ACCTG 211 – Exam 1 – Practice Exam Solutions

1. **B** – Historical cost

2. (1) Analyze transactions and create journal entries, (2) poster journal entries to ledger accounts, (3) Balance ledger accounts and transfer balances to unadjusted trial balance

3. **C** – The income statement is prepared first because you need net income to create the statement of shareholders' equity, which is the 2nd statement that is prepared.

4. **A** – They increase retained earnings in the shareholders' equity section. This is why we always credit revenues.

5. **C** – The balance sheet in the current assets section. Money a company is owed is referred to as accounts receivable.

6. **C** – $450,000 because we need to increase the sales revenue of $420,000 by $30,000 to account for the previously unearned revenue.

7. **A** – $14,000 because we need to reduce the balance of the unearned revenue account by $30,000 since the revenue is now earned.

8. **A** – $100 because the adjusted balance of the supplies account is what is left in the supplies account at the end of the period. We were given this value because we were told we had $100 of unused supplies.

9. **B** – $17,600

   Monthly Ins Exp = $22,000 / 10 = $2,200

   Two months have passed since the policy was purchased on 2/1.

   Ins Exp = $2,200 x 2 = $4,400

   Prepaid Ins = $22,000 – $4,400 = $17,600

10. **D** – $4,250. The wages payable account will increase by the amount earned but not paid to employees during the current pay period.

    Wages payable = $3,000 + $1,250
    Wages payable = $4,250

11. **B** – $4,000. Interest payable will increase by the amount of the interest expense for the year.

    Interest expense = $100,000 x 0.04
    Interest expense = $4,000

12. **B** – $16,000

    Depreciation expense = ($100,000 – $20,000) / 5
    Depreciation expense = $16,000

13. (1) Determine required adjustments and create adjusting journal entries, (2) Post adjusting entries to ledger accounts, (3) Rebalance ledger accounts and transfer balances to adjusted trial balance

14. **A** – Debit operating expenses $35,000; Credit cash $35,000. We debit operating expenses because expenses reduce shareholders equity. This is also why we always debit expenses. We credit cash because it is an asset that is decreasing.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
($35,000) cash						($35,000) operating expenses

15. **D** - This represents the Going-Concern assumption. If a company has long-term assets on its balance sheet, it is assumed it will continue its operations for future periods.

16. **C** – For this problem you will need to find Ferro Co.'s retained earnings for this year then add the retained earnings for the year to the beginning balance of the retained earnings account because retained earnings is a continuously increasing account.

    Retained earnings for the year = Net income – Dividends
    Retained earnings for the year = $80,000 - $50,000 = $30,000

    Total retained earnings = Beginning retained earnings + Retained earnings for the year
    Total retained earnings = $10,000 + $30,000 = $40,000

17. **No effect on net income** – We can see neither revenues nor expenses are impacted by the transaction below.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
($2,000) cash $2,000 prepaid insurance						

18. **Decrease cash flows** – We can see cash decreases in the transaction below.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
($2,000) cash $2,000 prepaid insurance						

19. **No effect on net income** – We can see neither revenues nor expenses are impacted by the transaction below.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$9,000 cash ($9,000) accounts receivable						

20. **Increase cash flows** – We can see that cash increases in the transaction below.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$9,000 cash ($9,000) accounts receivable						

21. **Decrease net income** – The interest expense in the transaction below will decrease net income.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
		$420 interest payable				($420) interest expense

22. **No effect on cash flows** – The transaction below does not impact cash flows.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
		$420 interest payable				($420) interest expense

23. **No effect on net income** – The transaction below does not impact revenues or expenses.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$350,000 cash				$350,000 common stock		

24. **Increase cash flows** – The transaction below increases cash flows.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$350,000 cash				$350,000 common stock		

25. **B** – A clothing company will use a computer to run its business so the computer is considered equipment. Inventory is only goods that a company sales as part of its core operations. For a clothing company, clothing would be considered inventory.

