

CONCORDIA UNIVERSITY
John Molson School of Business
Department of Accountancy

Course: Introduction to Financial Accounting
Number: ACCO 230.2
Sections: Sections A and B (S. Mroz); Section AA (S. Tamas)
Examination: FINAL (3 hours)
Date: December 19, 2009
No. of Pages: **Ten (10)**, including this page. Ensure your copy is complete.
Materials Allowed: Non-programmable / non-graphical calculators, and one ordinary dictionary, i.e., not electronic. Pens, pencils, rulers, erasers.

INSTRUCTIONS

- Show all answers in the spaces provided. If space is insufficient, use the back of the page.
- Show details of all calculations, except for multiple-choice.
- Invigilators will not answer questions, unless you think there is actually an error in the exam.

Student name (please print very clearly) _____

ID number _____

Section _____

For grader's use only

Problem 1 (MC) _____
Problem 2 _____
Problem 3 _____
Problem 4 _____
Problem 5 _____
Total =====

PROBLEM 1 (18 marks; 16 minutes)

Multiple-choice

Circle clearly (no overlap) the letter that corresponds to the best answer for each of the following.

1. Included in the balance sheet of J Ltd. on December 31, 2007 were total assets of \$100,000 and total shareholders' equity of \$65,000. During 2008 assets increased by \$35,000 and the company reported net earnings of \$15,000. Also during 2008 the company issued \$3,000 of new shares, and declared dividends of \$3,000. Which of the following statements is true?
 - (a) Liabilities increased by \$20,000 during 2008.
 - (b) Liabilities increased by \$35,000 during 2008.
 - (c) Liabilities increased by \$55,000 during 2008.
 - (d) Liabilities increased by \$29,000 during 2008.

2. It was discovered that the bookkeeper for U Ltd. had recorded a \$200 deposit from a customer for service work to be performed in the future as follows: Dr. Unearned revenue \$200; Cr. Cash \$200. As a result of this entry
 - (a) Cash is understated by \$200 and Unearned revenue is understated by \$200.
 - (b) Cash is understated by \$400 and Unearned revenue is overstated by \$400.
 - (c) Cash is understated by \$400 and Unearned revenue is understated by \$400
 - (d) Cash is understated by \$200 and Unearned revenue is overstated by \$200.

3. A Ltd. shows a balance in Salaries Payable of \$45,000 at the end of November. The next payroll amounting to \$50,000 is to be paid in early December, and includes \$5,000 of wages earned in December. What will be the journal entry to record the payment of salaries?

(a) Salaries Expense	50,000	
Salaries Payable.....		5,000
Cash.....		45,000
(b) Salaries Expense	50,000	
Cash.....		50,000
(c) Salaries Expense	50,000	
Salaries Payable.....	45,000	
Cash.....		95,000
(d) Salaries Expense	5,000	
Salaries Payable.....	45,000	
Cash.....		50,000

4. During 2008 Z Ltd. incurred a net loss of \$50,000 and issued \$10,000 of common shares. On the company's balance sheet as at December 31, 2008 Z Ltd. showed total assets of \$150,000 and a retained earnings balance of \$60,000. Which of the following statements is true if total liabilities decreased by \$20,000 during 2008?
 - (a) Total assets at the end of 2007 were \$210,000.
 - (b) Total assets at the end of 2007 were \$90,000.
 - (c) Total assets at the end of 2007 were \$150,000.
 - (d) Total assets at the end of 2007 were \$60,000.

5. After the books were closed in 2008 it was discovered that the bookkeeper for N Ltd. had recorded the declaration of a cash dividend to be paid in 2009 as follows: Dr. Dividend expense \$9,000; Cr. Cash \$9,000. Regarding the 2008 financial statements, which of the following statements is true?
 - (a) Cash is understated by \$9,000 and Retained earnings is overstated by \$9,000.
 - (b) Liabilities are understated by \$9,000 but Retained earnings is neither overstated nor understated.
 - (c) Net earnings are understated by \$9,000 and working capital is understated by \$9,000.
 - (d) Net earnings are understated by \$9,000 and Retained earnings is understated by \$9,000.

