# *Accounting 30th edition Warren Solutions Manual*

SKU: 9798214053011-SOLUTIONS

# CHAPTER 1
# INTRODUCTION TO ACCOUNTING AND BUSINESS

## DISCUSSION QUESTIONS

**1.** Some users of accounting information include managers, employees, investors, creditors, customers, and the government.

**2.** The role of accounting is to provide information for managers to use in operating the business. In addition, accounting provides information to others to use in assessing the economic performance and condition of the business.

**3.** The corporate form allows the company to obtain large amounts of resources by issuing stock. For this reason, most companies that require large investments in property, plant, and equipment are organized as corporations.

**4.** No. The business entity assumption limits the recording of economic data to transactions directly affecting the activities of the business. The payment of the interest of $4,500 is a personal transaction of Josh Reilly and should not be recorded by Dispatch Delivery Service.

**5.** The land should be recorded at its cost of $167,500 to Reliable Repair Service. This is consistent with the cost principle.

**6.** **a.** No. The offer of $2,000,000 and the increase in the assessed value should not be recognized in the accounting records.

**b.** Cash would increase by $2,125,000, land would decrease by $900,000, and owner's capital would increase by $1,225,000.

**7.** An account receivable is a claim against a customer for goods or services sold. An account payable is an amount owed to a creditor for goods or services purchased. Therefore, an account receivable in the records of the seller is an account payable in the records of the purchaser.

**8.** **(b)** The business realized net income of $91,000 ($679,000 – $588,000).

**9.** **(a)** The business incurred a net loss of $75,000 ($640,000 – $715,000).

**10.** **(a)** Net income or net loss
**(b)** Owner's capital at the end of the period
**(c)** Cash at the end of the period

## BASIC EXERCISES

**BE 1–1**

**$190,000. Under the cost principle, the land should be recorded at the cost to Upstate Metal Roofing.**

**BE 1–2**

**a.**

| | | |
|---:|:---:|:---|
| **A** | **=** | **L + OE** |
| **$710,000** | **=** | **$195,000 + OE** |
| **OE** | **=** | **$515,000** |

**b.**

| | | |
|---:|:---:|:---|
| **A** | **=** | **L + OE** |
| **$710,000 + $125,000** | **=** | **$195,000 + $25,000 + OE** |
| **$835,000** | **=** | **$220,000 + OE** |
| **OE** | **=** | **$615,000** |

**BE 1–3**

**(2) Expense (Advertising Expense) increases by $8,500;**
**Asset (Cash) decreases by $8,500.**

**(3) Asset (Supplies) increases by $3,200;**
**Liability (Accounts Payable) increases by $3,200.**

**(4) Asset (Accounts Receivable) increases by $31,750;**
**Revenue (Delivery Service Fees) increases by $31,750.**

**(5) Asset (Cash) increases by $27,700;**
**Asset (Accounts Receivable) decreases by $27,700.**

**BE 1–4**

| Worldwide Travel<br>Income Statement<br>For the Year Ended July 31, 20Y6 | | |
|---|---:|---:|
| Fees earned | | $ 1,175,000 |
| Expenses: | | |
| Salary and wages expense | $776,000 | |
| Office expense | 175,000 | |
| Miscellaneous expense | 80,000 | |
| Total expenses | | (1,031,000) |
| Net income | | $ 144,000 |
| | | |

**BE 1–5**

| Worldwide Travel<br>Statement of Owner's Equity<br>For the Year Ended July 31, 20Y6 | |
|---|---|
| Sheldon LaCount, capital, August 1, 20Y5 | $670,000 |
| Additional investment by owner | 60,000 |
| Net income for the year | 144,000 |
| Withdrawals | (35,000) |
| Sheldon LaCount, capital, July 31, 20Y6 | $839,000 |
| | |

**BE 1–6**

| Worldwide Travel<br>Balance Sheet<br>July 31, 20Y6 | |
|---|---|
| Assets | |
| Cash | $143,450 |
| Accounts receivable | 42,750 |
| Supplies | 3,800 |
| Land | 675,000 |
| Total assets | $865,000 |
| Liabilities | |
| Accounts payable | $ 26,000 |
| Owner's Equity | |
| Sheldon LaCount, capital | 839,000 |
| Total liabilities and owner's equity | $865,000 |
| | |

**BE 1–7**

| Worldwide Travel<br>Statement of Cash Flows<br>For the Year Ended July 31, 20Y6 | | |
|---|---|---|
| Cash flows from (used for) operating activities: | | |
| Cash received from customers | $ 1,225,000 | |
| Cash paid for operating expenses | (1,116,050) | |
| Net cash flows from operating activities | | $108,950 |
| Cash flows from (used for) investing activities: | | |
| Cash paid for purchase of land | | (50,000) |
| Cash flows from (used for) financing activities: | | |
| Cash received from owner's investment | $ 60,000 | |
| Cash paid for owner withdrawals | (35,000) | |
| Net cash flows from financing activities | | 25,000 |
| Net increase in cash | | $ 83,950 |
| Cash balance, August 1, 20Y5 | | 59,500 |
| Cash balance, July 31, 20Y6 | | $143,450 |

**BE 1–8**

a.

| | Dec. 31, 20Y4 | Dec. 31, 20Y3 |
|---|---|---|
| Total liabilities | $4,085,000 | $2,880,000 |
| Total stockholders' equity | $4,300,000 | $3,600,000 |
| Ratio of liabilities to stockholders' equity | 0.95* | 0.80** |

* $4,085,000 ÷ $4,300,000
** $2,880,000 ÷ $3,600,000

b. Increased

## EXERCISES

**Ex. 1–1**

**a.**

| | | |
|---|---|---|
| **1. manufacturing** | **6. merchandising** | **11. service** |
| **2. manufacturing** | **7. manufacturing** | **12. service** |
| **3. manufacturing** | **8. service** | **13. manufacturing** |
| **4. service** | **9. manufacturing** | **14. service** |
| **5. merchandising** | **10. merchandising** | **15. merchandising** |

**b. The accounting equation is relevant to all companies. It serves as the basis of the accounting information system.**

**Ex. 1–2**

**As in many ethics issues, there is no one right answer. Oftentimes, disclosing only what is legally required may not be enough. In this case, it would be best for the company's chief executive officer to disclose both reports to the county representatives. In doing so, the chief executive officer could point out any flaws or deficiencies in the fired researcher's report.**

**Ex. 1–3**

**a.**

| | | |
|---|---|---|
| **1. X** | **5. O** | **9. X** |
| **2. L** | **6. O** | **10. O** |
| **3. O** | **7. X** | |
| **4. M** | **8. L** | |

**b. A business transaction is an economic event or condition that directly changes an entity's financial condition or results of operations.**

**Ex. 1–4**

**Kroger's stockholders' equity: $50,505 – $38,904 = $11,601**
**Procter & Gamble's stockholders' equity: $122,370 – $71,811 = $50,559**

**Ex. 1–5**

**Dollar Tree's stockholders' equity: $22,023 – $14,710 = $7,313**
**Target's stockholders' equity: $55,356 – $41,924 = $13,432**

**Ex. 1–6**

a. Aquadyne Designs: $3,000,000 ($1,000,000 + $2,000,000)
b. Morales & Associates: $2,500,000 ($6,000,000 – $3,500,000)
c. Omega Power Consultants: $6,000,000 ($10,000,000 – $4,000,000)

**Ex. 1–7**

a. $1,270,000 ($2,450,000 – $1,180,000)
b. $1,580,000 ($1,270,000 + $825,000 – $515,000)
c. $835,000 ($1,270,000 – $375,000 – $60,000)
d. $2,115,000 ($1,270,000 + $725,000 + $120,000)
e. Net income: $630,000 ($3,300,000 – $1,400,000 – $1,270,000)

**Ex. 1–8**

a. (2) liability
b. (1) asset
c. (3) owner's equity (revenue)
d. (1) asset
e. (3) owner's equity (expense)
f. (3) owner's equity (expense)

**Ex. 1–9**

a. Increases assets and increases owner's equity.
b. Decreases assets and decreases owner's equity.
c. Decreases assets and decreases owner's equity.
d. Increases assets and increases liabilities.
e. Increases assets and increases owner's equity.

**Ex. 1–10**

a. (1) Total assets increased $183,000 ($298,000 – $115,000).
   (2) No change in liabilities.
   (3) Owner's equity increased $183,000.

b. (1) Total assets decreased $80,000.
   (2) Total liabilities decreased $80,000.
   (3) No change in owner's equity.

c. No, it is false that a transaction always affects at least two elements (Assets, Liabilities, or Owner's Equity) of the accounting equation. Some transactions affect only one element of the accounting equation. For example, purchasing supplies for cash only affects assets.

**Ex. 1–11**

1. (a) increase
2. (a) increase
3. (b) decrease
4. (b) decrease

**Ex. 1–12**

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

**Ex. 1–13**

a. (1) Provided catering services for cash, $71,800.
(2) Purchase of land for cash, $15,000.
(3) Payment of cash for expenses, $47,500.
(4) Purchase of supplies on account, $1,100.
(5) Paid cash to owner for personal use, $5,000.
(6) Payment of cash to creditors, $4,000.
(7) Recognition of cost of supplies used, $1,500.

b. $300 ($40,300 – $40,000)
c. $17,800 (–$5,000 + $71,800 – $49,000)
d. $22,800 ($71,800 – $49,000)
e. $17,800 ($22,800 – $5,000)

**Ex. 1–14**

No. It would be incorrect to say that the business had incurred a net loss of $8,000. The excess of owner withdrawals over the net income for the period is a decrease in the amount of owner's equity (capital) in the business.

**Ex. 1–15**

**Amber**

| | |
|---|---|
| Owner's equity at end of year ($1,730,000 – $1,150,000) | $ 580,000 |
| Deduct owner's equity at beginning of year ($1,220,000 – $990,000) | (230,000) |
| Net income (increase in owner's equity) | $ 350,000 |

**Blue**

| | |
|---|---|
| Increase in owner's equity (as determined for Amber) | $ 350,000 |
| Add owner withdrawals | 60,000 |
| Net income | $ 410,000 |

**Coral**

| | |
|---|---|
| Increase in owner's equity (as determined for Amber) | $ 350,000 |
| Deduct additional investment by owner | (140,000) |
| Net income | $ 210,000 |

**Daffodil**

| | |
|---|---|
| Increase in owner's equity (as determined for Amber) | $ 350,000 |
| Deduct additional investment by owner | (140,000) |
| | $ 210,000 |
| Add owner withdrawals | 60,000 |
| Net income | $ 270,000 |

**Ex. 1–16**

**Balance sheet items: 1, 2, 3, 5, 7, 8, 10**

**Ex. 1–17**

**Income statement items: 4, 6, 9**

**Ex. 1–18**

a.

| Organic Products Company<br>Statement of Owner's Equity<br>For the Month Ended June 30, 20Y9 | |
|---|---|
| Billie Soares, capital, June 1, 20Y9 | $1,810,000 |
| Additional investment by owner | 50,000 |
| Net income for June | 115,000 |
| Withdrawals | (25,000) |
| Billie Soares, capital, June 30, 20Y9 | $1,950,000 |

b. The statement of owner's equity is prepared before the June 30, 20Y9, balance sheet since Billie Soares, Capital as of June 30, 20Y9, is needed for the June 30, 20Y9, balance sheet.