26. **B** - Selling stock is a method of financing for a corporation, so this would be an inflow under the financing section.

27. **C** – Our accountant should have increased accounts receivable and revenue for this accounting period because the revenue was earned during the current accounting period. However, he did not record the revenue so both accounts receivable and revenue will be understated.

Assets	Liabilities	SE	Rev	Exp	NI
U			U		

Assets	Liabilities	SE	Rev	Exp	NI
U	NE	U	U	NE	U

28. **C** – Our accountant should have recorded salary expense for the period and increased salaries payable for the same amount; however, he did not record this transaction so both salary expense and salaries payable will be understated.

Assets	Liabilities	SE	Rev	Exp	NI
	U			U	

Assets	Liabilities	SE	Rev	Exp	NI
NE	U	O	NE	U	O

29. **A** – Our accountant should have increase revenue for the current period while decreasing unearned revenue, a liability, because the revenue has now been earned. Our accountant did not do either of these so revenue will be understated and unearned revenue, a liability, will be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
	O		U		

Assets	Liabilities	SE	Rev	Exp	NI
NE	O	U	U	NE	U

30. **C** – We can initially deduce from the information given that expenses are overstated and assets are understated.

Assets	Liabilities	SE	Rev	Exp	NI
U				O	

Assets	Liabilities	SE	Rev	Exp	NI
U	NE	U	NE	O	U

31. **C** – Our accountant should have recorded the insurance expense and then reduced the asset prepaid insurance. Since he did not record this transaction, expenses will be understated and assets will be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
O				U	

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	NE	U	O

32. **C** – A balance sheet is the only financial statement above that summarizes a company's financial position at a given date. All the other statements summarize financial performance over a specified period of time.

33. **D** – Debit salaries expense $16,000; Credit cash $16,000. All salary expenses were paid during the current month so we do not need to record a salaries payable liability for this transaction. We debit salaries expense because it reduces SE. This is why we always debit expenses. We credit cash because it is an asset that is decreasing.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
($16,000) cash						($16,000) salaries expense

34. **A** – Debit cash $24,000; Credit note payable $24,000. We debit cash because it is an asset that is increasing. We credit note payable because it is a liability that is increasing.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$24,000 cash		$24,000 note payable				

35. **A**

Assets = Liabilities + Shareholders Equity
$50,000 = $35,000 + SE
SE = $15,000

36. **C** – This first thing you need to do to solve this problem is find the change in SE between 2005 and 2006. The change in SE will tell you what the RE was in 2006 because there were no investments in contributed capital. Then you can solve for the NI for 2006.

    SE 2005 = $750,000 - $390,000 = $360,000
    SE 2006 = $1,250,000 - $500,000 = $750,000
    Change in SE = $750,000 - $360,000 = $390,000

    $Dividends_{2006} = NI_{2006} – RE_{2006}$
    $900,000 = NI_{2006} - $390,000
    NI_{2006} = $1,290,000

37. **D**

    Retained Earnings = Beginning Balance + Net Income – Dividends
    RE= 350,000 + (780,000 – 520,000) – 100,000
    RE= 510, 000

38. **C** – This problem gives you a good bit of extra information. Remember that NI is simply revenues minus expenses.

    NI = $100,000 - $25,000 - $15,000 - $30,000 = $30,000

39. **D** – We record revenue once a good is shipped or a service is delivered. It does not matter when cash is actually received.

40. **C** – We started 2006 with $1,000 in the unearned revenue account. Then we increased unearned revenue by $50,000 with a credit to the account so we had a total of $51,000 in unearned revenue. The only way for the unearned revenue account to go down is for us to earn the revenue. Since the unearned revenue account had a balance of $7,000 at the end of 2006 we must have earned $44,000 in revenue in 2006 ($51,000 - $7,000 = $44,000).