6. A company reports cash provided by operating activities of \$565,000, cash used by investing activities of \$612,000, cash provided by financing activities of \$12,000, net capital expenditures of \$395,000, and dividends paid of \$130,000. Its free cash flow is
 - (a) \$(35,000).
 - (b) \$(47,000).
 - (c) \$40,000
 - (d) \$87,000.

Multiple choice, cont'd

7. Gillis Corporation sells merchandise on account for \$1,000 to Mountain Corporation with credit terms of 2/10, n/30. Mountain returns \$400 of merchandise that was seriously defective and at the same time includes a cheque to settle the account within the discount period. What entry does Gillis make upon receipt of the cheque?
- | | | | |
|-----|------------------------------------|-----|-------|
| (a) | Cash | 600 | |
| | Sales Returns and Allowances | 380 | |
| | Accounts Receivable | | 980 |
| (b) | Cash | 600 | |
| | Sales Returns and Allowances | 392 | |
| | Sales Discounts | 8 | |
| | Accounts Receivable | | 1,000 |
| (c) | Cash | 588 | |
| | Sales Returns and Allowances | 400 | |
| | Sales Discounts | 12 | |
| | Accounts Receivable | | 1,000 |
| (d) | Cash | 580 | |
| | Sales Discounts | 20 | |
| | Sales Returns and Allowances | 400 | |
| | Accounts Receivable | | 1,000 |
8. A consulting firm received \$6,840 cash in advance for services to be rendered in the future. The full amount was credited to Consulting Service Revenue. If only 50% of the services were actually performed by the end of the accounting period and no adjusting entry is made, this would cause
- Revenues to be overstated and assets to be understated.
 - Revenues to be overstated and liabilities to be understated.
 - Revenues to be overstated and liabilities to be overstated
 - Revenues to be overstated and assets to be overstated
9. It was discovered that the bookkeeper for V Ltd. had recorded a \$90 payment on account to a supplier as follows: Dr. Accounts receivable \$90; Cr. Cash \$90. As a result of this entry
- Accounts receivable is overstated by \$90 and Accounts payable is overstated by \$90.
 - Accounts payable is overstated by \$90 and Accounts receivable is understated by \$90.
 - Accounts payable is understated by \$90 and Accounts receivable is understated by \$90.
 - Accounts receivable is overstated by \$90 and Accounts payable is understated by \$90.
10. Which of the following accounts would not be closed at the end of the accounting period?
- Deposits from customers.
 - Dividends declared.
 - Interest income.
 - All of the above accounts would be closed.
11. A legal firm received \$2,000 cash in advance for legal services to be rendered in the future. The full amount was credited to Unearned Service Revenue. If the legal services were actually provided by the end of the accounting period and no adjusting entry is made, this would cause
- Assets to be understated.
 - Shareholders' equity to be overstated.
 - Liabilities to be understated.
 - Revenues to be understated.
12. If a company fails to adjust the Prepaid Rent account for rent that has expired, what effect will this have on that month's financial statements?
- Expenses will be understated and working capital will be understated.
 - Working capital will be overstated and net earnings and shareholders' equity will be overstated.
 - Assets will be overstated and net earnings and shareholders' equity will be understated.
 - Expenses will be overstated and net earnings and shareholders' equity will be understated.

PROBLEM 2, cont'd

5. What will be the effect on the following financial items immediately after the transaction in Requirement (4) only (improves, deteriorates, or no change)?
No calculations are required for Requirement (5).

- (a) Debt to Total Assets ratio (78 % before transaction) _____
- (b) Current ratio (1.15 before transaction) _____
- (c) Working capital _____
- (d) Free cash flow _____

(3.5 marks)

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PROBLEM 3 (16 marks; 32 minutes)

Preparation of cash flow statement

Below are the summary balance sheets for KB Ltd. as at Dec. 31, 2009 and 2008, respectively:

	<u>2009</u>	<u>2008</u>
Cash	\$ 12,000	\$ 90,000
Accounts receivable	53,000	62,000
Merchandise inventory	29,000	32,000
Prepaid rent	14,000	9,000
Fixed assets	367,000	270,000
Accumulated depreciation	<u>(80,000)</u>	<u>(30,000)</u>
Total Assets	<u>\$395,000</u>	<u>\$433,000</u>
Accounts payable	\$ 21,000	\$ 34,000
Interest payable	4,000	2,500
Income taxes payable	10,000	5,500
Notes payable	0	100,000
Common shares	110,000	100,000
Retained earnings	<u>250,000</u>	<u>191,000</u>
Total Liabilities and Equity	<u>\$395,000</u>	<u>\$433,000</u>