**Ex. 1–19**

| Imaging Services<br>Income Statement<br>For the Month Ended March 31, 20Y5 | | |
|---|---|---|
| Fees earned | | $ 482,000 |
| Expenses: | | |
| Wages expense | $300,000 | |
| Rent expense | 41,500 | |
| Supplies expense | 3,600 | |
| Miscellaneous expense | 1,900 | |
| Total expenses | | (347,000) |
| Net income | | $ 135,000 |

**Ex. 1–20**

**In each case, solve for a single unknown, using the following equation:**

**Owner's Equity (beginning) + Additional Investments by Owner – Withdrawals by Owner + Revenues – Expenses = Owner's Equity (ending)**

**Freeman**

| | | |
|---|---|---|
| Owner's equity at end of year ($1,260,000 – $330,000) | | $ 930,000 |
| Owner's equity at beginning of year ($900,000 – $360,000) | | (540,000) |
| Increase in owner's equity | | $ 390,000 |
| Deduct increase due to net income ($570,000 – $240,000) | | (330,000) |
| | | $ 60,000 |
| Add withdrawals by owner | | 75,000 |
| Additional investment by owner | (a) | $ 135,000 |

**Heyward**

| | | |
|---|---|---|
| Owner's equity at end of year ($675,000 – $220,000) | | $ 455,000 |
| Owner's equity at beginning of year ($490,000 – $260,000) | | (230,000) |
| Increase in owner's equity | | $ 225,000 |
| Add withdrawals by owner | | 32,000 |
| | | $ 257,000 |
| Deduct additional investment by owner | | (150,000) |
| Increase due to net income | | $ 107,000 |
| Add expenses | | 128,000 |
| Revenue | (b) | $ 235,000 |

**Jones**

| | | |
|---|---|---|
| Owner's equity at end of year ($100,000 – $80,000) | | $ 20,000 |
| Owner's equity at beginning of year ($115,000 – $81,000) | | (34,000) |
| Decrease in owner's equity | | $(14,000) |
| Decrease in owner's equity due to net loss ($115,000 – $122,500) | | 7,500 |
| | | $ (6,500) |
| Deduct additional investment by owner | | (10,000) |
| Withdrawals by owner | (c) | $(16,500) |

**Ramirez**

| | | |
|---|---|---|
| Owner's equity at end of year ($270,000 – $136,000) | | $134,000 |
| Add decrease due to net loss ($115,000 – $128,000) | | 13,000 |
| | | $147,000 |
| Add withdrawals by owner | | 39,000 |
| Owner's equity at beginning of year | | $186,000 |
| Deduct additional investment by owner | | (55,000) |
| | | $131,000 |
| Add liabilities at beginning of year | | 120,000 |
| Assets at beginning of year | (d) | $251,000 |

**Ex. 1–21**

**a.**

| Ebony Interiors<br>Balance Sheet<br>February 28, 20Y3 | |
|---|---|
| **Assets** | |
| Cash | $ 320,000 |
| Accounts receivable | 800,000 |
| Supplies | 30,000 |
| Total assets | $1,150,000 |
| **Liabilities** | |
| Accounts payable | $ 310,000 |
| **Owner's Equity** | |
| Kylar Gee, capital | 840,000* |
| Total liabilities and owner's equity | $1,150,000 |

* $840,000 = $320,000 + $800,000 + $30,000 – $310,000

| Ebony Interiors<br>Balance Sheet<br>March 31, 20Y3 | |
|---|---|
| **Assets** | |
| Cash | $ 380,000 |
| Accounts receivable | 960,000 |
| Supplies | 35,000 |
| Total assets | $1,375,000 |
| **Liabilities** | |
| Accounts payable | $ 400,000 |
| **Owner's Equity** | |
| Kylar Gee, capital | 975,000* |
| Total liabilities and owner's equity | $1,375,000 |

* $975,000 = $380,000 + $960,000 + $35,000 – $400,000

**b.**

| | |
|---|---|
| Owner's equity, March 31 | $ 975,000 |
| Owner's equity, February 28 | (840,000) |
| Net income | $ 135,000 |

**Ex. 1–21 (Concluded)**

| | | |
|---|---|---|
| c. | Owner's equity, March 31 | $ 975,000 |
| | Owner's equity, February 28 | (840,000) |
| | Increase in owner's equity | $ 135,000 |
| | Add withdrawals by owner | 50,000 |
| | Net income | $ 185,000 |

**Ex. 1–22**

a. Balance sheet: 1, 2, 3, 4, 6, 7, 8, 9, 10, 11, 13
Income statement: 5, 12, 14, 15

b. Yes, an item can appear on more than one financial statement. For example, cash appears on both the balance sheet and statement of cash flows. However, the same item cannot appear on both the income statement and balance sheet.

c. Yes, the accounting equation is relevant to all companies, including Exxon Mobil Corporation. The accounting equation is the basis for all accounting systems.

**Ex. 1–23**

1. (c) financing activity
2. (a) operating activity
3. (b) investing activity
4. (c) financing activity

**Ex. 1–24**

| Parker Consulting Group<br>Statement of Cash Flows<br>For the Year Ended January 31, 20Y4 | | |
|---|---|---|
| Cash flows from (used for) operating activities: | | |
| Cash received from customers | $1,200,000 | |
| Cash paid for operating expenses | (800,000) | |
| Net cash flows from operating activities | | $ 400,000 |
| Cash flows from (used for) investing activities: | | |
| Cash paid for purchase of land | | (300,000) |
| Cash flows from (used for) financing activities: | | |
| Cash received from owner's investment | $ 90,000 | |
| Cash paid for owner withdrawals | (36,000) | |
| Net cash flows from financing activities | | 54,000 |
| Net increase in cash | | $ 154,000 |
| Cash balance, February 1, 20Y3 | | 66,000 |
| Cash balance, January 31, 20Y4 | | $ 220,000 |

**Ex. 1–25**

**a. 1. All financial statements should contain the name of the business in their heading. The statement of owner's equity is incorrectly headed as "Omar Farah" rather than "We-Sell Realty." The heading of the balance sheet needs to include the name of the business.**

**2. The income statement covers a period of time and should be labeled "For the Month Ended August 31, 20Y7."**

**3. The year in the heading for the statement of owner's equity should be 20Y7 rather than 20Y6.**

**4. The balance sheet should be labeled "August 31, 20Y7," rather than "For the Month Ended August 31, 20Y7."**

**5. On the income statement, the miscellaneous expense amount should be listed as the last expense.**

**6. On the income statement, the total expenses are subtracted from the sales commissions, resulting in an incorrect net income amount of $25,000. The correct net income should be $24,150. This also affects the statement of owner's equity and the amount of Omar Farah, capital that appears on the balance sheet.**

**7. The statement of owner's equity should be for the "month" rather than for the "year" ended August 31, 20Y7. In addition, the investment by Omar Farah to organize We-Sell Realty of $15,000 is not reported.**

**8. Accounts payable should be listed as a liability on the balance sheet.**

**9. Accounts receivable and supplies should be listed as assets on the balance sheet.**

**10. The balance sheet assets should equal the sum of the liabilities and owner's equity.**

**Ex. 1–25 (Concluded)**

**b. Corrected financial statements appear as follows:**

| We-Sell Realty<br>Income Statement<br>For the Month Ended August 31, 20Y7 | | |
|---|---|---|
| Sales commissions | | $ 140,000 |
| Expenses: | | |
| Office salaries expense | $87,000 | |
| Rent expense | 18,000 | |
| Automobile expense | 7,500 | |
| Supplies expense | 1,150 | |
| Miscellaneous expense | 2,200 | |
| Total expenses | | (115,850) |
| Net income | | $ 24,150 |

| We-Sell Realty<br>Statement of Owner's Equity<br>For the Month Ended August 31, 20Y7 | |
|---|---|
| Omar Farah, capital, August 1, 20Y7 | $ 0 |
| Investment by owner | 15,000 |
| Net income for August | 24,150 |
| Withdrawals | (10,000) |
| Omar Farah, capital, August 31, 20Y7 | $ 29,150 |

| We-Sell Realty<br>Balance Sheet<br>August 31, 20Y7 | |
|---|---|
| Assets | |
| Cash | $ 8,900 |
| Accounts receivable | 38,600 |
| Supplies | 4,000 |
| Total assets | $51,500 |
| Liabilities | |
| Accounts payable | $22,350 |
| Owner's Equity | |
| Omar Farah, capital | 29,150 |
| Total liabilities and owner's equity | $51,500 |

## PROBLEMS

**Prob. 1–1A**

**1.**

| | Assets | | | = Liabilities + | Owner's Equity | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Cash | + Accts. Rec. | + Supplies | = Accts. Payable | + Chris Bates, Capital | – Chris Bates, Drawing | + Fees Earned | – Rent Expense | – Salaries Expense | – Supplies Expense | – Auto Exp. | – Misc. Exp. |
| a. | + 75,000 | | | | + 75,000 | | | | | | | |
| b. | | | + 2,200 | + 2,200 | | | | | | | | |
| Bal. | 75,000 | | 2,200 | 2,200 | 75,000 | | | | | | | |
| c. | + 19,500 | | | | | | + 19,500 | | | | | |
| Bal. | 94,500 | | 2,200 | 2,200 | 75,000 | | 19,500 | | | | | |
| d. | – 8,000 | | | | | | | – 8,000 | | | | |
| Bal. | 86,500 | | 2,200 | 2,200 | 75,000 | | 19,500 | – 8,000 | | | | |
| e. | – 1,850 | | | – 1,850 | | | | | | | | |
| Bal. | 84,650 | | 2,200 | 350 | 75,000 | | 19,500 | – 8,000 | | | | |
| f. | | + 6,000 | | | | | + 6,000 | | | | | |
| Bal. | 84,650 | 6,000 | 2,200 | 350 | 75,000 | | 25,500 | – 8,000 | | | | |
| g. | – 2,300 | | | | | | | | | | – 1,500 | – 800 |
| Bal. | 82,350 | 6,000 | 2,200 | 350 | 75,000 | | 25,500 | – 8,000 | | | – 1,500 | – 800 |
| h. | – 5,500 | | | | | | | | – 5,500 | | | |
| Bal. | 76,850 | 6,000 | 2,200 | 350 | 75,000 | | 25,500 | – 8,000 | – 5,500 | | – 1,500 | – 800 |
| i. | | | – 1,650 | | | | | | | – 1,650 | | |
| Bal. | 76,850 | 6,000 | 550 | 350 | 75,000 | | 25,500 | – 8,000 | – 5,500 | – 1,650 | – 1,500 | – 800 |
| j. | – 4,000 | | | | | – 4,000 | | | | | | |
| Bal. | 72,850 | 6,000 | 550 | 350 | 75,000 | – 4,000 | 25,500 | – 8,000 | – 5,500 | – 1,650 | – 1,500 | – 800 |

2. Owner's equity is the rights of the owner to the assets of the business. These rights are increased by owner investments and revenues and decreased by owner withdrawals and expenses.

3. $8,050 ($25,500 – $8,000 – $5,500 – $1,650 – $1,500 – $800)

4. June's transactions increased owner's equity by $79,050, which is the owner's initial investment of $75,000 plus June's net income of $8,050 less the owner's withdrawal of $4,000.

**Prob. 1–2A**

1.

| Preferred Travel Agency<br>Income Statement<br>For the Year Ended December 31, 20Y5 | | |
|---|---|---|
| Fees earned | | $1,075,000 |
| Expenses: | | |
| Wages expense | $615,000 | |
| Rent expense | 170,000 | |
| Utilities expense | 51,500 | |
| Supplies expense | 16,000 | |
| Miscellaneous expense | 22,500 | |
| Total expenses | | (875,000) |
| Net income | | $ 200,000 |

2.

| Preferred Travel Agency<br>Statement of Owner's Equity<br>For the Year Ended December 31, 20Y5 | |
|---|---|
| Irvin Dempski, capital, January 1, 20Y5 | $ 973,000 |
| Additional investment by owner | 60,000 |
| Net income for the year | 200,000 |
| Withdrawals | (25,000) |
| Irvin Dempski, capital, December 31, 20Y5 | $1,208,000 |

3.

| Preferred Travel Agency<br>Balance Sheet<br>December 31, 20Y5 | |
|---|---|
| **Assets** | |
| Cash | $ 65,500 |
| Accounts receivable | 90,000 |
| Supplies | 4,500 |
| Land | 1,100,000 |
| Total assets | $1,260,000 |
| **Liabilities** | |
| Accounts payable | $ 52,000 |
| **Owner's Equity** | |
| Irvin Dempski, capital | 1,208,000 |
| Total liabilities and owner's equity | $1,260,000 |

**Prob. 1–2A (Concluded)**

4. **Ending owner's capital appears on both the statement of owner's equity and the balance sheet. For Preferred Travel Agency, Irvin Dempski, capital as of December 31, 20Y5, of $1,208,000 appears on the statement of owner's equity and the balance sheet.**

**Prob. 1–3A**

1.

