

Chapter 2 Questions

Multiple Choice

1. A current asset is
 - a. the last asset purchased by a business.
 - b. an asset which is currently being used to produce a product or service.
 - c. usually found as a separate classification in the income statement.
 - d. expected to be converted to cash or used in the business within a relatively short period of time.

2. Trademarks would appear in which balance sheet section?
 - a. Intangible assets
 - b. Investments
 - c. Property, plant, and equipment
 - d. Current assets

3. Equipment is classified on the balance sheet as
 - a. a current asset.
 - b. property, plant, and equipment.
 - c. an intangible asset.
 - d. a long-term investment.

*****Use the following information to answer the questions for 4, 5, and 6**

Koonce Office Supplies
Balance Sheet
December 31, 2017

Cash	\$	195,000	Accounts payable	\$	210,000
Accounts receivable		150,000	Salaries and wages payable		30,000
Inventory		165,000	Mortgage payable		<u>240,000</u>
Prepaid insurance		90,000	Total liabilities		\$480,000
Stock investments (Short-Term)		255,000			
Land		270,000			
Buildings	\$315,000		Common stock		\$360,000
Less: Accumulated depreciation		<u>(60,000)</u>	Retained earnings		<u>750,000</u>
Trademarks		<u>210,000</u>	Total stockholders' equity		<u>\$1,110,000</u>
Total assets		<u>\$1,590,000</u>	Total liabilities and stockholders' equity		<u>\$1,590,000</u>

4. What is the total dollar amount of assets to be classified as current assets?
 - a. \$855,000
 - b. \$600,000
 - c. \$510,000
 - d. \$435,000

5. What is the total dollar amount of assets to be classified as classified as property, plant, and equipment?
 - a. \$990,000
 - b. \$525,000
 - c. \$735,000
 - d. \$585,000

6. What is the total dollar amount of assets to be classified as investments?
- \$525,000
 - \$0
 - \$255,000
 - \$465,000
7. Accounts Receivable is classified on the balance sheet as
- a current asset.
 - property, plant, and equipment.
 - an intangible asset.
 - a long-term investment.
8. On a classified balance sheet, companies usually list current assets
- in alphabetical order.
 - with the largest dollar amounts first.
 - in the order in which they are expected to be converted into cash.
 - in the order of acquisition.
9. In the current year Company Z had cash receipts of \$35,000 and cash disbursements of \$20,000. Company Z's ending cash balance at December 31 of the current year was \$65,000. What was Company Z's beginning cash balance?
- \$50,000
 - \$60,000
 - \$85,000
 - \$80,000
10. What organization issues U.S. accounting standards?
- Security Exchange Commission
 - International Accounting Standards Committee
 - International Auditing Standards Committee
 - Financial Accounting Standards Board
11. The two fundamental qualities of useful information are
- relevance and faithful representation.
 - verifiability and timeliness.
 - comparability and flexibility.
 - understandability and consistency.
12. In order for accounting information to be relevant, it must
- have very little cost.
 - help predict future events or confirm prior expectations.
 - not be reported to the public.
 - be used by a lot of different firms.

13. The assumption that requires only those things that can be expressed in money are included in the accounting records is the
- economic entity assumption.
 - monetary unit assumption.
 - going concern assumption.
 - periodicity assumption.
14. The concept that a business has a reasonable expectation of remaining in business for the foreseeable future is called the
- economic entity assumption.
 - monetary unit assumption.
 - periodicity assumption.
 - going concern assumption.
15. Company J has two buildings that cost \$800,000. The current market value of the buildings is \$1,200,000. The buildings will be reported as assets at
- \$1,200,000
 - \$400,000
 - \$800,000
 - \$2,000,000

EXERCISES

1. The following lettered items represent a classification scheme for a balance sheet, and the numbered items represent data found on balance sheets. In the blank next to each account, write the letter indicating to which category it belongs.

- Current assets
- Investments
- Property, plant, and equipment
- Intangible assets
- Current liabilities
- Long-term liabilities
- Stockholders' equity
- Not on the balance sheet

- | | | | |
|----------|---------------------------------|-----------|----------------------------|
| _____ 1. | Accumulated depreciation-equip. | _____ 6. | Inventory |
| _____ 2. | Common stock | _____ 7. | Patents |
| _____ 3. | Interest expense | _____ 8. | Prepaid insurance |
| _____ 4. | Salaries and wages payable | _____ 9. | Mortgage payable |
| _____ 5. | Retained earnings | _____ 10. | Land (held for investment) |

2. Each of the following statements is justified by a fundamental quality or an enhancing of quality accounting. Write the letter in the blank next to each statement corresponding to the quality involved.

