

Multiple Choice – There is only ONE best answer (2 points each)

1. Having one person responsible for the related activities of ordering merchandise, receiving goods, and paying for them
 - a. **increases the potential for errors and fraud.**
 - b. decreases the potential for errors and fraud.
 - c. is an example of good internal control.
 - d. is a good example of safeguarding the company's assets.

2. A very small company would have the most difficulty in implementing which of the following internal control activities?
 - a. **Separation of duties**
 - b. Limited access to assets
 - c. Periodic independent verification
 - d. Sound personnel procedures

3. If employees are bonded
 - a. it means that they are not allowed to handle cash.
 - b. they have worked for the company for at least 10 years.
 - c. **they have been insured against misappropriation of assets.**
 - d. it is impossible for them to steal from the company.

4. The reconciliation of the cash register tape with the cash in the register is an example of
 - a. other controls.
 - b. **independent internal verification.**
 - c. establishment of responsibility.
 - d. segregation of duties.

5. The receivable that is usually evidenced by a formal instrument of credit is a(n)
 - a. trade receivable.
 - b. **note receivable.**
 - c. accounts receivable.
 - d. income tax receivable.

6. Under the allowance method, Bad Debt Expense is recorded
 - a. when an individual account is written off.
 - b. when the loss amount is known.
 - c. **for an amount that the company estimates it will not collect.**
 - d. several times during the accounting period.

7. Under the allowance method, writing off an uncollectible account
 - a. **affects only balance sheet accounts.**
 - b. affects both balance sheet and income statement accounts.
 - c. affects only income statement accounts.
 - d. is not acceptable practice.

8. If a company fails to record estimated bad debts expense,
- cash realizable value is understated.
 - expenses are understated.**
 - revenues are understated.
 - receivables are understated.
9. When the allowance method is used to account for uncollectible accounts, Bad Debts Expense is debited when
- a sale is made.
 - an account becomes bad and is written off.
 - management estimates the amount of uncollectibles.**
 - a customer's account becomes past due.
10. An aging of a company's accounts receivable indicates that \$4,000 are estimated to be uncollectible. If Allowance for Doubtful Accounts has a \$1,200 credit balance, the adjustment to record bad debts for the period will require a
- debit to Bad Debts Expense for \$4,000.
 - debit to Allowance for Doubtful Accounts for \$2,800.
 - debit to Bad Debts Expense for \$2,800.**
 - credit to Allowance for Doubtful Accounts for \$4,000.
11. Under the allowance method of accounting for uncollectible accounts,
- the cash realizable value of accounts receivable is greater before an account is written off than after it is written off.
 - Bad Debts Expense is debited when a specific account is written off as uncollectible.
 - the cash realizable value of accounts receivable in the balance sheet is the same before and after an account is written off.**
 - Allowance for Doubtful Accounts is closed each year to Income Summary.
12. Allowance for Doubtful Accounts on the balance sheet
- is offset against total current assets.
 - increases the cash realizable value of accounts receivable.
 - appears under the heading "Other Assets."
 - is deducted from accounts receivable.**
13. Laurs Company uses the percentage of receivables method for recording bad debts expense. The Accounts Receivable balance is \$200,000 and credit sales are \$1,000,000. Management estimates that 4% of accounts receivable will be uncollectible. What adjusting entry will Manning Company make if the Allowance for Doubtful Accounts has a credit balance of \$2,000 before adjustment?

a. Bad Debts Expense	10,000	
Allowance for Doubtful Accounts		10,000
b. Bad Debts Expense	8,000	
Allowance for Doubtful Accounts		8,000
c. Bad Debts Expense	6,000	
Allowance for Doubtful Accounts.....		6,000
d. Bad Debts Expense	12,000	
Accounts Receivable		12,000

14. Under the direct write-off method of accounting for uncollectible accounts
- the allowance account is increased for the actual amount of bad debt at the time of write-off.
 - a specific account receivable is decreased for the actual amount of bad debt at the time of write-off.**
 - balance sheet relationships are emphasized.
 - bad debt expense is always recorded in the period in which the revenue was recorded.
15. Elway Company purchases land for \$85,000 cash. Elway assumes \$2,500 in property taxes due on the land. The title and attorney fees totaled \$1,000. Elway has the land graded for \$2,200. They paid \$10,000 for paving of a parking lot. What amount does Elway record as the cost for the land?
- \$88,200
 - \$100,700
 - \$90,700**
 - \$85,000
16. Stories Company purchased equipment and these costs were incurred:
- | | |
|--------------------------|-----------------|
| Cash price | \$22,500 |
| Sales taxes | 1,800 |
| Insurance during transit | 320 |
| Installation and testing | <u>430</u> |
| Total costs | <u>\$25,050</u> |
- Stories will record the acquisition cost of the equipment as
- \$22,500.
 - \$24,300.
 - \$24,620.
 - \$25,050.**
17. Management should select the depreciation method that
- is easiest to apply.
 - best measures the plant asset's market value over its useful life.
 - best measures the plant asset's contribution to revenue over its useful life.**
 - has been used most often in the past by the company.
18. An expenditure for which of the following items would be considered a revenue expenditure?
- Plant asset
 - Ordinary repair**
 - Addition
 - Improvements
19. An asset was purchased for \$40,000. It had an estimated salvage value of \$10,000 and an estimated useful life of 10 years. After 5 years of use, the estimated salvage value is revised to \$8,000 but the estimated useful life is unchanged. Assuming straight-line depreciation, depreciation expense in year 6 would be
- \$6,000.
 - \$4,250.
 - \$3,400.**
 - \$5,000.