| Reliance Financial Services<br>Income Statement<br>For the Month Ended July 31, 20Y2 | | |
|---|---|---|
| Fees earned | | $ 144,500 |
| Expenses: | | |
| Salaries expense | $55,000 | |
| Rent expense | 33,000 | |
| Auto expense | 16,000 | |
| Supplies expense | 4,500 | |
| Miscellaneous expense | 4,800 | |
| Total expenses | | (113,300) |
| Net income | | $ 31,200 |

2.

| Reliance Financial Services<br>Statement of Owner's Equity<br>For the Month Ended July 31, 20Y2 | |
|---|---|
| Seth Feye, capital, July 1, 20Y2 | $ 0 |
| Investment by owner | 50,000 |
| Net income for July | 31,200 |
| Withdrawals | (15,000) |
| Seth Feye, capital, July 31, 20Y2 | $ 66,200 |

**Prob. 1–3A (Concluded)**

3.

| Reliance Financial Services<br>Balance Sheet<br>July 31, 20Y2 | |
|---|---|
| **Assets** | |
| Cash | $32,600 |
| Accounts receivable | 34,500 |
| Supplies | 2,500 |
| Total assets | $69,600 |
| **Liabilities** | |
| Accounts payable | $ 3,400 |
| **Owner's Equity** | |
| Seth Feye, capital | 66,200 |
| Total liabilities and owner's equity | $69,600 |

4. **Optional**

| Reliance Financial Services<br>Statement of Cash Flows<br>For the Month Ended July 31, 20Y2 | | |
|---|---|---|
| Cash flows from (used for) operating activities: | | |
| Cash received from customers | $ 110,000 | |
| Cash paid for expenses and to creditors* | (112,400) | |
| Net cash flows used for operating activities | | $ (2,400) |
| Cash flows from (used for) investing activities | | 0 |
| Cash flows from (used for) financing activities: | | |
| Cash received from owner's investment | $ 50,000 | |
| Cash paid for owner withdrawals | (15,000) | |
| Net cash flows from financing activities | | 35,000 |
| Net increase in cash | | $32,600 |
| Cash balance, July 1, 20Y2 | | 0 |
| Cash balance, July 31, 20Y2 | | $32,600 |

* $3,600 + $33,000 + $20,800 + $55,000; these amounts are taken from the Cash column presented in the problem.

**Prob. 1–4A**

**1.**

| | Assets | | = Liabilities + | Owner's Equity | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Cash | + Supplies | = Accts. Payable | + Brooke Kline, Capital | – Brooke Kline, Drawing | + Sales Comm. | – Salaries Exp. | – Rent Exp. | – Auto Exp. | – Supplies Exp. | – Misc. Exp. |
| a. | + 35,000 | | | + 35,000 | | | | | | | |
| b. | | + 2,750 | + 2,750 | | | | | | | | |
| Bal. | 35,000 | 2,750 | 2,750 | 35,000 | | | | | | | |
| c. | – 1,800 | | – 1,800 | | | | | | | | |
| Bal. | 33,200 | 2,750 | 950 | 35,000 | | | | | | | |
| d. | + 52,800 | | | | | + 52,800 | | | | | |
| Bal. | 86,000 | 2,750 | 950 | 35,000 | | 52,800 | | | | | |
| e. | – 4,500 | | | | | | | – 4,500 | | | |
| Bal. | 81,500 | 2,750 | 950 | 35,000 | | 52,800 | | – 4,500 | | | |
| f. | – 3,000 | | | | – 3,000 | | | | | | |
| Bal. | 78,500 | 2,750 | 950 | 35,000 | – 3,000 | 52,800 | | – 4,500 | | | |
| g. | – 2,300 | | | | | | | | – 1,100 | | – 1,200 |
| Bal. | 76,200 | 2,750 | 950 | 35,000 | – 3,000 | 52,800 | | – 4,500 | – 1,100 | | – 1,200 |
| h. | – 5,250 | | | | | | – 5,250 | | | | |
| Bal. | 70,950 | 2,750 | 950 | 35,000 | – 3,000 | 52,800 | – 5,250 | – 4,500 | – 1,100 | | – 1,200 |
| i. | | – 1,000 | | | | | | | | – 1,000 | |
| Bal. | 70,950 | 1,750 | 950 | 35,000 | – 3,000 | 52,800 | – 5,250 | – 4,500 | – 1,100 | – 1,000 | – 1,200 |

**Prob. 1–4A (Concluded)**

**2.**

| Western Realty<br>Income Statement<br>For the Month Ended August 31, 20Y9 | | |
|---|---|---|
| Sales commissions | | $ 52,800 |
| Expenses: | | |
| Salaries expense | $5,250 | |
| Rent expense | 4,500 | |
| Automobile expense | 1,100 | |
| Supplies expense | 1,000 | |
| Miscellaneous expense | 1,200 | |
| Total expenses | | (13,050) |
| Net income | | $ 39,750 |

| Western Realty<br>Statement of Owner's Equity<br>For the Month Ended August 31, 20Y9 | |
|---|---|
| Brooke Kline, capital, August 1, 20Y9 | $ 0 |
| Investment by owner | 35,000 |
| Net income for August | 39,750 |
| Withdrawals | (3,000) |
| Brooke Kline, capital, August 31, 20Y9 | $71,750 |

| Western Realty<br>Balance Sheet<br>August 31, 20Y9 | |
|---|---|
| **Assets** | |
| Cash | $70,950 |
| Supplies | 1,750 |
| Total assets | $72,700 |
| **Liabilities** | |
| Accounts payable | $ 950 |
| **Owner's Equity** | |
| Brooke Kline, capital | 71,750 |
| Total liabilities and owner's equity | $72,700 |

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**Prob. 1–5A**

**1.**

| | Assets | | | | = Liabilities + | Owner's Equity | |
|---|---|---|---|---|---|---|---|
| | Cash + | Accts. Rec. + | Supplies + | Land = | Accts. Payable + | Joel Palk, Capital – | Joel Palk, Drawing |
| Bal. | 45,000 | 93,000 | 7,000 | 75,000 | 40,000 | 180,000 | |
| a. | + 35,000 | | | | | + 35,000 | |
| Bal. | 80,000 | 93,000 | 7,000 | 75,000 | 40,000 | 215,000 | |
| b. | – 50,000 | | | + 50,000 | | | |
| Bal. | 30,000 | 93,000 | 7,000 | 125,000 | 40,000 | 215,000 | |
| c. | + 32,125 | | | | | | |
| Bal. | 62,125 | 93,000 | 7,000 | 125,000 | 40,000 | 215,000 | |
| d. | – 6,000 | | | | | | |
| Bal. | 56,125 | 93,000 | 7,000 | 125,000 | 40,000 | 215,000 | |
| e. | | | + 2,500 | | + 2,500 | | |
| Bal. | 56,125 | 93,000 | 9,500 | 125,000 | 42,500 | 215,000 | |
| f. | – 22,800 | | | | – 22,800 | | |
| Bal. | 33,325 | 93,000 | 9,500 | 125,000 | 19,700 | 215,000 | |
| g. | | + 84,750 | | | | | |
| Bal. | 33,325 | 177,750 | 9,500 | 125,000 | 19,700 | 215,000 | |
| h. | | | | | + 29,500 | | |
| Bal. | 33,325 | 177,750 | 9,500 | 125,000 | 49,200 | 215,000 | |
| i. | – 14,000 | | | | | | |
| Bal. | 19,325 | 177,750 | 9,500 | 125,000 | 49,200 | 215,000 | |
| j. | + 88,000 | – 88,000 | | | | | |
| Bal. | 107,325 | 89,750 | 9,500 | 125,000 | 49,200 | 215,000 | |
| k. | | | – 3,600 | | | | |
| Bal. | 107,325 | 89,750 | 5,900 | 125,000 | 49,200 | 215,000 | |
| l. | – 12,000 | | | | | | – 12,000 |
| Bal. | 95,325 | 89,750 | 5,900 | 125,000 | 49,200 | 215,000 | – 12,000 |

## Prob. 1–5A (Continued)

| | | | | Owner's Equity (Continued) | | | | |
|---|---|---|---|---|---|---|---|---|
| | + Dry Cleaning Revenue | – Dry Cleaning Exp. | – Wages Exp. | – Rent Exp. | – Supplies Exp. | – Truck Exp. | – Utilities Exp. | – Misc. Exp. |
| Bal. | | | | | | | | |
| a. | | | | | | | | |
| Bal. | | | | | | | | |
| b. | | | | | | | | |
| Bal. | | | | | | | | |
| c. | + 32,125 | | | | | | | |
| Bal. | 32,125 | | | | | | | |
| d. | | | | – 6,000 | | | | |
| Bal. | 32,125 | | | – 6,000 | | | | |
| e. | | | | | | | | |
| Bal. | 32,125 | | | – 6,000 | | | | |
| f. | | | | | | | | |
| Bal. | 32,125 | | | – 6,000 | | | | |
| g. | + 84,750 | | | | | | | |
| Bal. | 116,875 | | | – 6,000 | | | | |
| h. | | – 29,500 | | | | | | |
| Bal. | 116,875 | – 29,500 | | – 6,000 | | | | |
| i. | | | – 7,500 | | | – 2,500 | – 1,300 | – 2,700 |
| Bal. | 116,875 | – 29,500 | – 7,500 | – 6,000 | | – 2,500 | – 1,300 | – 2,700 |
| j. | | | | | | | | |
| Bal. | 116,875 | – 29,500 | – 7,500 | – 6,000 | | – 2,500 | – 1,300 | – 2,700 |
| k. | | | | | – 3,600 | | | |
| Bal. | 116,875 | – 29,500 | – 7,500 | – 6,000 | – 3,600 | – 2,500 | – 1,300 | – 2,700 |
| l. | | | | | | | | |
| Bal. | 116,875 | – 29,500 | – 7,500 | – 6,000 | – 3,600 | – 2,500 | – 1,300 | – 2,700 |

**Prob. 1–5A (Continued)**

**2.**

| D'Lite Dry Cleaners<br>Income Statement<br>For the Month Ended July 31, 20Y4 | | |
|---|---|---|
| Dry cleaning revenue | | $116,875 |
| Expenses: | | |
| Dry cleaning expense | $29,500 | |
| Wages expense | 7,500 | |
| Rent expense | 6,000 | |
| Supplies expense | 3,600 | |
| Truck expense | 2,500 | |
| Utilities expense | 1,300 | |
| Miscellaneous expense | 2,700 | |
| Total expenses | | (53,100) |
| Net income | | $ 63,775 |

| D'Lite Dry Cleaners<br>Statement of Owner's Equity<br>For the Month Ended July 31, 20Y4 | |
|---|---|
| Joel Palk, capital, July 1, 20Y4 | $180,000 |
| Additional investment by owner | 35,000 |
| Net income for July | 63,775 |
| Withdrawals | (12,000) |
| Joel Palk, capital, July 31, 20Y4 | $266,775 |

| D'Lite Dry Cleaners<br>Balance Sheet<br>July 31, 20Y4 | |
|---|---|
| Assets | |
| Cash | $ 95,325 |
| Accounts receivable | 89,750 |
| Supplies | 5,900 |
| Land | 125,000 |
| Total assets | $315,975 |
| Liabilities | |
| Accounts payable | $ 49,200 |
| Owner's Equity | |
| Joel Palk, capital | 266,775 |
| Total liabilities and owner's equity | $315,975 |

**Prob. 1–5A (Concluded)**

**3. Optional**

| D'Lite Dry Cleaners<br>Statement of Cash Flows<br>For the Month Ended July 31, 20Y4 | | |
|---|---|---|
| Cash flows from (used for) operating activities: | | |
| Cash received from customers* | $120,125 | |
| Cash paid for expenses and to creditors** | (42,800) | |
| Net cash flows from operating activities | | $ 77,325 |
| Cash flows from (used for) investing activities: | | |
| Cash paid for acquisition of land | | (50,000) |
| Cash flows from (used for) financing activities: | | |
| Cash received from owner's investment | $ 35,000 | |
| Cash paid for owner withdrawals | (12,000) | |
| Net cash flows from financing activities | | 23,000 |
| Net increase in cash | | $ 50,325 |
| Cash balance, July 1, 20Y4 | | 45,000 |
| Cash balance, July 31, 20Y4 | | $ 95,325 |

* $32,125 + $88,000; these amounts are taken from the Cash column of the spreadsheet in Part 1.

