

Chapter 3 Questions

Multiple Choice

1. The **revenue recognition** principle state that:
 - a. Expenses should be matched with revenues
 - b. Revenue should be recognized in the accounting period in which a performance obligation is satisfied
 - c. The fiscal year should correspond with the calendar year
 - d. The economic life of a business can be divided into artificial time periods.
2. **Accumulated Depreciation** is a(n):
 - a. expense account.
 - b. stockholders' equity account.
 - c. liability account.
 - d. contra asset account.
3. If a business has received cash in advance of services performed and credits a liability account, the **adjusting entry** needed after the services are performed will be:
 - a. debit Unearned Service Revenue and credit Cash.
 - b. debit Unearned Service Revenue and credit Service Revenue.
 - c. debit Unearned Service Revenue and credit Prepaid Expense.
 - d. debit Unearned Service Revenue and credit Accounts Receivable.
4. A law firm has billed their clients for services performed. They subsequently received payments from their clients. What entry will the law firm make **upon receipt of the payments**?
 - a. Debit Unearned Service Revenue and credit Service Revenue
 - b. Debit Cash and credit Accounts Receivable
 - c. Debit Accounts Receivable and credit Service Revenue
 - d. Debit Cash and credit Service Revenue
5. The **expense recognition** principle matches:
 - a. customers with businesses.
 - b. expenses with revenues.
 - c. assets with liabilities.
 - d. creditors with businesses.
6. Given the data below for a firm in its first year of operation, **determine net income** under the **accrual** basis of accounting.

Revenue recognized	\$19,000
Accounts receivable	3,000
Expenses incurred	7,250
Accounts payable (related to expenses)	750
Supplies purchased with cash	1,800

 - a. \$11,750
 - b. \$14,000
 - c. \$9,500
 - d. \$12,200

7. La More Company had the following transactions during 20X1.

- Sales of \$9,000 on account
- Collected \$4,000 for services to be performed in 20X2
- Paid \$2,650 cash in salaries
- Purchased airline tickets for \$500 in December for a trip to take place in 20X2

What is La More's 20X1 net income using **cash basis** accounting?

- a. \$10,350
- b. \$1,350
- c. \$9,850
- d. \$850

8. The **primary source** used in the preparation of the financial statements is the:

- a. trial balance.
- b. post-closing trial balance.
- c. general trial balance.
- d. adjusted trial balance.

9. Which of the following statements about the **accrual basis** of accounting is False?

- a. Events that change a company's financial statements are recorded in the periods in which the events occur.
- b. Revenue is recorded only when cash is received, and expense is recorded only when cash is paid.
- c. Revenue is recognized in the period in which services are performed
- d. This basis is in accordance with GAAP (Generally accepted accounting principles)

10. On July 1 the Fisher Shoe Store paid \$24,000 to Acme Realty for 6 months rent beginning July 1. **Prepaid Rent** was debited for the full amount. If financial statements are prepared on July 31, the **adjusting entry** to be made by the Fisher Shoe Store is:

- a. debit Rent Expense, \$24,000; credit Prepaid Rent, \$4,000.
- b. debit Prepaid Rent, \$4,000; credit Rent Expense, \$4,000.
- c. debit Rent Expense, \$4,000; credit Prepaid Rent, \$4,000.
- d. debit Rent Expense, \$24,000; credit Prepaid Rent, \$20,000.

11. The Harris Company purchased equipment for \$15,000 on December 1. It is estimated that annual **depreciation** on the computer will be \$3,000. If financial statements are to be prepared on December 31, the company should make the following **adjusting entry**:

- a. debit Depreciation Expense, \$3,000; credit Accumulated Depreciation, \$3,000.
- b. debit Depreciation Expense, \$250; credit Accumulated Depreciation, \$250.
- c. debit Depreciation Expense, \$12,000; credit Accumulated Depreciation, \$12,000.
- d. debit Equipment, \$15,000; credit Accumulated Depreciation, \$15,000.