20. The book value of a plant asset is the difference between the
- replacement cost of the asset and its historical cost.
 - cost of the asset and the amount of depreciation expense for the year.
 - cost of the asset and the accumulated depreciation to date.**
 - proceeds received from the sale of the asset and its original cost.
21. A company sells a plant asset that originally cost \$150,000 for \$50,000 on December 31, 2007. The accumulated depreciation account had a balance of \$60,000 after the current year's depreciation of \$15,000 had been recorded. The company should recognize a
- \$100,000 loss on disposal.
 - \$40,000 gain on disposal.**
 - \$40,000 loss on disposal.
 - \$25,000 loss on disposal.
22. Intangible assets are the rights and privileges that result from ownership of long-lived assets that
- must be generated internally.
 - are depreciated over their useful life.
 - have been exchanged at a gain.
 - do not have physical substance.**
23. Goodwill can be recorded
- when customers keep returning because they are satisfied with the company's products.
 - when the company acquires a good location for its business.
 - when the company has exceptional management.
 - only when there is an exchange transaction involving the purchase of an entire business.**
24. Cost allocation of an intangible asset is referred to as
- amortization.**
 - depreciation.
 - accretion.
 - capitalization.
25. Research and development costs
- are classified as intangible assets.
 - must be expensed when incurred under generally accepted accounting principles.**
 - should be included in the cost of the patent they relate to.
 - are capitalized and then amortized over a period **not** to exceed 20 years.

Problem I (20 points)

Barlowe Corporation purchased a piece of equipment on January 1, 2006 for \$24,000. The equipment has an estimated life of five years, or 40,000 units of production and an estimated residual value of \$4,000. The company's fiscal year corresponds to the calendar year.

Required: Compute annual depreciation expense for 2006, 2007, and 2008 using the methods indicated below. Show calculations.

	<u>2006</u>	<u>2007</u>	<u>2008</u>
Annual Expense			
Straight-line	<u>4,000</u>	<u>4,000</u>	<u>4,000</u>
	$\frac{24,000 - 4,000}{5} =$	$\frac{20,000}{5} = 4,000$	
Units of Production (actual production)	$\frac{6,000}{(12,000)} \times .50$	$\frac{4,000}{(8,000)} \times .5$	$\frac{5,000}{(10,000)} \times .5$
	$\frac{24,000 - 4,000}{40,000} =$.50 / cents	
Double-declining-balance	$\frac{9,600}{.40 (24,000)}$	$\frac{5,760}{.4 (24,000 - 9,600)}$	$\frac{3,456}{4 (24,000 - 9,600)}$

$1/5 \times 2 = 40\%$ Double decline ratio

Problem II (20 points)

The Portland Boat Company's bank statement for the month of November showed a balance per bank of \$7,000. The company's Cash account in the general ledger had a balance of \$5,659 at November 30. Other information is as follows:

- (1) A deposit of \$5,200 was recorded on the books of the company on November 30 \$5,200 but this amount does not appear on the bank statement.
- (2) The bank statement shows a debit memorandum for \$40 for check printing charges.
- (3) Check No. 119 payable to Lynch Company was recorded in the company books and cleared the bank for \$248.
- (4) The total amount of checks still outstanding at November 30 amounted to \$5,800.
- (5) Check No. 138 was correctly written and paid by the bank for \$409. The company books reflect an entry for Check No. 138 as a debit to Accounts Payable and a credit to Cash in Bank for \$490.
- (6) The bank returned an NSF check from a customer for \$560.
- (7) The bank included a credit memorandum for \$1,260 which represents collection of a customer's note by the bank for the company; principal amount of the note was \$1,200 and interest was \$60. Interest has not been accrued.

Instructions

Prepare a bank reconciliation for the Portland Boat Company at November 30.

Balance per Bank	7,000	Balance per Books	5,659
Add: deposit in transit	5,200	Less: sewer charge	(40)
Less: outstanding checks	<u>(5,800)</u>	NSF check	(56)
		Add: check error	81
		bank collection	<u>1,260</u>
Adjusted	<u>6,400</u>	Adjusted	<u>6,400</u>

b. Prepare the General Journal entries required:

Date	Description	Debit	Credit
11-30	Cash	1,341	
	Accounts payable		81
	Notes receivable		1,200
	Interest income		60
	Service charge expense	40	
	Accounts receivable	560	
	Cash		600

Problem III (10 points) Internal Controls

Sam Hill has worked for Dr. Lee Chang for several years. Sam demonstrates a loyalty that is rare among employees. He hasn't taken a vacation in the last three years. One of Sam's primary duties at the medical office is to open the mail and list the checks received. He also takes cash from patients at the cashier window as patients leave. At times it is so hectic that Sam doesn't bother with giving patients a receipt for the cash paid on their accounts. He assures them he will see to it that they receive the proper credit. When the traffic is slow in the office Sam offers to help Mary post the payments to the patients' accounts receivable. She is always happy to receive his help, because he is a very conscientious worker.

Required: Using the information in the case, indicate one example for **three** of the six types of internal controls listed below and indicate whether it is a strength or weakness.

<u>Type of Internal Control</u>	<u>Case Application</u>	<u>Strength or Weakness</u>
1. Establishment of responsibility	Sam does multi-tasks	weakness
2. Segregation of duties	Sam collects cash and posts receivables	weakness
3. Physical, mechanical, and electronic control	No cash register	weakness
4. Independent internal verification	No indication of key	weakness
5. Documentation procedures	No receipt sometimes	weakness
6. Other Controls	No vacation	weakness