** $6,000 + $22,800 + $14,000; these amounts are taken from the Cash column of the spreadsheet in Part 1.

**Prob. 1–6A**

**a. Fees earned, $750,000 ($275,000 + $475,000)**

**b. Supplies expense, $30,000 ($475,000 – $300,000 – $100,000 – $20,000 – $25,000)**

**c. Investment by owner, $375,000; from the statement of cash flows**

**d. Net income for April, $275,000 from the income statement**

**e. $525,000 ($375,000 + $275,000 – $125,000)**

**f. Total assets, $625,000 ($462,500 + $12,500 + $150,000)**

**g. Jamie D'Angora, capital, $525,000; same as (e)**

**h. Total liabilities and owner's equity, $625,000 ($100,000 + $525,000)**

**i. Cash received from customers, $750,000 ($387,500 + $362,500); this is the same as fees earned (a) since there are no accounts receivable.**

**j. Net cash flows from operating activities, $362,500 ($750,000 – $387,500)**

**k. Cash paid for land, $(150,000)**

**l. Cash paid for owner withdrawals, $(125,000)**

**m. Net cash flows from financing activities, $250,000 ($375,000 – $125,000)**

**n. Net increase in cash, $462,500 ($362,500 – $150,000 + $250,000)**

**o. Cash as of April 30, 20Y0, $462,500; same as (n) since Wolverine Realty was organized on April 1, 20Y0; also cash balance on the balance sheet.**

**Prob. 1–1B**

1\.

| | Assets | | | = Liabilities + | Owner's Equity | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Cash | + Accts. Rec. | + Supplies | = Accts. Payable | + Amy Austin, Capital | – Amy Austin, Drawing | + Fees Earned | – Rent Expense | – Salaries Expense | – Supplies Expense | – Auto Exp. | – Misc. Exp. |
| a. | + 50,000 | | | | + 50,000 | | | | | | | |
| b. | | | + 4,000 | + 4,000 | | | | | | | | |
| Bal. | 50,000 | | 4,000 | 4,000 | 50,000 | | | | | | | |
| c. | – 2,300 | | | – 2,300 | | | | | | | | |
| Bal. | 47,700 | | 4,000 | 1,700 | 50,000 | | | | | | | |
| d. | + 13,800 | | | | | | + 13,800 | | | | | |
| Bal. | 61,500 | | 4,000 | 1,700 | 50,000 | | 13,800 | | | | | |
| e. | – 5,000 | | | | | | | – 5,000 | | | | |
| Bal. | 56,500 | | 4,000 | 1,700 | 50,000 | | 13,800 | – 5,000 | | | | |
| f. | – 1,450 | | | | | | | | | | – 1,150 | – 300 |
| Bal. | 55,050 | | 4,000 | 1,700 | 50,000 | | 13,800 | – 5,000 | | | – 1,150 | – 300 |
| g. | – 2,500 | | | | | | | | – 2,500 | | | |
| Bal. | 52,550 | | 4,000 | 1,700 | 50,000 | | 13,800 | – 5,000 | – 2,500 | | – 1,150 | – 300 |
| h. | | | – 1,300 | | | | | | | – 1,300 | | |
| Bal. | 52,550 | | 2,700 | 1,700 | 50,000 | | 13,800 | – 5,000 | – 2,500 | – 1,300 | – 1,150 | – 300 |
| i. | | + 12,500 | | | | | + 12,500 | | | | | |
| Bal. | 52,550 | 12,500 | 2,700 | 1,700 | 50,000 | | 26,300 | – 5,000 | – 2,500 | – 1,300 | – 1,150 | – 300 |
| j. | – 3,900 | | | | | – 3,900 | | | | | | |
| Bal. | 48,650 | 12,500 | 2,700 | 1,700 | 50,000 | – 3,900 | 26,300 | – 5,000 | – 2,500 | – 1,300 | – 1,150 | – 300 |

2. Owner's equity is the rights of the owner to the assets of the business. These rights are increased by owner investments and revenues and decreased by owner withdrawals and expenses.

3. $16,050 ($26,300 – $5,000 – $2,500 – $1,300 – $1,150 – $300)

4. March's transactions increased owner's equity by $62,150, which is the owner's initial investment of $50,000 plus March's net income of $16,050 less the owner's withdrawal of $3,900.

**Prob. 1–2B**

1.

| Ocean Cruiser<br>Income Statement<br>For the Year Ended February 28, 20Y7 | | |
|---|---|---|
| Fees earned | | $ 875,000 |
| Expenses: | | |
| Wages expense | $525,000 | |
| Rent expense | 75,000 | |
| Utilities expense | 38,000 | |
| Supplies expense | 12,000 | |
| Taxes expense | 10,000 | |
| Miscellaneous expense | 15,000 | |
| Total expenses | | (675,000) |
| Net income | | $ 200,000 |

2.

| Ocean Cruiser<br>Statement of Owner's Equity<br>For the Year Ended February 28, 20Y7 | |
|---|---|
| Todd Colby, capital, March 1, 20Y6 | $180,000 |
| Additional investment by owner | 10,000 |
| Net income for the year | 200,000 |
| Withdrawals | (40,000) |
| Todd Colby, capital, February 28, 20Y7 | $350,000 |

3.

| Ocean Cruiser<br>Balance Sheet<br>February 28, 20Y7 | |
|---|---|
| Assets | |
| Cash | $156,000 |
| Accounts receivable | 210,000 |
| Supplies | 9,000 |
| Total assets | $375,000 |
| Liabilities | |
| Accounts payable | $ 25,000 |
| Owner's Equity | |
| Todd Colby, capital | 350,000 |
| Total liabilities and owner's equity | $375,000 |

4. Net income (or net loss) appears on both the income statement and the statement of owner's equity. For Ocean Cruiser, net income for the year of $200,000 appears on the income statement and statement of owner's equity.

**Prob. 1–3B**

1.

| Bronco Consulting<br>Income Statement<br>For the Month Ended August 31, 20Y1 | | |
|---|---|---|
| Fees earned | | $ 125,000 |
| Expenses: | | |
| Salaries expense | $58,000 | |
| Rent expense | 27,000 | |
| Auto expense | 15,500 | |
| Supplies expense | 6,100 | |
| Miscellaneous expense | 7,500 | |
| Total expenses | | (114,100) |
| Net income | | $ 10,900 |

2.

| Bronco Consulting<br>Statement of Owner's Equity<br>For the Month Ended August 31, 20Y1 | |
|---|---|
| Jose Loder, capital, August 1, 20Y1 | $ 0 |
| Investment by owner | 75,000 |
| Net income for August | 10,900 |
| Withdrawals | (5,000) |
| Jose Loder, capital, August 31, 20Y1 | $80,900 |

3.

| Bronco Consulting<br>Balance Sheet<br>August 31, 20Y1 | |
|---|---|
| Assets | |
| Cash | $48,000 |
| Accounts receivable | 33,000 |
| Supplies | 2,900 |
| Total assets | $83,900 |
| Liabilities | |
| Accounts payable | $ 3,000 |
| Owner's Equity | |
| Jose Loder, capital | 80,900 |
| Total liabilities and owner's equity | $83,900 |

**Prob. 1–3B (Concluded)**

**4. Optional**

| Bronco Consulting<br>Statement of Cash Flows<br>For the Month Ended August 31, 20Y1 | | |
|---|---|---|
| Cash flows from (used for) operating activities: | | |
| Cash received from customers | $ 92,000 | |
| Cash paid for expenses and to creditors* | (114,000) | |
| Net cash flows used for operating activities | | $(22,000) |
| Cash flows from (used for) investing activities | | 0 |
| Cash flows from (used for) financing activities: | | |
| Cash received from owner's investment | $ 75,000 | |
| Cash paid for owner withdrawal | (5,000) | |
| Net cash flows from financing activities | | 70,000 |
| Net increase in cash | | $ 48,000 |
| Cash balance, August 1, 20Y1 | | 0 |
| Cash balance, August 31, 20Y1 | | $ 48,000 |

* $27,000 + $6,000 + $23,000 + $58,000; these amounts are taken from the Cash column presented in the problem.

**Prob. 1–4B**

**1.**

| | Assets | | = Liabilities + | Owner's Equity | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Cash | + Supplies | = Accts. Payable | + Maria Adams, Capital | − Maria Adams, Drawing | + Sales Comm. | − Rent Exp. | − Salaries Exp. | − Auto Exp. | − Supplies Exp. | − Misc. Exp. |
| a. | + 24,000 | | | + 24,000 | | | | | | | |
| b. | – 3,600 | | | | | | – 3,600 | | | | |
| Bal. | 20,400 | | | 24,000 | | | – 3,600 | | | | |
| c. | – 1,950 | | | | | | | | – 1,350 | | – 600 |
| Bal. | 18,450 | | | 24,000 | | | – 3,600 | | – 1,350 | | – 600 |
| d. | | + 1,200 | + 1,200 | | | | | | | | |
| Bal. | 18,450 | 1,200 | 1,200 | 24,000 | | | – 3,600 | | – 1,350 | | – 600 |
| e. | + 19,800 | | | | | + 19,800 | | | | | |
| Bal. | 38,250 | 1,200 | 1,200 | 24,000 | | 19,800 | – 3,600 | | – 1,350 | | – 600 |
| f. | – 750 | | – 750 | | | | | | | | |
| Bal. | 37,500 | 1,200 | 450 | 24,000 | | 19,800 | – 3,600 | | – 1,350 | | – 600 |
| g. | – 2,500 | | | | | | | – 2,500 | | | |
| Bal. | 35,000 | 1,200 | 450 | 24,000 | | 19,800 | – 3,600 | – 2,500 | – 1,350 | | – 600 |
| h. | – 3,500 | | | | – 3,500 | | | | | | |
| Bal. | 31,500 | 1,200 | 450 | 24,000 | – 3,500 | 19,800 | – 3,600 | – 2,500 | – 1,350 | | – 600 |
| i. | | – 900 | | | | | | | | – 900 | |
| Bal. | 31,500 | 300 | 450 | 24,000 | – 3,500 | 19,800 | – 3,600 | – 2,500 | – 1,350 | – 900 | – 600 |

**Prob. 1–4B (Concluded)**

**2.**

| Custom Realty<br>Income Statement<br>For the Month Ended April 30, 20Y8 | | |
|---|---|---|
| Sales commissions | | $19,800 |
| Expenses: | | |
| Rent expense | $3,600 | |
| Salaries expense | 2,500 | |
| Automobile expense | 1,350 | |
| Supplies expense | 900 | |
| Miscellaneous expense | 600 | |
| Total expenses | | (8,950) |
| Net income | | $10,850 |

| Custom Realty<br>Statement of Owner's Equity<br>For the Month Ended April 30, 20Y8 | |
|---|---|
| Maria Adams, capital, April 1, 20Y8 | $ 0 |
| Investment by owner | 24,000 |
| Net income for April | 10,850 |
| Withdrawals | (3,500) |
| Maria Adams, capital, April 30, 20Y8 | $31,350 |

| Custom Realty<br>Balance Sheet<br>April 30, 20Y8 | |
|---|---|
| **Assets** | |
| Cash | $31,500 |
| Supplies | 300 |
| Total assets | $31,800 |
| **Liabilities** | |
| Accounts payable | $ 450 |
| **Owner's Equity** | |
| Maria Adams, capital | 31,350 |
| Total liabilities and owner's equity | $31,800 |

