

MIDTERM EXAMINATION (REGULAR)
FALL 2013

Name: _____ ID: _____ Section: _____

Duration: 3 hours

Instructions (very important):

1. This examination paper consists of **8 pages including this page**. Please make sure your copy has all pages before commencing to write.
2. Make sure that your FULL name (last name first), Student ID and Section Letter are on the three documents: computer input sheet, answer booklet and examination paper.
3. You must answer the multiple choice questions by using the **computer input sheet**; darken the letter you choose **in pencil** on the computer input sheet. Write all your answers to the other questions in the **examination answer booklet**. You may answer the questions in any order you prefer. **Only the answers on the computer input sheet and in the examination booklet will be graded.**
4. Read the questions carefully and budget your time wisely.
5. Show all calculations on the examination booklet, and omit narratives for journal entries. Using abbreviated account names, headings, subheadings, totals and subtotals is not recommended, and it may be subject to mark deduction.
6. This is a closed book examination. However, a silent hand-held (not graphical or programmable) calculator and one standard language (not electronic) dictionary are permitted.
7. **Invigilators will not answer questions.** If you think there is an **error** in the question, ask your instructor when he/she visits the exam room.
8. Return the exam along with the computer input sheet and answer booklet(s) when you have finished.

Question	Topic	Total Marks
1	Multiple Choice	27
2	Journal Entries	14
3	Financial Statements	36
4	Trade Receivables and Bad Debt	23
Total		100

Question 1 (27 marks; 45 minutes):

Multiple Choice

For each of the following multiple choice question, choose the letter that corresponds to the **best** answer, and **show your answer on the computer input sheet**. Each correct answer is worth 1.5 marks.

1. On January 1, 2013, Thomas Co. paid \$1,000 for a two-year insurance policy on the building. The accounting period ends December 31. At December 31, the end of the accounting period, the financial statements should report which of the following?
 - A. Prepaid Insurance \$0 on the Statement of Financial Position and Insurance Expense \$1000 on the Income Statement.
 - B. Prepaid Insurance \$500 on the Statement of Financial Position and Insurance Expense \$500 on the Statement of Shareholders' Equity.
 - C. Prepaid Insurance \$500 on the Statement of Financial Position and Insurance Expense \$500 on the Income Statement.
 - D. Prepaid Insurance \$1,000 on the Statement of Financial Position and Insurance Expense \$500 on the Income Statement.
2. If a company fails to adjust a Prepaid Rent account at the end of its fiscal year, what effect will this incidence have on the company's financial statements?
 - A. No effect.
 - B. Assets will be overstated; shareholders' equity will be understated.
 - C. Assets will be overstated; shareholders' equity will be overstated.
 - D. Expenses will be overstated; shareholders' equity will be understated.
3. Which statement below best describes the accounting equation?
 - A. The change in retained earnings equals profit less dividends.
 - B. Equality of the effects of revenue and expense transactions over time.
 - C. Resources of the company equal creditors' and owners' claims to those resources.
 - D. Financing activities equal investing and operating activities.
4. On January 1, 2012, Brooks Inc. started the year with a balance of \$492,000 in Retained Earnings and a balance of \$605,000 in Share Capital. During 2012, the company earned profit of \$92,000, paid a dividend of \$15,200, and issued additional shares for \$27,500. What is total shareholders' equity on December 31, 2012?
 - A. \$1,231,700.
 - B. \$1,097,000.
 - C. \$1,201,300.
 - D. \$1,588,300.
5. The classified statement of financial position allows one to ascertain which of the following?
 - A. The most valuable asset of the company.
 - B. The specific due date for all liabilities of the company.
 - C. Which liabilities must be paid within the upcoming year.
 - D. None of the above.
6. A company makes an accrual adjustment that increases a liability. This must mean:
 - A. an asset account is decreasing by the same amount.
 - B. an expense account is increasing by the same amount.
 - C. a revenue account is increasing by the same amount.
 - D. a different liability account is decreasing by the same amount.

7. SAS Ltd. ordered and received goods in January, paid for them in February, sold them in March and was paid by customers in April. Using the accrual basis of accounting:
- A. expenses were recorded in February and revenues were recorded in April.
 - B. expenses were recorded in February and revenues were recorded in March.
 - C. expenses and revenues were recorded in March.
 - D. expenses were recorded in January and revenues were recorded in April.
8. Which of the following would NOT represent good controls over cash receipts?
- A. Record all cash receipts as soon as possible.
 - B. The employee that receives cash and cheques should also deposit them in the bank.
 - C. Open mail each day and make a list of cheques received with the amount and payer's name.
 - D. Verify cash receipts by comparing the bank deposit slip with the accounting records.
9. Which of the following would not affect a company's profit?
- A. A change in the company's income taxes.
 - B. A change in the selling price of a company's product.
 - C. Paying a dividend to shareholders.
 - D. Advertising a new product.
10. Coca-Cola reported net sales revenues of \$18.8 billion and cost of goods sold of \$5.6 billion while PepsiCo reported revenues of \$22.3 billion and cost of goods sold of \$9.3 billion. Which of the following statements is correct?
- A. PepsiCo generated more revenues, but a lower gross profit percentage, than Coca-Cola.
 - B. Coca-Cola generated a lower gross profit percentage because its sales revenue was lower.
 - C. PepsiCo better controlled product costs as a percentage of sales than did Coca-Cola.
 - D. None of the above.
11. In October, Suma Inc. prepaid rent of \$7,000 for November and December. Which of the following describes the effects of this transaction in October?
- A. Assets decrease \$7,000 and liabilities decrease \$7,000.
 - B. Assets increase \$7,000 and shareholders' equity increases \$7,000.
 - C. There is no change to total assets, liabilities or shareholders' equity.
 - D. Liabilities decrease \$7,000 and shareholders' equity increases \$7,000.
12. Guco reported the following amounts on its income statement: total revenues, \$31,500; interest expense, \$300; profit, \$1,600; income tax expense, \$900; and operating profit, \$2,800. What was the amount of Guco's profit before income taxes?
- A. \$1,300. B. \$2,500. C. \$29,000. D. \$29,900.