Income statement information for 2009 is shown below:

Sales	\$ 850,000
Cost of goods sold	<u>580,000</u>
Gross profit	270,000
Depreciation expense	65,000
Rent expense	13,000
Other operating expenses	<u>57,000</u>
Operating income	135,000
Interest expense	5,000
Gain on disposal of fixed assets	<u>22,000</u>
Earnings before income taxes	152,000
Income tax expense	<u>64,000</u>
Net earnings	<u>\$ 88,000</u>

Additional information

- 1. Fixed assets were acquired for \$170,000 cash during 2009. Also during 2009, fixed assets were disposed of in exchange for cash (the amount can be derived).
- 2. Accounts payable relates only to transactions with suppliers of merchandise inventory.
- 3. Ninety-percent (90%) of all sales are made on credit.

Required

Prepare in proper form a complete cash flow statement (all sections) for the year 2009. Use the indirect method for the operating section of the statement. Show your answer on the next page.

Problem 3, Answer

PROBLEM 4, continued

- g) Average collection period for accounts receivable.

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PROBLEM 5 (31 marks; 62 minutes)

Financial accounting and reporting issues

Tina Reynolds works at an accounting firm. She has many small clients who all adhere to GAAP and have a December 31 yearend. Over the last many months she has helped her clients answer the following independent questions. *The marks for each case are shown in brackets.*

- a) Client A overstated inventory on December 31, 2007 by \$16,000 and understated inventory on December 31, 2008 by \$12,000. Client A reported gross profit of \$167,000 in 2007 and gross profit of \$146,000 in 2008. Calculate the correct gross profit for each year. (4)
- b) Client B showed a balance of \$400,000 in Accounts Receivable as at December 31, 2008. An ageing schedule showed that \$12,000 of these accounts receivable are doubtful of collection. The unadjusted balance in Allowance for Doubtful Accounts was a debit of \$2,000. Show the journal entry to record bad debts expense for 2008. How much is the net realizable value of accounts receivable on December 31, 2008 *after* this entry is made? (4)
- c) Client C disposed of a machine for \$50,000 cash on October 1, 2009. The machine had been purchased on January 1, 2008 for \$90,000. At the time of acquisition it was estimated that the useful life of the machine was five years, with a residual value of \$8,000. Client C uses the double-diminishing balance method of depreciation. Calculate the gain or loss on disposal (no journal entry required). (5)

PROBLEM 5, continued

- d) Client D received \$430 from a customer for a cash sale. This amount included 5% GST. Show the journal entry to record this transaction. Round to nearest dollar; ignore PST. (3)
- e) One of Client E's customers went bankrupt. The customer owed Client E \$10,000. Show the journal entry to write-off the account. If the net realizable value of accounts receivable was \$234,000 immediately before the write-off, how much was the net realizable value of accounts receivable immediately after the write-off? (3)
- f) Client F acquired a truck on July 1, 2007 for \$50,000. The truck has an estimated useful life of eight years (250,000 kilometres) and a residual value of \$5,000. The truck was driven 20,000 kilometres in 2007, and 40,000 kilometres in 2008. Client F uses the units of production method of depreciation. Show the journal entry to record depreciation expense for 2007. Calculate the carrying amount (net book value) of the truck on December 31, 2008 (no journal entry required for 2008). If, instead, Client F had always been using the straight-line method, would the carrying amount be higher or lower on December 31, 2008? By how much? (6)

PROBLEM 5, continued

- g) The office manager for Client G has heard Tina refer to the *matching principle*, but is not sure what it means. Briefly explain the meaning of the term *matching principle*, and why it is important in modern financial reporting. (3)

- h) On August 9, 2008 Client H received a cheque for \$6,000 from a customer whose account had been written off earlier that year. Show the journal entry to record this recovery. Will the net realizable value of accounts receivable increase, decrease, or remain the same immediately *after* this journal entry is recorded? (3)