41. **D** – Debit dividends for $40,000 and Credit dividends payable for $40,000. We debit dividends because the account will reduce the retained earning section of shareholders' equity. We credit dividends payable because it is a liability that is increasing.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
		40,000 Dividends Payable				(40,000) Dividends

42. **A** – We can initially deduce that liabilities and expenses are overstated.

Assets	Liabilities	SE	Rev	Exp	NI
	O			O	

Assets	Liabilities	SE	Rev	Exp	NI
NE	O	U	NE	O	U

43. **C** - At the end of the year, the company must accrue for the salary expense up until December 31, regardless if the employees had been paid or not. Therefore, since the company has a $25,000 payroll for a five-day work week, and since the year end falls on a Wednesday, the company will expense $15,000 ($5,000 per day) in salary expense and create a salary payable of $15,000 until the employees are paid.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
		15,000 Salary Payable				(15,000) Salary Expense

44. **B** – When the company pays its employees at the end of the week, it will pay $25,000 in cash, expense the $10,000 for the two days it has not yet expense, and decrease the liability Salary Payable which it has now satisfied by paying cash.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
(25,000) Cash		(15,000) Salary Payable				(10,000) Salary Expense

45. **B** – WE STILL NEED TO ACCRUE FOR INTEREST EVEN THOUGH WE HAVE NOTE PAID ANY YET!

    Interest expense = Principal x Rate x Time
    Interest expense = $100,000 x .06 x 6/12 = $3,000

46. **D** –$4,100

    Supplies Expense = Beg Balance in Supplies + Supply Purchases – Ending Balance in Supplies
    Supplies Expense =$3,500 + $2,200 - $1,600 = $4,100

47. **D –** Accumulated depreciation

48. **C** – To solve this problem you will first need to solve for the annual depreciation expense under straight line depreciation. However, this will not be the answer because we only used the machine for 9 months during 2004.

    Annual depreciation expense = ($9,300 - $700)/8 = $1,075

    9 month depreciation expense = $1,075 x 9/12 = $806.25

49. **C** – To find the book value on Dec 31, 2005 you will first need to solve for the accumulated depreciation on Dec 31, 2005. We solved for the depreciation expense for 2004 in the problem above. Since we will use the machine for all of the 2005 the depreciation expense for 2005 will be $1,075.

    Accumulated depreciation Dec 31, 2005 = $806.25 + $1,075 = $1,881.25

    Book value Dec 31, 2005 = $9,300 - $1,881.25 = $7,418.75

50. **D** – Not recording depreciation expense will cause our expenses to be understated. Additionally, because we understated depreciation it will cause our assets to be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
O				U	

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	NE	U	O

51. **D** – The company recorded the amount of the loan as more than it actually was. This means that cash (asset) will be overstated and notes payable (liability) will be overstated. Neither revenues nor expenses are affected by the transaction. Thus net income will not be affected.

Assets	Liabilities	SE	Rev	Exp	NI
O	O				

Assets	Liabilities	SE	Rev	Exp	NI
O	O	NE	NE	NE	NE

52. **B** – The company should have recorded an interest expense and increased interest payable. Since nothing was recorded, expenses and liabilities will both be understated.

Assets	Liabilities	SE	Rev	Exp	NI
	U			U	

Assets	Liabilities	SE	Rev	Exp	NI
NE	U	O	NE	U	O

53. **D** – The company should have reduced cash and increased notes receivable. Cash should have been reduced by the same amount that notes receivable should have increased. Consequently, the amount of total assets is not affected by this transaction. Neither revenues nor expenses are affected by the transaction. Thus net income will not be affected.

Assets	Liabilities	SE	Rev	Exp	NI
NE	NE	NE	NE	NE	NE

54. **A** – The company should have recorded interest revenue and increased interest receivable (asset).

Assets	Liabilities	SE	Rev	Exp	NI
U			U		

Assets	Liabilities	SE	Rev	Exp	NI
U	NE	U	U	NE	U

55. **C** – The company recorded too much revenue and increased accounts receivable by too much.