13. Puffing Co. had \$6,000 of supplies at the end of October. During November, the company bought \$2,000 of supplies. At the end of November, the company had \$1,000 of supplies remaining. Which of the following statements is NOT true?
- A. During November, the company used \$7,000 of supplies.
 - B. The carrying value of supplies on November 30 should be \$1,000.
 - C. An expense should be debited for \$7,000 in November.
 - D. An expense should be debited for \$1,000 in November.
14. On September 30, 2013, the bank's records indicated that CIC Inc. has \$12,956.73 in its chequing account. CIC was aware of three outstanding cheques for a total of \$2,112.19. During September 2013, the bank rejected two deposited cheques from CIC's customers totalling \$654.19 because of insufficient funds. The bank also charged CIC \$12.00 in service fees. CIC had not yet received notice about the bad cheques, but it had already recorded the service fees. Prior to any adjustments on September 30, 2013, CIC's Cash account would have a balance of:
- A. \$14,402.73.
 - B. \$15,711.11.
 - C. \$11,498.73.
 - D. \$10,202.35.
15. On January 1, 2012, a company has assets of \$16 billion and shareholders' equity of \$8 billion. On December 31, 2012, the same company has assets of \$20 billion and shareholders' equity of \$9 billion. During 2012, the company had total sales revenue of \$900 million and total expenses of \$700 million. The company's asset turnover ratio for 2012 is:
- A. 0.25
 - B. 0.05
 - C. 0.045
 - D. 0.01
16. When a dividend has been declared but not yet paid,
- A. assets will increase and shareholders' equity will decrease.
 - B. assets will decrease and shareholders' equity will increase.
 - C. the statement of financial position will not change until the dividend is paid.
 - D. liabilities will increase and shareholders' equity will decrease.
17. Purrfect Ltd. announces that its gross profit rose 5% and its net profit decreased. Which of the following statements is true?
- A. This is not possible given that net profit is determined by gross profit.
 - B. Other expenses must have risen more than 5%.
 - C. Other expenses must have decreased.
 - D. Sales revenue must have decreased.
18. Which of the following is a possible adjusting journal entry?
- A. Debit Cash, credit Accounts Payable.
 - B. Debit Service Revenue, credit Cash.
 - C. Debit Salaries Expense, credit Salaries Payable.
 - D. Debit Utilities Expense, credit Retained Earnings.

Question 2 (14 marks; 35 minutes):***Journal Entries*****Part A: Recording Transactions (6 Marks)**

Bronco Corporation uses accrual accounting to record revenues and expenses, and had the following transactions during 2013:

- a. January 1: Paid two years' worth for rent to its landlord in the amount of \$24,000.
- b. July 1: Purchased machinery for \$10,000 cash. This machinery was thought to have a useful life of 5 years with no salvage value.
- c. August 1: Purchased merchandise inventory for \$2,000,000 on account.
- d. September 1: Sold merchandise to a client for \$1,000,000 on account. Bronco's gross profit percentage is 30%.
- e. November 1: Received \$120,000 from a client for services to be performed evenly through April 30, 2014.

Required

Prepare journal entries in the proper format for the above transactions. Please skip a line between journal entries and omit narratives.

Part B: Closing Entries (4 Marks)

A partial list of Bangle Inc.'s account balances as at December 31, 2013 are shown below. All accounts have "normal" debit or credit balances.

Cash	\$ 10,000	Trade Payables	\$ 30,000
Trade Receivables	50,000	Cost of Goods Sold	120,000
Land	100,000	Loan Payable	40,000
Sales Revenue	200,000	Common shares	100,000
Sales Discounts	10,000	Operating Expenses	5,000
Sales Returns and Allowances	5,000	Interest Expense	3,000

Required

Prepare Bangle Inc.'s closing journal entries for the year ended December 31, 2013.

Part C: Correcting Erroneous Journal Entries (4 Marks)

Snow White works as an accountant for Seven Dwarfs, Ltd. She has prepared the following journal entries; however, being new to the job, she is not sure whether her journal entries are correct. You are a very good friend of Snow White. Having taken COMM 217 at Concordia, you are confident that you can help her to correct erroneous journal entries.