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## Prob. 1–5B

**1.**

| | Assets | | | | = Liabilities + | Owner's Equity | |
|---|---|---|---|---|---|---|---|
| | Cash | + Accts. Rec. | + Supplies | + Land | = Accts. Payable | + Beverly Zahn, Capital | – Beverly Zahn, Drawing |
| Bal. | 39,000 | 80,000 | 11,000 | 50,000 | 31,500 | 148,500 | |
| a. | + 21,000 | | | | | + 21,000 | |
| Bal. | 60,000 | 80,000 | 11,000 | 50,000 | 31,500 | 169,500 | |
| b. | – 35,000 | | | + 35,000 | | | |
| Bal. | 25,000 | 80,000 | 11,000 | 85,000 | 31,500 | 169,500 | |
| c. | – 4,000 | | | | | | |
| Bal. | 21,000 | 80,000 | 11,000 | 85,000 | 31,500 | 169,500 | |
| d. | | + 72,000 | | | | | |
| Bal. | 21,000 | 152,000 | 11,000 | 85,000 | 31,500 | 169,500 | |
| e. | – 20,000 | | | | – 20,000 | | |
| Bal. | 1,000 | 152,000 | 11,000 | 85,000 | 11,500 | 169,500 | |
| f. | | | + 8,000 | | + 8,000 | | |
| Bal. | 1,000 | 152,000 | 19,000 | 85,000 | 19,500 | 169,500 | |
| g. | + 38,000 | | | | | | |
| Bal. | 39,000 | 152,000 | 19,000 | 85,000 | 19,500 | 169,500 | |
| h. | + 77,000 | – 77,000 | | | | | |
| Bal. | 116,000 | 75,000 | 19,000 | 85,000 | 19,500 | 169,500 | |
| i. | | | | | + 29,450 | | |
| Bal. | 116,000 | 75,000 | 19,000 | 85,000 | 48,950 | 169,500 | |
| j. | – 29,200 | | | | | | |
| Bal. | 86,800 | 75,000 | 19,000 | 85,000 | 48,950 | 169,500 | |
| k. | | | – 7,200 | | | | |
| Bal. | 86,800 | 75,000 | 11,800 | 85,000 | 48,950 | 169,500 | |
| l. | – 5,000 | | | | | | – 5,000 |
| Bal. | 81,800 | 75,000 | 11,800 | 85,000 | 48,950 | 169,500 | – 5,000 |

**Prob. 1–5B (Continued)**

| | Owner's Equity (Continued) | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | + Dry Cleaning Revenue | – Dry Cleaning Exp. | – Wages Exp. | – Supplies Exp. | – Rent Exp. | – Truck Exp. | – Utilities Exp. | – Misc. Exp. |
| Bal. | | | | | | | | |
| a. | | | | | | | | |
| Bal. | | | | | | | | |
| b. | | | | | | | | |
| Bal. | | | | | | | | |
| c. | | | | | – 4,000 | | | |
| Bal. | | | | | – 4,000 | | | |
| d. | + 72,000 | | | | | | | |
| Bal. | 72,000 | | | | – 4,000 | | | |
| e. | | | | | | | | |
| Bal. | 72,000 | | | | – 4,000 | | | |
| f. | | | | | | | | |
| Bal. | 72,000 | | | | – 4,000 | | | |
| g. | + 38,000 | | | | | | | |
| Bal. | 110,000 | | | | – 4,000 | | | |
| h. | | | | | | | | |
| Bal. | 110,000 | | | | – 4,000 | | | |
| i. | | – 29,450 | | | | | | |
| Bal. | 110,000 | – 29,450 | | | – 4,000 | | | |
| j. | | | – 24,000 | | | – 2,100 | – 1,800 | – 1,300 |
| Bal. | 110,000 | – 29,450 | – 24,000 | | – 4,000 | – 2,100 | – 1,800 | – 1,300 |
| k. | | | | – 7,200 | | | | |
| Bal. | 110,000 | – 29,450 | – 24,000 | – 7,200 | – 4,000 | – 2,100 | – 1,800 | – 1,300 |
| l. | | | | | | | | |
| Bal. | 110,000 | – 29,450 | – 24,000 | – 7,200 | – 4,000 | – 2,100 | – 1,800 | – 1,300 |

**Prob. 1–5B (Continued)**

2.

| Bev's Dry Cleaners<br>Income Statement<br>For the Month Ended November 30, 20Y3 | | |
|---|---|---|
| Dry cleaning revenue | | $110,000 |
| Expenses: | | |
| Dry cleaning expense | $29,450 | |
| Wages expense | 24,000 | |
| Supplies expense | 7,200 | |
| Rent expense | 4,000 | |
| Truck expense | 2,100 | |
| Utilities expense | 1,800 | |
| Miscellaneous expense | 1,300 | |
| Total expenses | | (69,850) |
| Net income | | $ 40,150 |

| Bev's Dry Cleaners<br>Statement of Owner's Equity<br>For the Month Ended November 30, 20Y3 | |
|---|---|
| Beverly Zahn, capital, November 1, 20Y3 | $148,500 |
| Additional investment by owner | 21,000 |
| Net income for November | 40,150 |
| Withdrawals | (5,000) |
| Beverly Zahn, capital, November 30, 20Y3 | $204,650 |

| Bev's Dry Cleaners<br>Balance Sheet<br>November 30, 20Y3 | |
|---|---|
| **Assets** | |
| Cash | $ 81,800 |
| Accounts receivable | 75,000 |
| Supplies | 11,800 |
| Land | 85,000 |
| Total assets | $253,600 |
| **Liabilities** | |
| Accounts payable | $ 48,950 |
| **Owner's Equity** | |
| Bevery Zahn, capital | 204,650 |
| Total liabilities and owner's equity | $253,600 |

**Prob. 1–5B (Concluded)**

**3. Optional**

| Bev's Dry Cleaners<br>Statement of Cash Flows<br>For the Month Ended November 30, 20Y3 | | |
|---|---|---|
| Cash flows from (used for) operating activities: | | |
| Cash received from customers* | $115,000 | |
| Cash paid for expenses and to creditors** | (53,200) | |
| Net cash flows from operating activities | | $ 61,800 |
| Cash flows from (used for) investing activities: | | |
| Cash paid for acquisition of land | | (35,000) |
| Cash flows from (used for) financing activities: | | |
| Cash received from owner's investment | $ 21,000 | |
| Cash paid for owner withdrawals | (5,000) | |
| Net cash flows from financing activities | | 16,000 |
| Net increase in cash | | $ 42,800 |
| Cash balance, November 1, 20Y3 | | 39,000 |
| Cash balance, November 30, 20Y3 | | $ 81,800 |

* $38,000 + $77,000; these amounts are taken from the Cash column of the spreadsheet in Part 1.

** $4,000 + $20,000 + $29,200; these amounts are taken from the Cash column of the spreadsheet in Part 1.

**Prob. 1–6B**

**a. Wages expense, $203,200 ($288,000 – $48,000 – $17,600 – $14,400 – $4,800)**

**b. Net income, $112,000 ($400,000 – $288,000)**

**c. Investment by owner, $160,000; from statement of cash flows.**

**d. Net income for May, $112,000; from (b)**

**e. Withdrawals, $64,000; from statement of cash flows**

**f. Chris Ying, capital, May 31, 20Y6, $208,000 ($160,000 + $112,000 – $64,000)**

**g. Land, $120,000; from statement of cash flows.**

**h. Total assets, $256,000 ($123,200 + $12,800 + $120,000)**

**i. Chris Ying, capital, $208,000; same as (f)**

**j. Total liabilities and owner's equity, $256,000 ($48,000 + $208,000)**

**k. Cash received from customers, $400,000; this is the same as fees earned since there are no accounts receivable.**

**l. Net cash flows from operating activities, $147,200 ($400,000 – $252,800)**

**m. Net cash flows from financing activities, $96,000 ($160,000 – $64,000)**

**n. Net increase in cash, $123,200 ($147,200 – $120,000 + $96,000)**

**o. Cash as of May 31, 20Y6, $123,200; same as (n) since Atlas Realty was organized on May 1, 20Y6; also the cash balance on the balance sheet.**

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## CONTINUING PROBLEM

1.

| | Assets | | | = Liabilities + | Owner's Equity | | |
|---|---|---|---|---|---|---|---|
| | Cash + | Accts. Rec. + | Supplies = | Accts. Payable + | Peyton Smith, Capital – | Peyton Smith, Drawing + | Fees Earned |
| June 1 | + 4,000 | | | | + 4,000 | | |
| June 2 | + 3,500 | | | | | | + 3,500 |
| Bal. | 7,500 | | | | 4,000 | | 3,500 |
| June 2 | – 800 | | | | | | |
| Bal. | 6,700 | | | | 4,000 | | 3,500 |
| June 4 | | | + 350 | + 350 | | | |
| Bal. | 6,700 | | 350 | 350 | 4,000 | | 3,500 |
| June 6 | – 500 | | | | | | |
| Bal. | 6,200 | | 350 | 350 | 4,000 | | 3,500 |
| June 8 | – 675 | | | | | | |
| Bal. | 5,525 | | 350 | 350 | 4,000 | | 3,500 |
| June 12 | – 350 | | | | | | |
| Bal. | 5,175 | | 350 | 350 | 4,000 | | 3,500 |
| June 13 | – 100 | | | – 100 | | | |
| Bal. | 5,075 | | 350 | 250 | 4,000 | | 3,500 |
| June 16 | + 300 | | | | | | + 300 |
| Bal. | 5,375 | | 350 | 250 | 4,000 | | 3,800 |
| June 22 | | + 1,000 | | | | | + 1,000 |
| Bal. | 5,375 | 1,000 | 350 | 250 | 4,000 | | 4,800 |
| June 25 | + 500 | | | | | | + 500 |
| Bal. | 5,875 | 1,000 | 350 | 250 | 4,000 | | 5,300 |
| June 29 | – 240 | | | | | | |
| Bal. | 5,635 | 1,000 | 350 | 250 | 4,000 | | 5,300 |
| June 30 | + 900 | | | | | | + 900 |
| Bal. | 6,535 | 1,000 | 350 | 250 | 4,000 | | 6,200 |
| June 30 | – 400 | | | | | | |
| Bal. | 6,135 | 1,000 | 350 | 250 | 4,000 | | 6,200 |
| June 30 | – 300 | | | | | | |
| Bal. | 5,835 | 1,000 | 350 | 250 | 4,000 | | 6,200 |
| June 30 | | | – 180 | | | | |
| Bal. | 5,835 | 1,000 | 170 | 250 | 4,000 | | 6,200 |
| June 30 | – 415 | | | | | | |
| Bal. | 5,420 | 1,000 | 170 | 250 | 4,000 | | 6,200 |
| June 30 | – 1,000 | | | | | | |
| Bal. | 4,420 | 1,000 | 170 | 250 | 4,000 | | 6,200 |
| June 30 | – 500 | | | | | – 500 | |
| Bal. | 3,920 | 1,000 | 170 | 250 | 4,000 | – 500 | 6,200 |

## Continuing Problem (Continued)

| | | Owner's Equity (Continued) | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | – Music Exp. | – Office Rent Exp. | – Equip. Rent Exp. | – Advertising Exp. | – Wages Exp. | – Utilities Exp. | – Supplies Exp. | – Misc. Exp. |
| June | 1 | | | | | | | | |
| June | 2 | | | | | | | | |
| Bal. | | | | | | | | | |
| June | 2 | | – 800 | | | | | | |
| Bal. | | | – 800 | | | | | | |
| June | 4 | | | | | | | | |
| Bal. | | | – 800 | | | | | | |
| June | 6 | | | | – 500 | | | | |
| Bal. | | | – 800 | | – 500 | | | | |
| June | 8 | | | – 675 | | | | | |
| Bal. | | | – 800 | – 675 | – 500 | | | | |
| June | 12 | – 350 | | | | | | | |
| Bal. | | – 350 | – 800 | – 675 | – 500 | | | | |
| June | 13 | | | | | | | | |
| Bal. | | – 350 | – 800 | – 675 | – 500 | | | | |
| June | 16 | | | | | | | | |
| Bal. | | – 350 | – 800 | – 675 | – 500 | | | | |
| June | 22 | | | | | | | | |
| Bal. | | – 350 | – 800 | – 675 | – 500 | | | | |
| June | 25 | | | | | | | | |
| Bal. | | – 350 | – 800 | – 675 | – 500 | | | | |
| June | 29 | – 240 | | | | | | | |
| Bal. | | – 590 | – 800 | – 675 | – 500 | | | | |
| June | 30 | | | | | | | | |
| Bal. | | – 590 | – 800 | – 675 | – 500 | | | | |
| June | 30 | | | | | – 400 | | | |
| Bal. | | – 590 | – 800 | – 675 | – 500 | – 400 | | | |
| June | 30 | | | | | | – 300 | | |
| Bal. | | – 590 | – 800 | – 675 | – 500 | – 400 | – 300 | | |
| June | 30 | | | | | | | – 180 | |
| Bal. | | – 590 | – 800 | – 675 | – 500 | – 400 | – 300 | – 180 | |
| June | 30 | | | | | | | | – 415 |
| Bal. | | – 590 | – 800 | – 675 | – 500 | – 400 | – 300 | – 180 | – 415 |
| June | 30 | – 1,000 | | | | | | | |
| Bal. | | – 1,590 | – 800 | – 675 | – 500 | – 400 | – 300 | – 180 | – 415 |
| June | 30 | | | | | | | | |
| Bal. | | – 1,590 | – 800 | – 675 | – 500 | – 400 | – 300 | – 180 | – 415 |