Assets	Liabilities	SE	Rev	Exp	NI
O			O		

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	O	NE	O

56. **D** – The amount recorded for cash was understated, and the reduction to accounts receivable was understated. However, since both cash and accounts receivable are assets, nothing is affected by the transaction.

Assets	Liabilities	SE	Rev	Exp	NI
NE	NE	NE	NE	NE	NE

57. **E** – All of the above. Note that we say dividends are increasing even though they have a negative sign in the accounting equation. When dividends increase, they cause retained earnings to decrease. This is why dividends have the negative sign in the accounting equation. The negative sign is showing the increase in dividends is causing retained earnings to decrease.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
		$40,000 dividends payable				($40,000) dividends

58. **B** – Liabilities decrease

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
($40,000) cash		($40,000) dividends payable				

59. **A** – Statement of cash flows

60. **C** – We need to make it so the temporary accounts are ready to use for the next period. We use the closing entries to give the revenue, expense, and dividend accounts a balance of $0 for the start of the next period.

61. (1) Creasing closing journal entries, (2) Post closing entries to ledger account, (3) Rebalance ledger accounts and transfer balances to post-closing trial balance

62. **D** – Since the company has not delivered the service, it cannot record the receipt of cash as revenue. Instead, the company will increase cash and increase unearned revenue (liability). This means that both cash and unearned revenue will be overstated. Neither revenues nor expenses are affected by this transaction.

Assets	Liabilities	SE	Rev	Exp	NI
O	O	NE	NE	NE	NE

63. **A** – When the company provided the service that had already been paid for, it should have recognized the revenue from selling the product and reduced the liability unearned revenue. However, this was not recorded so liabilities are overstated and revenue is understated.

Assets	Liabilities	SE	Rev	Exp	NI
	O		U		

Assets	Liabilities	SE	Rev	Exp	NI
NE	O	U	U	NE	U

64. **C** – Expenses will be understated. It is not clear if cash or prepaid insurance should have been reduced when the expense was recorded; however, it doesn't matter because either way assets would have been reduced. This means that assets will be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
O				U	

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	NE	U	O

65. **D** – Expenses will be overstated. It is not clear if cash or prepaid rent was reduced by the transaction; however, it doesn't matter because they are both assets. This means assets will be understated.

Assets	Liabilities	SE	Rev	Exp	NI
U				O	

Assets	Liabilities	SE	Rev	Exp	NI
U	NE	U	NE	O	U

66. **D** – The company should have reduced cash and increased prepaid rent. However, these are both assets so total assets will not be affected by the transaction. This transaction does not affect revenues or expenses.

Assets	Liabilities	SE	Rev	Exp	NI
NE	NE	NE	NE	NE	NE

67. **D** – The amount of cash was reduced by too much and the amount of prepaid rent was increased by too much. However, these are both assets so total assets will not be affected by the transaction. This transaction does not affect revenues or expenses.

Assets	Liabilities	SE	Rev	Exp	NI
NE	NE	NE	NE	NE	NE

68. **B** – A debit to rent expense for $2,000

69. **A** – Debit supplies, credit accounts payable

70. **C** – Debit accounts payable, credit cash

71. **B –** Debit revenues, credit expenses, and credit retained earnings. See step 7 in the appendix B example in the packet.

72. **D** – Dividends are decreased by debits.

73. **B** – It is the same thing as a balance sheet.

74. **D** – Accumulated depreciation. See step 7 in the appendix B example in the packet.

75. **A** – Ensure that retained earnings has the correct balance.

76. **B** – Expenses are always a debit.

77. **A** - This transaction increases cash and increases common stock. Therefore, cash, an asset, is debited (see that it is written first) and common stock, an equity account, is credited (see that it is indented and written second).

78. **C** - Remember, when we accrue an expense, we must set up a liability account. In this case, we create a salary payable account. Since we are increasing our expenses, we debit salary expense and as we are increasing a liability, we credit the salary payable account.