- | | | | |
|----|-------------------|----|-------------------------|
| a. | Comparability | d. | Consistency |
| b. | Understandability | e. | Relevance |
| c. | Verifiable | f. | Faithful representation |

____ 1. A company uses the same accounting principles from year to year.

____ 2. Information that is free from error.

____ 3. Information presented in a clear and concise fashion.

____ 4. Information that makes a difference in a decision.

____ 5. Information accurately depicts what really happened.

3. Presented below are the basic assumptions and principles underlying financial statements.

- | | | | |
|----|----------------------------|----|--------------------------|
| a. | Historical cost principle | d. | Going concern assumption |
| b. | Economic entity assumption | e. | Monetary unit assumption |
| c. | Full disclosure principle | f. | Periodicity assumption |

Identify the basic assumption or principle that is described below.

___ 1. The economic life of a business can be divided into artificial time periods.

___ 2. The business will continue in operation long enough to carry out its existing objectives.

___ 3. Assets should be recorded at their cost.

___ 4. Economic events can be identified with a particular unit of accountability.

___ 5. Circumstances and events that make a difference to financial statement users should be disclosed.

___ 6. Only transaction data that can be expressed in terms of money should be included in the accounting records.

4. These items are taken from the financial statements of Donovan Company at December 31, 2019.

Buildings	\$95,800
Accounts receivable	15,600
Prepaid insurance	4,680
Cash	18,840
Equipment	79,400
Land	61,200
Insurance expense	780
Depreciation expense	7,300
Interest expense	2,600
Common stock	57,000
Retained earnings (January 1, 2019)	40,000
Accumulated depreciation—buildings	45,600
Accounts payable	15,500
Mortgage payable	88,600
Accumulated depreciation—equipment	18,720
Interest payable	3,600
Service revenue	17,180

Instructions

Prepare a classified balance sheet. Assume that \$13,600 of the mortgage payable will be paid in 2020.

Chapter 2 Solutions**Multiple Choice Solutions**

1. D
2. A
3. B
4. A
5. B
6. B
7. A
8. C
9. A
10. D
11. A
12. B
13. B
14. D
15. C

Exercise Solutions

1. 1. C 2. G 3. H 4. E 5. G 6. A 7. D 8. A 9. F 10. B
2. 1. D 2. F 3. B 4. E. 5. F
3. 1. F 2. D 3. A 4. B 5. C 6. E

Exercises Solutions (Cont.)

4.

DONOVAN COMPANY

Balance Sheet
December 31, 2017

Assets			
Current assets			
Cash		\$18,840	
Accounts receivable		15,600	
Prepaid Insurance		<u>4,680</u>	
Total current assets (Cash + Acc. rec. + Prep. ins.)			\$39,120
Property, plant, and equipment			
Land		61,200	
Buildings.....	\$95,800		
Less: Accumulated depreciation— buildings.....	<u>45,600</u>	50,200	
Equipment	79,400		
Less: Accumulated depreciation— equipment	<u>18,720</u>	<u>60,680</u>	<u>172,080</u>
Total assets			<u>\$211,200</u>

(Tot. cur. assets + Land + Build. – Acc. depr. + Equip. – Acc. depr.)

Liabilities and Stockholders' Equity			
Current liabilities			
Accounts payable		\$ 15,500	
Current portion of note payable		13,600	
Interest payable		<u>3,600</u>	
Total current liabilities			\$ 32,700
Long-term liabilities			
Mortgage payable			<u>75,000</u>
Total liabilities			107,700
Stockholders' equity			
Common stock.....		57,000	
Retained earnings (\$40,000 + \$6,500*)		<u>46,500</u>	
Total stockholders' equity			<u>103,500</u>
Total liabilities and Stockholders' equity			<u>\$211,200</u>

(Tot. cur. liab. + Mort. pay. + Com. stock + Beg. ret. earn. + Net. inc.*)

*Net income = \$17,180 – \$780 – \$7,300 – \$2,600 = \$6,500