875)</u>	<u>(4975)</u>	<u>(3650)</u>
Cost of Sales	<u>15,625</u>	<u>15,500</u>	<u>14,400</u>	<u>15,725</u>
Gross Profit	<u>4375</u>	<u>4500</u>	<u>5600</u>	<u>4275</u>
—				

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

You are a politician running for office. One of your big campaign issues is fixing the social security system. The government currently uses the cash method of accounting for social security revenues and expenses.

Required: Indicate whether you think the government should continue to use the cash basis or switch to the accrual basis of accounting for social security revenues and expense and briefly defend your answer.