79. **D** - Retained Earnings is considered an ongoing account since the ending balance one year becomes the beginning balance the next year. Revenues, Expenses, and Dividends are not ongoing, and are therefore closed at the end of every accounting period to Retained Earnings.

80. **C** – The trick to this problem is realizing that it is asking about the **correcting** entry, which is the same thing as the closing entry. We don't want to record the dividend, we want to close the dividend account to retained earnings. Dividends is a temporary account, and therefore, it must be closed to Retained Earnings at the end of an accounting period. We always debit dividends when they are recorded. Thus we must credit dividends to close the account. We will then debit that amount to retained earnings.

81. **C** – Corporation

82. **B** – Historical cost

83. **A** – They increase retained earnings in the shareholder's equity section

84. **E** – This problem is a little confusing because we do close dividends out to retained earnings as part of the closing process. However, this problem is specifically asking about the amount that will be closed to retained earnings **for net income**. Dividends are not on the income statement because they are not an expense so they are not part of solving this problem. Thus, this problem only wants us to look at closing revenues and expenses to retained earnings because revenues and expenses are what are found on the income statement. Sales revenue is the only revenue account listed. There are three expenses listed in the problem: interested expense, salary expense, and rent expense. All of the other accounts provided are permanent accounts so they do not need to be closed out at the end of the year.

    Sales Revenue = $450
    Expenses = $60 + $60 + $60 = $180

    Amount closed to RE for net income = $450 – $180
    Amount closed to RE for net income = $270

85. **A** – Since rent expense wasn't recorded, expenses will be understated. It is not clear if the transaction should have reduced cash or prepaid rent; however, it doesn't matter because both accounts are assets. Thus we know that assets will be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
O				U	

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	NE	U	O

86. **C** – Expenses will be overstated because the problem tells us accrued salary expense was overstated. Since the salary expense is an **accrued** expense, it means that the expense has been incurred; however, it has not yet been paid. So when the expense is recorded the liability salaries payable is increased. Thus liabilities will be overstated as well.

Assets	Liabilities	SE	Rev	Exp	NI
	O			O	

Assets	Liabilities	SE	Rev	Exp	NI
NE	O	U	NE	O	U

87. **C** – Supplies are considered assets until they are used. When the supplies expense is recorded at the end of the period, assets are reduced by the amount of the supplies expense. Since supplies expense was understated, assets will be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
O				U	

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	NE	U	O

88. **D** – Our company should have increased cash by the amount of the loan and recorded the liability notes payable. This did not happen to assets and liabilities will be understated. This transaction has no effect on revenues or expenses so there is no effect on net income as well.

Assets	Liabilities	SE	Rev	Exp	NI
U	U				

Assets	Liabilities	SE	Rev	Exp	NI
U	U	NE	NE	NE	NE

89. **A** – Depreciation expense reduces total assets. Since depreciation expense was understated, the value of total assets will be overstated.

Assets	Liabilities	SE	Rev	Exp	NI
O				U	

Assets	Liabilities	SE	Rev	Exp	NI
O	NE	O	NE	U	O

90. **D** – Cash should have decreased and supplies should have increased; however, they are both assets so there is no effect on total assets. Neither revenues nor expenses are affected by this transaction.

Assets	Liabilities	SE	Rev	Exp	NI
NE	NE	NE	NE	NE	NE

91. **B** – Debit cash $80,000; Credit common stock $80,000. We debit cash because it is an asset that is increasing, and we credit common stock because it is a SE account that is increasing.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$80,000 cash				$80,000 common stock		

92. **C** – Debit cash $8,000; Debit accounts receivable $70,000; Credit service revenue $78,000. We debit cash and accounts receivable because they are assets that are increasing. We credit service revenue because it is an SE account that is increasing. Also, we also credit revenue.

Assets	=	Liabilities	+	Shareholders' equity		
				Contributed capital	+	Retained earnings
$8,000 cash $70,000 accounts receivable						$78,000 service revenue