12. If a company fails to adjust an **Unearned Rent Revenue** account for rent that has been recognized, what effect will this have on that month's financial statements?

- a. Assets will be understated and revenues will be understated.
- b. Liabilities will be understated and revenues will be understated.
- c. Liabilities will be overstated and revenues will be understated.
- d. Assets will be overstated and revenues will be understated.

13. Adjustments for **prepaid expenses**:

- a. decrease assets and increase revenues.
- b. decrease expenses and increase assets
- c. decrease revenues and increase assets
- d. decrease assets and increase expenses

14. **Adjusting entries** are made to ensure that:

- a. expense are recognized in the period in which they are incurred.
- b. revenues are recorded in the period in which the performance obligation is satisfied.
- c. balance sheet and income statement accounts have correct balances at the end of an accounting period.
- d. All of these answer choices are correct.

15, Chris Harper earned a salary of \$550 for the last week of January. She will be paid on Feb 1. The adjusting entry for Chris' employer at Jan 31 is:

- a. Dr. Salaries and Wages Expense \$550
 Cr. Salaries and Wages Payable \$550
- b. Dr Salaries and Wages Expense \$550
 Cr Cash \$550
- c. Dr Salaries and Wages Payable \$550
 Cr Cash \$550
- d. No entry is required

EXERCISES

1. Match the statements below with the appropriate terms by entering the appropriate letter code in the spaces provided.

TERMS:

- A. Prepaid Expenses
- B. Unearned Revenues
- C. Accrued Revenues
- D. Accrued Expenses

STATEMENTS:

- ___ 1. A revenue not yet recognized; collected in advance.
- ___ 2. Office supplies on hand that will be used in the next period.
- ___ 3. Subscription revenue collected; not yet recognized.
- ___ 4. Rent not yet collected; already recognized.
- ___ 5. An expense incurred; not yet paid or recorded.
- ___ 6. A revenue recognized; not yet collected or recorded.
- ___ 7. An expense not yet incurred; paid in advance.
- ___ 8. Interest expense incurred; not yet paid.

Chapter 3 Solutions

Multiple Choice Solutions

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

Chapter 3 Solutions (Cont.)

Exercise Solutions

1. 1. **B** 2. **A** 3. **B** 4. **C** 5. **D** 6. **C** 7. **A** 8. **D**

2.

<i>Example: Bought supplies for \$500 on Jan. 1.</i>	Date	Debit	Credit
<i>Supplies</i>	Jan. 1	500	
<i>Cash</i>			500
a. Depreciation Expense	Dec. 31	1,340	
Accumulated Depreciation- Equipment			1,340
b. Interest Expense	Dec. 31	275	
Interest Payable			275
c. Supplies Expense	Dec. 31	450	
Supplies (\$550 - \$100)			450
d. Rent Expense	Dec. 31	700	
Prepaid Rent			700
e. Salaries and Wages Expense	Dec. 31	900	
Salaries and Wages Payable			900

Chapter 3 Solutions (Cont.)

Exercise Solutions (Cont.)

3.

<i>Example: Bought supplies for \$500 on Jan. 1.</i>	Date	Debit	Credit
<i>1.</i>			
Supplies	Jan. 1	500	
Cash			500
a. Interest Receivable	Dec. 31	30	
Interest Revenue			30
b. Unearned Service Revenue	Dec. 31	1,000	
Service Revenue			1,000
c. Rent Expense (\$45,000 ÷ 3 years)	Dec. 31	15,000	
Prepaid Rent			15,000
d. Accounts Receivable	Dec. 31	2,900	
Service Revenue			2,900
e. Depreciation Expense	Dec. 31	6,500	
Accumulated Depreciation—Equipment			6,500
f. Supplies Expense (\$850 – \$250)	Dec. 31	600	
Supplies			600
g. Salaries and Wages Expense	Dec. 31	960	
Salaries and Wages Payable			960