March 1: Yvonne Bushes gave Seven Dwarfs a truck worth \$30,000 in exchange of 10,000 common shares for the same value.

Cash.....	30,000	
Truck		30,000

May 1: Seven Dwarfs borrowed \$100,000 from DT bank at 6% for 6 months.

Cash.....	100,000	
Interest Expenses	3,000	
Loan.....		103,000

August 31: Seven Dwarfs hired Mary Pumpkin as the Chief Financial Officer and promised to pay her an annual salary of \$150,000. Mary Pumpkin is expected to start her job on January 1st, 2014.

No journal entry was recorded.

December 31: Snow White prepared adjusting entries to record depreciation expense of a machine purchased two years earlier. The machine was purchased for \$30,000, had an estimated useful life of 10 years with no salvage value.

Depreciation Expense	3,000	
Machinery.....		3,000

Required

If you think Snow White’s original journal entries are incorrect, prepare correct journal entries. If you think Snow White’s original journal entries are correct, write “No correction is required” and briefly explain the reason.

Question 3 (36 marks; 60 minutes): *Financial Statements*

Packers Ltd. manufactures small gadgets. Below is a list of accounts and their unadjusted balances as at **December 30, 2012** – prepared one day before the company's fiscal year end. Each account has a "normal" debit or credit balance, as the term is defined in the textbook.

Accumulated depreciation	\$ 50,000
Cash	5,000
Cost of Goods Sold	1,000,000
Equipment	102,000
General and administrative expenses	88,000
Inventories	200,000
Land	1,400,000
Notes payable (6%, 20 years, due December 31, 2020)	1,000,000
Rent revenue	20,000
Retained earnings	81,000
Sales revenue	2,000,000
Sales returns and allowances	100,000
Share capital (150,000 shares)	150,000
Small tools	20,000
Trade payables	45,000
Trade receivables	75,000
Wages expenses	356,000

You have obtained the following information:

- The company declared cash dividend of 10 cents (\$0.10) per share on December 31, 2012. The dividend is to be paid in January 2013.
- The company received a \$3,000 deposit on December 31, 2012 for work to be commenced in January 2013.
- As of December 31, 2012, wages earned but not yet paid totaled \$4,000.
- Small tools worth \$9,000 were on hand on December 31, 2012.
- The equipment's useful life is ten years and its residual value is \$2,000. The company uses the **straight-line method** to record depreciation.
- The company uses the percentage of credit sales method to estimate bad debts. 80% of the company's sales were on credit and the bad debt rate is 1%. In fiscal year 2012, all sales returns and allowances are related to cash sales only.
- The company is subject to an income tax rate of 20%.

Required

1. Record journal entries and all necessary adjusting entries. (11 Marks)
2. Prepare in proper form a classified ("multi-step") income statement for fiscal year 2012. (11 Marks)
3. Prepare in proper form a classified statement of financial position (balance sheet) as at December 31, 2012. (14 Marks)

Question 4 (23 marks; 40 minutes)

Trade Receivables and Bad Debt

O'Reily Corp. had the following events during its final three months of the fiscal year ending on May 31, 2013.

- (a) March 28: Sold \$800 of merchandise to Andrew on account.
- (b) March 29: Andrew returned \$150 of the merchandise purchased on March 28.
- (c) April 3: Sold \$2,400 of merchandise to Michael. Michael used a VISA credit card to pay for his purchase. A 3% service fee is charged by VISA.
- (d) April 6: Andrew paid off the balance of his account.
- (e) April 14: Wrote-off an old account for \$ 1,500 which is related to sales made prior to March 1, 2013.
- (f) April 25: Patel purchased \$6,000 of merchandise, paid half in cash.
- (g) May 30: O'Reily recovered \$500 from the receivables that were written-off on April 14.

Additional information:

- Credit terms: 2/10, n/30
- Andrew has a balance of \$500 outstanding as of March 1, 2013, from purchases made on January 10, 2013.
- O'Reily's records show the following account balances as of March 1, 2013:

Trade Receivables	\$ 8,500
Allowances of Doubtful Account (credit balance).....	500
Net Credit Sales.....	95,500
Cash Sales	50,000

Required

1. Prepare the journal entries to record the above transactions (11 Marks).
2. O'Reily uses **the Aging of Trade Receivables method** to determine the amount of receivables that may not be collected in the future according to the following schedule:

	Estimated Uncollectible Rate
Not yet due.....	5%
1-30 days past due.....	10%
31-60 days past due.....	15%
More than 60 days past due.....	20%

Determine the amount of receivables that may not be collected in the future, and prepare the journal entry to record the bad debt expense on May 31, 2013. Show all your calculations. (6 Marks)

3. Suppose O'Reily estimate bad debts to equal 1% of its **Net Credit Sales**. Would O'Reily incur a higher or lower bad debt expense for the fiscal year ending on May 31, 2013? Show your calculations. (3 Marks)
4. O'Reily's Trade Receivables account had a balance of \$8,500 at May 31, 2012. Compute the Trade Receivables Turnover ratio for O'Reily. Comment also on its ability to collect account receivables. (3 Marks)