**Continuing Problem (Concluded)**

**2.**

| PS Music<br>Income Statement<br>For the Month Ended June 30, 20Y5 | | |
|---|---|---|
| Fees earned: | | $ 6,200 |
| Expenses: | | |
| Music expense | $1,590 | |
| Office rent expense | 800 | |
| Equipment rent expense | 675 | |
| Advertising expense | 500 | |
| Wages expense | 400 | |
| Utilities expense | 300 | |
| Supplies expense | 180 | |
| Miscellaneous expense | 415 | |
| Total expenses | | (4,860) |
| Net income | | $ 1,340 |

**3.**

| PS Music<br>Statement of Owner's Equity<br>For the Month Ended June 30, 20Y5 | |
|---|---|
| Peyton Smith, capital, June 1, 20Y5 | $ 0 |
| Investment by owner | 4,000 |
| Net income for June | 1,340 |
| Withdrawals | (500) |
| Peyton Smith, capital, June 30, 20Y5 | $4,840 |

**4.**

| PS Music<br>Balance Sheet<br>June 30, 20Y5 | |
|---|---|
| Assets | |
| Cash | $3,920 |
| Accounts receivable | 1,000 |
| Supplies | 170 |
| Total assets | $5,090 |
| Liabilities | |
| Accounts payable | $ 250 |
| Owner's Equity | |
| Peyton Smith, capital | 4,840 |
| Total liabilities and owner's equity | $5,090 |

## MAKE A DECISION

**MAD 1–1**

**a. Ratio of Liabilities to Stockholders' Equity = $\dfrac{\text{Total Liabilities}}{\text{Total Stockholders' Equity}}$**

**Amazon:** $\dfrac{\$325{,}979}{\$201{,}875} = 1.61$

**Best Buy:** $\dfrac{\$11{,}914}{\$3{,}053} = 3.90$

**b. Amazon's ratio is 1.61, which means the total liabilities are over one and a half times as great as the stockholders' equity. For Best Buy, the ratio is 3.90, which is almost 2.5 times that of Amazon. Thus, the margin of protection is higher for Amazon's creditors than it is for Best Buy's creditors.**

**MAD 1–2**

**a. Ratio of Liabilities to Stockholders' Equity = $\dfrac{\text{Total Liabilities}}{\text{Total Stockholders' Equity}}$**

**Year 1:** $\dfrac{\$40{,}984}{\$12{,}827} = 3.20$

**Year 2:** $\dfrac{\$42{,}103}{\$11{,}232} = 3.75$

**Year 3:** $\dfrac{\$41{,}924}{\$13{,}432} = 3.12$

**b. The ratio of liabilities to stockholders' equity for Target varies from 3.20 in Year 1 to 3.75 in Year 2 to 3.12 in Year 3. Thus, the margin of protection for creditors has remained relatively consistent throughout the three years.**

**MAD 1–3**

a. **Ratio of Liabilities to Stockholders' Equity** $= \dfrac{\textbf{Total Liabilities}}{\textbf{Total Stockholders' Equity}}$

**Year 1:** $\dfrac{\$152{,}959}{\$91{,}891} = 1.66$

**Year 2:** $\dfrac{\$159{,}443}{\$83{,}754} = 1.90$

**Year 3:** $\dfrac{\$162{,}050}{\$90{,}349} = 1.79$

b. **The ratio of liabilities to stockholders' equity for Walmart increased from 1.66 in Year 1 to 1.90 in Year 2 and decreased to 1.79 in Year 3. Thus, the margin of protection for creditors has remained relatively consistent throughout the three years.**

**MAD 1–4**

**The ratios of liabilities to stockholders' equity are summarized below for Target (MAD 1–2) and Walmart (MAD 1–3).**

| | Year 3 | Year 2 | Year 1 |
|---|---|---|---|
| Target | 3.12 | 3.75 | 3.20 |
| Walmart | 1.79 | 1.90 | 1.66 |

**Target's ratio of liabilities to stockholders' equity is more than that of Walmart for all three years. Thus, the risk to Target's creditors is more than that of Walmart's creditors. Target appears to be slightly more aggressive than Walmart in its use of debt.**

**MAD 1–5**

a. **Ratio of Liabilities to Stockholders' Equity** $= \dfrac{\textbf{Total Liabilities}}{\textbf{Total Stockholders' Equity}}$

**Wendy's:** $\dfrac{\$4{,}873}{\$310} = 15.72$

**Chipotle:** $\dfrac{\$4{,}982}{\$3{,}062} = 1.63$

b. **The ratio of liabilities to stockholders' equity is 15.72 for Wendy's. This ratio is relatively high and suggests that creditors have risk with their investments. Specifically, the small level of stockholders' equity provides a low margin of protection for creditors.**

c. **Chipotle's ratio of liabilities to stockholders' equity of 1.63 suggests that Chipotle is not using as much debt to finance its operations as Wendy's. This, in turn, suggests that Chipotle's creditors have more protection than Wendy's creditors.**

## TAKE IT FURTHER

**TIF 1–1**

1. **The car repair is a personal expense and is Marco's personal responsibility. By using partnership funds to pay for the repair, Marco is behaving unethically since he is violating the business entity assumption. The business entity assumption treats the business as a separate entity from its owners. By taking money from the partnership for a personal expense, Marco is effectively stealing from his partners.**
2. **The partnership's net income will be reduced by the $2,000 Marco has taken. This will reduce the amount of net income available to Marco's partners.**
3. **Marco could ask his partners for a loan from the partnership. The loan could be repaid out of his salary or from his share of the partnership income.**

**TIF 1–2**

1. **Acceptable professional conduct requires that Colleen Fernandez supply First Federal Bank with all the relevant financial statements necessary for the bank to make an informed decision. Therefore, Colleen should provide the complete set of financial statements. These can be supplemented with a discussion of the net loss in the past year or other data explaining why granting the loan is a good investment for the bank.**

2. a. **Owners are generally willing to provide bankers with information about the operating and financial condition of the business, such as the following:**
   - **Operating Information:**
     - **Description of business operations**
     - **Results of past operations**
     - **Preliminary results of current operations**
     - **Plans for future operations**
   - **Financial Condition:**
     - **List of assets and liabilities (balance sheet)**
     - **Estimated current values of assets**
     - **Owner's personal investment in the business**
     - **Owner's commitment to invest additional funds in the business**

   **Owners are normally reluctant to provide the following types of information to bankers:**
   - ***Proprietary Operating Information.*** **Such information, which could hurt the business if it becomes known by competitors, might include special processes used by the business or future plans to expand operations into areas that are not currently served by a competitor.**
   - ***Personal Financial Information.*** **Owners may have little choice here since banks often require owners of small businesses to pledge their personal assets as security for a business loan. Personal financial information requested by bankers often includes the owner's net worth, salary, and other income. In addition, bankers usually request information about factors that might affect the personal financial condition of the owner. For example, a pending divorce by the owner might significantly affect the owner's personal wealth.**

   b. **Bankers typically want as much information as possible about the ability of the business and the owner to repay the loan with interest. Examples of such information are described above.**

   c. **Both bankers and business owners share the common interest of the business doing well and being successful. If the business is successful, the bankers will receive their loan payments on time with interest, and the owners will increase their personal wealth.**

**TIF 1–3**

**A sample solution based on Amazon's Form 10-K for the fiscal year ended December 31, 2023, follows:**

1. **Amazon.com, Inc.**
2. **Seattle, Washington**
3. **Andrew R. Jassy**
4. **Merchandising**
5. **We serve consumers through our online and physical stores and focus on selection, price, and convenience. We design our stores to enable hundreds of millions of unique products to be sold by us and by third parties across dozens of product categories. Customers access our offerings through our websites, mobile apps, Alexa, devices, streaming, and physically visiting our stores. We also manufacture and sell electronic devices, including Kindle, Fire tablet, Fire TV, Echo, Ring, Blink, and eero, and we develop and produce media content. We seek to offer our customers low prices, fast and free delivery, easy-to-use functionality, and timely customer service. In addition, we offer subscription services such as Amazon Prime, a membership program that includes fast, free shipping on tens of millions of items, access to award-winning movies and series, and other benefits.**
6. **Statement of cash flows, statement of operations, statement of comprehensive income (loss) (discussed in Online Appendix 3), balance sheet, and statement of stockholders' equity.**

**TIF 1–4**

**Example Memo**

| | |
|---|---|
| **To:** | **Teacher** |
| **From:** | **Student** |
| **Date:** | **Current Date** |
| **Subject:** | **Causes of Accounting Fraud** |

**Business and accounting fraud typically result from either a failure of individual character or a culture of greed within an organization. Managers and accountants often face pressure to meet or exceed a company's financial goals. At times, supervisors can place pressure on individuals to violate accounting standards to improve a company's reported financial results. Individuals who give in to these pressures exhibit a failure of individual character. In other situations, a company may indirectly encourage employees to violate accounting rules as part of their job. This occurs in organizations that do not value ethical decision-making or fair financial reporting and exhibit a culture of ethical indifference.**

**TIF 1–5**

**The difference in the two bank balances, $55,000 ($80,000 – $25,000), may not be pure profit from an accounting perspective. To determine the accounting profit for the six-month period, the revenues for the period would need to be matched with the related expenses. The revenues minus the expenses would indicate whether the business generated net income (profit) or a net loss for the period. Using only the difference between the two bank account balances ignores such factors as amounts due from customers (receivables), liabilities (accounts payable) that need to be paid for wages or other operating expenses, additional investments that Dr. Cousins may have made in the business during the period, or withdrawals made during the period that Dr. Cousins might have taken for personal reasons unrelated to the business.**

**Some businesses that have few, if any, receivables or payables may use a "cash" basis of accounting. The cash basis of accounting ignores receivables and payables since they are assumed to be insignificant in amount. However, even with the cash basis of accounting, additional investments during the period and any withdrawals made during the period have to be considered in determining the net income (profit) or net loss for the period.**

**TIF 1–6**

**Excel**

| Row Labels | Sum of Amount |
|---|---|
| Asset | $31,417,915.20 |
| Liabilities + Equity | $31,417,915.20 |
| **Grand Total** | **$62,835,830.40** |

**Tableau**

Account Balance

| Category (group) | |
|---|---|
| Asset | $31,417,915.20 |
| Liabilities + Equity | $31,417,915.20 |

Sum of Amount broken down by Category (group).

# Instructor Manual

Warren, Accounting, 30e, 2027, 9798214053080; Chapter 1: Introduction to Accounting and Business

## TABLE OF CONTENTS

## Purpose and Perspective of the Chapter

The purpose of this chapter is to introduce students to business and accounting. For many students, Chapter 1 of *Accounting* is their first taste of the business or accounting disciplines. The teaching challenge is to get students to understand and accept the importance of learning business and accounting concepts. This will make the course more than just another requirement that students must complete to graduate. Because this chapter will set the tone for the entire course and the students' business careers, it is best to avoid the temptation of rushing through the material.

Chapter 1 begins with a discussion of the nature of business and accounting and the different types of businesses (service, retail, and manufacturing). Next, the chapter describes the role of accounting in business. The chapter then moves on to business ethics and discusses how individual character, firm culture, and laws and enforcement affect ethics as well as examples of accounting/business fraud. Opportunities in accounting professions/careers are discussed. Following this introductory information, the text explains generally accepted accounting principles (GAAP), the characteristics of financial information, and the assumptions that form the basis of GAAP. The forms of business entities (proprietorships, partnerships, corporations, and limited liability companies) are described. The four principles of financial accounting (measurement, historical cost, revenue recognition, and expense recognition) are defined. The accounting equation is introduced, and then the discussion of how business transactions affect accounts in the accounting equation begins. When transactions are analyzed, changes in assets, liabilities, and owner's equity are stated as "increases" or "decreases"; the terms *debit* and *credit* are not introduced until Chapter 2. The components of the accounting equation are discussed using several transactions for a business called NetSolutions. Next are examples of how to prepare the four primary financial statements using the accounting equation information and explanations of how the four financial statements are interrelated. The chapter ends with an explanation of the ratio of liabilities to owner's (stockholders') equity and how it is particularly important to creditors.

