Suggested solution -- ACCO 230 Midterm exam, May 2013

Question 1 -- Multiple-choice

1. c
2. d
3. c
4. b
5. d
6. b
7. a
8. a
9. a
10. e

11. a
12. a
13. e
14. b
15. a
16. c
17. b
18. d
19. e
20. c

Suggested solution -- ACCO 230 Midterm exam, May 2013

Question 2

1-a.

NM Ltd.
Income Statement
For the Year Ended December 31, 2012

Sales revenue		$210,000
Less: Sales returns and allowances		6,000
Net sales		204,000
Cost of goods sold		77,000
Gross profit		127,000
Operating expenses		
Salaries	$38,000	
Rent	34,000	
Promotional and advertising	20,000	
Depreciation	14,000	106,000
Operating income		21,000
Other income (expense)		
Interest income	2,000	
Interest expense	(3,000)	(1,000)
Income before income tax		20,000
Income tax expense		7,000
Net income		$13,000

Suggested solution -- ACCO 230 Midterm exam, May 2013

Question 2 -- 1-b.

NM Ltd.
Balance Sheet (partial)
As at December 31, 2012

ASSETS

Current assets		
Cash		$10,000
Trade receivables		11,000
Merchandise inventory		45,000
Prepaid rent		24,000
Total current assets		90,000
Non-current assets		
Equipment, at cost	$103,000	
Less: Accumulated depreciation	35,000	
Book value		68,000
Total assets		$158,000

==

2. Closing journal entries

Sales	210,000	
Interest income	2,000	
Retained earnings		212,000
Retained earnings	199,000	
Sales returns and allowances		6,000
Cost of goods sold		77,000
Salaries expense		38,000
Rent expense		34,000
Promotional and advertising expense		20,000
Depreciation expense		14,000
Interest expense		3,000
Income tax expense		7,000

<u>Question 2 -- 3.</u>

Gross profit percentage = $127,000 / $204,000 = 62.3%.

The gross profit percentage is a basic measure of profitability for merchandising firms. It shows the percentage of profit earned on merchandising transactions before other expenses, including income taxes, are considered.

Current ratio = $90,000 / ($8,000 + $7,000 + $64,000 + $4,000) = 1.08

The current ratio is a basic measure of liquidity. It shows how well the firm is able to meet its current liabilities as they generally come due. A ratio of 2 to 1 (2.0) is considered adequate. NM's current ratio is far below that figure and may suggest that liquidity is a serious concern for the company and its creditors.

==

4. Accumulated depreciation, 12-31-12 = $35,000
   Depreciation expense (straight-line) for 2012 = $14,000

   Age of equipment (in years), 12-31-12 = $35,000 / $14,000 = 2.5 years.

   Therefore, the equipment was placed into service about mid-way during the year 2010.

==

5. Total shareholders' equity, 12-31-12 = $25,000 + $37,000 + $13,000

   = $75,000

==

Suggested solution -- ACCO 230 Midterm exam, May 2013

Question 3

April 1	Cash	10,000,000	
	Common share capital		10,000,000
April 2	Office supplies	1,500	
	Trade payables		1,500
April 3	Office furniture	20,000	
	Equipment	30,000	
	Cash		50,000
April 4	Cash	200,000	
	Loan payable		200,000
April 6	Trade receivables	35,000	
	Service revenue		35,000
April 7	Trade payables	300	
	Cash		300
April 15	Cash	9,000	
	Trade receivables		9,000
April 20	Retained earnings (or, Dividends)	100,000	
	Cash		100,000
April 30	Salaries expense	17,000	
	Cash		17,000

Question 4

a. Periodic method.

May 4	Purchases	3,250	
	Trade payables		3,250
	[25 x $130 = $3,250]		
May 5	"No entry"		
May 6	Trade receivables	5,720	
	Sales revenue		5,720
	[22 x $260 = $5,720]		
May 7	Trade payables	390	
	Purchase returns and allowances		390
May 8	Trade receivables	1,040	
	Sales revenue		1,040
	[4 x $260 = $1,040]		
May 9	Transportation-out (or, Delivery expense)	350	
	Cash		350
May 10	"No entry"		
May 11	Sales returns and allowances	520	
	Trade receivables		520
	[2 x $260 = $520]		

Question 4 -- a, continued

May 12	Trade payables	2,860	
	Purchase discounts		57
	Cash		2,803
	[$3,250 - $390 = $2,860]		
	[$2,860 x .02 = $57 (rounded)]		
May 14	Cash	5,096	
	Sales discounts	104	
	Trade receivables		5,200
	[$5,720 - $520 = $5,200]		
	[$5,200 x .02 = $104]		
May 24	Cash	1,040	
	Trade receivables		1,040

Suggested solution -- ACCO 230 Midterm exam, May 2013

Question 4 -- b

Perpetual method (selected transactions)

May 4	Merchandise inventory	3,250	
	Trade payables		3,250
May 6	Trade receivables	5,720	
	Sales revenue		5,720
	Cost of goods sold	2,860	
	Merchandise inventory		2,860
	[22 x $130 = $2,860]		
May 7	Trade payables	390	
	Merchandise inventory		390
May 11	Sales returns and allowances	520	
	Trade receivables		520
	Merchandise inventory	260	
	Cost of goods sold		260
	[2 x $130 = $260]		

Suggested solution -- ACCO 230 Midterm exam, May 2013

Question 5

1. Adjusting journal entries

		Debit	Credit
a.	Rent expense	8,000	
	Prepaid rent		8,000
	[$4,000 x 2 = $8,000]		
b.	Depreciation expense	8,750	
	Accumulated depreciation (equipment)		8,750
	[$175,000 / 20 = $8,750]		
c.	Retained earnings (or, Dividends)	10,000	
	Dividends payable		10,000
d.	Insurance expense	16,000	
	Prepaid insurance		16,000
	[$24,000 / 18 x 12 = $16,000]		
e.	Interest expense	4,320	
	Interest payable		4,320
	[$72,000 x 6% x 12 / 12 = $4,320]		
f.	Unearned revenue	5,400	
	Service revenue		5,400
	[$9,000 x 60% = $5,400]		
g.	Trade receivables	700	
	Cash		700
h.	Income tax expense	25,000	
	Income taxes payable		25,000

Question 5, continued

2.

Dividends payable	10,000	
Cash		10,000

==

3.

Note payable	72,000	
Cash		72,000

Interest expense	720	
Interest payable	12,240	
Cash		12,960

[$72,000 x 6% x 2/12 = $720; interest for Jan. and Feb. 2013]

[$72,000 x 6% x 34/12 = $12,240; interest accrued in the accounts from March 1, 2010 to December 31, 2012 (34 months)]

==

4. Accumulated depreciation (equipment), 12-31-12 = $26,250 *

$26,250 / $8,750 = 3 years old as at 12-31-12 (straight-line method)

Therefore, estimated remaining life, 12-31-12 = 20 - 3 = 17 years.

* $17,500 + $8,750 (aje "a") = $26,250

(There are other ways to derive the correct answer.)

==