## Learning Objectives

The following objectives are addressed in this chapter:

**Obj. 1** Describe the nature of business and the role of accounting and ethics in business.

**Obj. 2** Describe generally accepted accounting principles, including the underlying assumptions and principles.

**Obj. 3** Define the accounting equation and each of its elements.

**Obj. 4** Illustrate how business transactions can be recorded in terms of the resulting change in the elements of the accounting equation.

**Obj. 5** Describe the financial statements of a proprietorship and how they interrelate.

**Obj. 6** Use the ratio of liabilities to owner's (stockholders') equity in evaluating a company's financial condition.

## Complete List of Chapter Activities and Assessments

The following table organizes activities and assessments in the PowerPoint by objective, so that you can see how all this content relates to objectives and make decisions about which content you would like to emphasize in your class based on your objectives. For additional activities, refer to the Teaching Online Guide and the Educator Guide

| Learning Objective | Activity/Assessment | Source (i.e., PPT slide, Workbook) |
|---|---|---|
| | | |
| Obj. 1 | Knowledge Check Activity 1 | PPT Slides 5-6 |
| Obj. 2 | Discussion Activity 1 | PPT Slides 23-24 |
| Obj. 3 | Discussion Activity 2 | PPT Slides 26-27 |
| Obj. 4 | Knowledge Check Activity 2 | PPT Slides 43-44 |
| Obj. 5 | Knowledge Check Activity 3 | PPT Slides 55-56 |

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## Key Terms

**Account payable:** The liability created by a purchase on account.

**Account receivable:** An asset, which is a claim against the customer created by selling merchandise or services on credit.

**Accounting:** An information system that provides reports to stakeholders about the economic activities and condition of a business.

**Accounting assumptions:** Assumptions that provide the framework upon which accounting standards are constructed.

**Accounting equation:** The equation that shows the relationship among assets, liabilities, and equity; expressed as Assets = Liabilities + Owner's Equity.

**Accounting principles:** Principles that provide the framework upon which accounting standards are constructed.

**Accounting standards:** The rules that determine the accounting for individual business transactions.

**Accounting Standards Codification:** An electronic database maintained by the Financial Accounting Standards Board (FASB) that contains all of the accounting standards that make up the generally accepted accounting principles (GAAP).

**Accounting Standards Updates:** Published changes to accounting standards that are the source of updates to the Accounting Standards Codification.

**Arm's-length transactions:** Transactions between two independent parties.

**Assets:** The resources owned by a business.

**Balance sheet:** A list of the assets, liabilities, and owner's equity as of a specific date, usually at the close of the last day of a month or a year.

**Business:** An organization in which basic resources (inputs), such as materials and labor, are assembled and processed to provide goods or services (outputs) to customers.

**Business entity assumption:** A concept of accounting that limits the economic data in the accounting system to data related directly to the activities of the business.

**Business transaction:** An economic event or condition that directly changes an entity's financial condition or directly affects its results of operations.

**Certified Public Accountants (CPAs):** Public accountants who have met a state's education, experience, and examination requirements.

**Comparability:** A secondary characteristic of financial information; comparability includes consistent reporting, that allows users to identify similarities and differences among reported items.

**Corporation:** A business organized under state or federal statutes as a separate legal entity.

**Cost principle:** A concept of accounting that states that an asset should be recorded and maintained in the accounting records at its initial transaction price.

**Data analytics:** The science of analyzing raw data to discover patterns, identify anomalies, or gain other useful insights.

**Earnings:** The amount by which revenues exceed expenses.

**Equity:** The rights of the owners of a business.

**Ethics:** Moral principles that guide the conduct of individuals.

**Expense recognition principle:** A principle, sometimes called the matching principle, that requires expenses to be recorded in the same period as the related revenue; a concept of accounting in which expenses are matched with the revenue generated during a period by those expenses.

**Expenses:** Amounts used to generate revenue; assets used up or services consumed in the process of generating revenues.

**Faithful representation:** A characteristic of financial reports that pertains to information accurately reflecting an entity’s economic activity or condition.

**Fees earned:** Revenue from providing services.

**Financial accounting:** The branch of accounting that is concerned with recording transactions using generally accepted accounting principles (GAAP) for a business or other economic unit and with a periodic preparation of various statements from such records.

**Financial Accounting Standards Board (FASB):** The authoritative body that has the primary responsibility for developing accounting principles.

**Financial statements:** Financial reports that summarize the effects of events on a business.

**Financing activities:** Activities by which a company obtains funds to start and operate the company.

**Fiscal year:** The annual accounting period adopted by a business.

**Generally accepted accounting principles (GAAP):** Generally accepted guidelines for the preparation of financial statements.

**General-purpose financial statements:** A type of financial accounting report that is distributed to external users. The term “general purpose” refers to the wide range of decision-making needs that the reports are designed to serve.

**Going concern assumption:** An assumption that requires that financial reports be prepared assuming that the entity will continue operating in the future.

**Historical cost principle:** A concept of accounting that states that an asset should be recorded and maintained in the accounting records at its initial transaction price.

**Income statement:** A summary of the revenue and expenses for a specific period of time, such as a month or a year.

**Interest revenue:** Earnings received for interest.

**International Accounting Standards Board (IASB):** An organization that issues International Financial Reporting Standards for many countries outside the United States.

**Investing activities:** Activities by which a company acquires long-term assets for use in the operating activities of the company.

**Liabilities:** The rights of creditors that represent debts of the business.

**Limited liability company (LLC):** A business form consisting of one or more persons or entities filing an operating agreement with a state to conduct business with limited liability to the owners, yet treated as a partnership for tax purposes.

**Managerial (or management) accounting:** The branch of accounting that uses both historical and estimated data in providing internal users (management) with information relevant to decision making.

**Manufacturing business:** A type of business that changes basic inputs into products that are sold to individual customers.

**Measurement principle:** A principle that requires that amounts be objective and verifiable.

**Monetary unit assumption:** An accounting assumption that requires that financial reports be expressed in a single monetary unit, or currency.

**Natural business year:** A fiscal year that ends when business activities have reached the lowest point in an annual operating cycle.

**Net income (or net profit):** The amount by which revenues exceed expenses.

**Net loss:** The amount by which expenses exceed revenues.

**Operating activities:** Activities by which a company generates revenues from customers.

**Owner's equity:** The equity for a proprietorship, partnership, or limited liability company.

**Partnership:** An unincorporated business form consisting of two or more persons conducting business as co-owners for profit.

**Prepaid expenses:** Assets created by making advanced payments for expense items, such as insurance premiums or supplies, that will be used in the business in the future.

**Private accounting:** The field of accounting whereby accountants are employed by a business firm or a not-for-profit organization.

**Profit:** The difference between the amounts received from customers for goods or services provided and the amounts paid for the inputs used to provide the goods or services.

**Proprietorship:** A business owned by one individual.

**Public accounting:** The field of accounting where accountants and their staff provide services on a fee basis.

**Public Company Accounting Oversight Board (PCAOB):** A new oversight body for the accounting profession that was established by the Sarbanes-Oxley Act.

**Ratio of liabilities to owner's (stockholders') equity:** A comprehensive leverage ratio that measures the relationship of the claims of creditors to owner's (stockholders') equity; a solvency ratio that measures how much of the company is financed by debt and equity, computed as total liabilities divided by total owner's (stockholders') equity.

**Relevant:** A characteristic of financial reports that pertains to information having the potential to impact decision making.

**Rent revenue:** Earnings from property that is leased to others for use.

**Report form:** A form of balance sheet with the "Liabilities" and "Owner's Equity" sections presented below the "Assets" section.

**Retail business:** A type of business that purchases products from other businesses and sells them to customers.

**Revenue:** Amount earned (received) from providing services or selling goods to customers.

**Revenue recognition principle:** A concept of accounting that states that revenues are recorded when earned, which is when the services have been performed or products have been delivered to customers.

**Sales:** How revenue from the sale of merchandise is recorded; the total amount charged customers for merchandise sold, including cash sales and sales on account.

**Sarbanes-Oxley Act (SOX):** An act passed by Congress to restore public confidence and trust in the financial statements of companies.

**Securities and Exchange Commission (SEC):** An agency of the U.S. government that has authority over the accounting and financial disclosures for companies whose shares of ownership (stock) are traded and sold to the public.

**Service business:** A business providing services rather than products to customers.

**Statement of cash flows:** A summary of the cash receipts and cash payments for a specific period of time, such as a month or a year.

**Statement of owner's equity:** A summary of the changes in the owner's equity in a company that have occurred during a specific period of time, such as a month or a year.

**Stockholders' equity:** The ownership rights of stockholders in a corporation; the stockholders' rights to the assets in a corporation.

**Timeliness:** A secondary characteristic of financial information that requires distribution of financial reports in time to influence a user's decision.

**Time period assumption:** An accounting assumption that allows a company to report its economic activities on a regular basis for a specific period of time.

**Understandability:** A secondary characteristic of financial information that requires clear and concise financial reports that facilitate user interpretation and analysis.

**Verifiability:** A secondary characteristic of financial information that allows users to agree on the meaning of reported items.

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## What's New in This Chapter

- See the Transition Guide for a list of improvements in this chapter from the previous edition.

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## Chapter Outline

The following outline organizes activities (including any existing discussion questions in PowerPoints or other supplements) and assessments by chapter (and therefore by topic), so that you can see how all the content relates to the topics covered in the text.

I. Nature of Business and Accounting (1-1, PPT Slides 3–13, BUSPROG: Analytic, AICPA: FN-Research)

   a. A business is an organization in which basic resources (inputs), such as materials and labor, are assembled and processed to provide goods or services (outputs) to customers.
   b. Profit is the difference between the amounts received from customers for goods or services and the amounts paid for the inputs used to provide the goods or services.
   c. Three types of businesses operating for profit include service, retail, and manufacturing businesses.
      i. Service businesses provide services rather than products to customers.
      ii. Retail businesses sell products they purchase from other businesses to customers.
      iii. Manufacturing businesses change basic inputs into products that are sold to customers.
   d. **Knowledge Check Activity 1:** *Which of the following businesses would be considered a service business?* (PPT Slides 5-6)
      - The answer is Southwest Airlines.
      - Southwest Airlines would be considered a service business. Walmart and Starbucks would be considered retail businesses, and Ford Motor Company would be a manufacturer.
   e. Exhibit 1 (PPT Slide 7) shows the three types of business activities: financing, operating, and investing.
   f. The role of accounting in business is to provide information for managers to use in operating the business.
      i. Accounting provides information to other users in assessing the economic performance and condition of the business.
      ii. Accounting can be defined as an information system that provides reports to users about the economic activities and condition of a business.
      iii. Exhibit 2 (PPT Slide 9) illustrates the role of accounting as an information system.

g. Internal users require information from managerial accounting, while external users require information from financial accounting.
h. Accountants must behave in an ethical manner so that the information they provide users will be trustworthy and, thus, useful for decision making.
    i. Ethics are moral principles that guide the conduct of individuals. Unfortunately, business managers and accountants sometimes behave in an unethical manner.
    ii. Failure of Individual Character: Ethical managers and accountants are honest and fair. However, managers and accountants often face pressures from supervisors to meet company and investor expectations.
    iii. Culture of Greed and Ethical Indifference: By their behavior and attitude, senior managers set the company culture.
i. The failure of individual character and a culture of corporate greed and ethical indifference led to the accounting and business frauds as shown in Exhibit 3 (PPT Slide 11).
    i. The Sarbanes-Oxley Act (SOX) was enacted in 2002 as a countermeasure to the fraud that was being committed.
    ii. One of the many regulations that SOX established was a new oversight body for the accounting profession called the Public Company Accounting Oversight Board (PCAOB).
    iii. In addition, SOX established standards for independence, corporate responsibility, and disclosure.
j. Opportunities for accountants are increasing as regulations increase, and people are beginning to realize the importance and value of accounting information.
    i. Exhibit 4 (PPT Slides 12-13) provides a list of accounting career paths and salaries.

II. Generally Accepted Accounting Principles (GAAP) (1-2, PPT Slides 14-24, BUSPROG: Analytic, AICPA: FN-Measurement)

a. Financial information in the United States is based on generally accepted accounting principles (GAAP). GAAP is a collection of accounting standards, principles, and assumptions that define how financial information will be reported.
    i. Accounting standards are the rules that determine the accounting for individual business transactions.
    ii. Accounting principles and assumptions provide the framework upon which accounting standards are constructed.

b. In the United States, these principles are the responsibility of the Financial Accounting Standards Board (FASB).
    i. The FASB maintains an electronic database, called the Accounting Standards Codification, that contains all the accounting standards that make up GAAP.
    ii. Changes in the FASB Codification are made using Accounting Standards Updates.

c. The Securities and Exchange Commission (SEC), an agency of the U.S. government, has authority over the accounting and financial disclosures for companies whose shares of ownership (stock) are traded and sold to the public.
    i. Outside the United States, most countries use accounting standards and principles adopted by the International Accounting Standards Board (IASB).

d. Financial reports must possess two important characteristics: relevance and faithful representation.
    i. Relevant information has the potential to impact decision making.
    ii. Faithful representation means that the information accurately reflects an entity's economic activity or condition.

e. Relevant and faithful representation are enhanced by the following:
    i. Comparability, which includes consistent reporting, allows users to identify similarities and differences among reported items.
    ii. Verifiability allows users to agree on the meaning of reported items.
    iii. Timeliness requires distribution of financial reports in time to influence a user's decision.
    iv. Understandability requires clear and concise financial reports that facilitate user interpretation and analysis.

f. Financial accounting and generally accepted accounting principles are based upon the following assumptions:
    i. Monetary unit: Requires that financial reports be expressed in a single money unit, or currency.
    ii. Time period: Allows a business to report its economic activities on a regular basis for a specific period of time.
    iii. Business entity: Limits the economic data in financial reports to that directly related to the activities of the business.
    iv. Going concern: Requires that financial reports be prepared assuming that the entity will continue operating into the future.

g. The annual accounting period adopted by a company is called its fiscal year. A natural business year is a fiscal year that ends when business activities have reached the lowest point in an annual operating cycle.
h. This chapter also introduces the four forms of business entities: proprietorship, partnership, corporation, and limited liability company (LLC).
    i. Exhibit 5 (PPT Slides 19-20) lists the types of business entities and the characteristics and advantages of each.
i. Financial accounting relies on principles regarding measurement, historical cost, revenue recognition, and expense recognition.
j. In addition to the preceding characteristics and assumptions, the following four principles are an integral part of financial accounting:
    i. Measurement: Determines the amount that will be recorded and reported.
    ii. Historical cost (cost principle): Recording an item at its initial transaction price.
    iii. Revenue recognition: Determines when revenue is recorded in the accounting records.
    iv. Expense recognition (matching principle): Requires expenses to be recorded in the same period as the related revenue.
k. Transactions between two independent parties, called arm's-length transactions, provide amounts that are objective and verifiable.
l. **Discussion Activity 1:** *In the following scenarios, which form of business entity do you think would be the best choice? Explain your reasons.* (PPT Slides 23-24)
    *1. A group of three dentists opening a full-service dental office*
    *2. A graphic design artist specializing in digital marketing*
    *3. Five entrepreneurs opening a chain of hair salons*
    - There are advantages and disadvantages for each type of business formation. Small businesses often select a sole proprietorship, although it does expose them to liability issues, including potential lawsuits.
    - For each of these scenarios, the answers may vary. Legal and medical professionals often select a form of partnership or LLC. An individual, such as the graphic artist, may choose to be a sole proprietor. When there are more people involved and the potential exists for shares to be issued, a corporation would be the best choice (likely for the hair salons).
    - What did you choose for each, and why? If you opened a business, which would you choose?

III. The Accounting Equation (1-3, PPT Slide 25, BUSPROG: Analytic, AICPA: FN-Measurement)

a. This objective defines assets, liabilities, and owner's (stockholders') equity and uses the accounting equation (Assets = Liabilities + Owner's Equity) to explain their relationship.
   i. The resources owned by a business are its assets.
   ii. The rights of creditors are the debts of the business and are called liabilities.
   iii. The rights of owners are called equity.
   iv. For a proprietorship, partnership, or limited liability company, equity is called owner's equity.
   v. Since stockholders own a corporation, equity is called stockholders' equity.
b. **Discussion Activity 2:** *Give an example of what a company would have as an asset and a liability. Then consider what an individual would have as an asset and a liability*. (PPT Slides 26-27)
   1. *How would an asset differ from a business compared to an individual?*
   2. *How would a liability differ from a business compared to an individual?*
   3. *Can an individual calculate their net worth using the same accounting equation as a business?*
      - What kinds of assets and liabilities did you find similar between a business and an individual?
      - Using fictitious numbers, can you give an example of using the accounting equation to calculate an individual's net worth?
      - Does relating the accounting equation to calculate an individual's net worth make it easier to understand what is meant by a company's equity?

IV. Business Transactions and the Accounting Equation (1-4, PPT Slides 28–44, BUSPROG: Analytic, AICPA: FN-Measurement)

a. Transactions, such as depositing cash, purchasing assets, selling services, and paying bills, affect the accounting equation. This shows students that through each transaction the two sides of the accounting equation must always be equal.
b. Using a sample company called NetSolutions, this objective demonstrates how business transactions affect a company's financial condition.

c. Exhibit 6 (PPT Slide 41) shows a summary of transactions for NetSoutions.
    i. The effect of every transaction is an increase or a decrease in one or more of the accounting equation elements.
    ii. The two sides of the accounting equation are always equal.
    iii. The owner's equity is increased by amounts invested by the owner.
    iv. The owner's equity is increased by revenues and decreased by expenses.
    v. The owner's equity is decreased by withdrawals by the owner.

d. **Knowledge Check Activity 2:** *Charles Lambert buys an adjoining piece of land to expand his public golf course. He pays $89,000 in cash to acquire this land. Based on the accounting equation, what would be the effect of this transaction?* (PPT Slides 43–44)
    - The answer is Cash −89,000, Land +89,000.
    - Cash would decrease by $89,000, and Land would increase by $89,000.

V. Financial Statements (1-5, PPT Slides 45-56, BUSPROG: Analytic, AICPA: FN-Reporting)

a. This objective explores the income statement, statement of owner's equity, balance sheet, and statement of cash flows.
b. Exhibit 8 (PPT Slide 46) shows the order in which the financial statements are prepared.
c. Using the same NetSolutions example as the previous objective, the order, preparation, and relationship among the four financial statements is demonstrated.
    i. Exhibit 9 (PPT Slides 47–48) shows the four financial statements for NetSolutions.
d. The income statement is the first one prepared.
    i. Revenue minus expenses is known as net income, net profit, or earnings.
    ii. If expenses exceed revenue, the excess is a net loss.
e. The statement of owner's equity reports the changes in owner's equity.
    i. It is prepared *after* the income statement because the net income or net loss for the period is reported on the statement of owner's equity.
    ii. It is prepared *before* the balance sheet because the amount of owner's equity at the end of the period is reported on the balance sheet.

iii. Because of this, the statement of owner's equity is viewed as the connecting link between the income statement and the balance sheet.

f. The balance sheet reports the amount of assets, liabilities, and owner's equity in a vertical format at a certain point in time.
g. The statement of cash flows has three sections: operating, investing, and financing activities.
h. Exhibit 10 (PPT Slide 53) explains the interrelationships between the financial statements.
i. The balance sheet is the connecting link between the financial statements, and this is shown in Exhibit 11 (PPT Slide 54).
j. **Knowledge Check Activity 3:** *Which financial statement would the owner want to review if they are interested in the company's sales, expenses, and net income or loss?* (PPT Slides 55–56)
    - The answer is income statement.
    - The income statement would list a company's sales, expenses, and net income or loss.

VI. Analysis for Decision Making: Ratio of Liabilities to Owner's (Stockholders') Equity (1-6, PPT Slides 57-59, BUSPROG: Analytic, AICPA: FN-Measurement)

a. Basic financial statements are useful to bankers, creditors, investors, and others in analyzing and interpreting the financial performance and condition of a company.
b. Various tools and techniques that are often used to analyze and interpret a company's financial performance and condition are described and illustrated below and on the next two slides.
c. The relationship between liabilities and owner's equity can be expressed as a ratio of liabilities to owner's equity, as follows: Ratio of Liabilities to Owner's Equity = Total Liabilities ÷ Total Owner's Equity.
d. Most large companies are organized as corporations, so the relationship is expressed as the ratio of liabilities to stockholders' equity. To illustrate, data from recent balance sheets of Alphabet and Meta are used.
e. The lower the ratio of liabilities to stockholders' equity, the better able the company is to withstand poor business conditions and to pay its obligations to creditors. Ratios less than 1.0 are protective to creditors.

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## Additional Discussion Questions

The following are discussion questions that do not appear in the text, PPTs, or courseware (if courseware exists)—they are for you to use as you wish. You can assign these questions several ways: in a discussion forum in your LMS; as whole-class discussions in person; or as a partner or group activity in class.

1. Discussion: Importance of Accounting (Nature of Business and Accounting, 1-1, PPT Slide 8) Duration 10 minutes.

    a. The role of accounting is to provide information to businesses about their activities, including operating, investing, and financing. Why is "accounting" so important?
        i. Answer: Accounting is the language of business. Without an organized system that provides information to users about the economic activities and condition of a business, there would be no guarantee of a company being profitable or continuing in existence.

    b. Why do I need to know about accounting if I am not going to be an accountant?
        i. Answer: Any business professional needs to be aware of the functions and information provided by an accounting system. Without these vital data, such as information on sales, expenses, assets, liabilities, and equity, a business cannot survive, nor can its owners be assured of its profitability. Basic financial statements, such as the income statement and balance sheet, provide useful information for all users, internal and external, regarding a business. For example, if you are a marketing manager, it is important to know the expenses of the company's product or service to ensure the items are sold at a price that will provide a profit. Every employee of a business has a responsibility to uphold the company's mission to attain and sustain profitability.

2. Discussion: Recording Financial Transactions (Business Transactions and the Accounting Equation, 1-4) Duration 10 minutes.

    a. Why can't I just use a computer program to do all my accounting? Isn't that what technology is for?
        i. Answer: Technology and software are extremely useful tools in all areas of business. Today's accounting software allows companies to record and process transactions very quickly and has many safeguards to protect against errors such as incorrect account

numbers, math mistakes, unbalanced journal entries, and confusion in creating financial statements. However, financial and accounting systems are maintained by humans who need to provide directions and “rules” within the software programs. Accounting rules can change, and in certain areas, such as payroll processing, they vary from year to year or even more often—think of tax rate changes and employment laws. So, while technology and accounting software are superb tools, it is important for trained employees to monitor the input and output carefully and to know how accounting works to use their judgment in processing data.

3. Discussion: Items Listed on Financial Statements (Financial Statements, 1-5, PPT Slides 47–48) Duration 15 minutes.

    a. The accounting system classifies different items into categories to help group similar items together for reporting and analysis. What is the difference between revenues and assets? Give examples of these items.
        i. Answer: Revenues are income derived from the sales of a company’s products or services. These will change over time as the company grows or has seasonal activity. For example, a company such as Hershey’s Food Corporation has increased sales prior to major holidays. A company’s assets are resources that a company owns to provide the ability to earn revenues. For example, FedEx owns many delivery trucks and planes to earn revenues from delivering packages. Examples of assets include property, plant, and equipment, as well as cash, accounts receivable, and inventory.

    b. What is the difference between expenses and liabilities? Give examples of these items.
        i. Answer: Expenses are costs incurred by a company to make a product or provide a service. Examples of expenses include rent, payroll costs, raw materials, shipping, travel, and many others. Liabilities are amounts owed by the company to another entity. Examples of liabilities include mortgages, accounts payable to vendors, bond interest payable to bondholders, etc.

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