

**S 1-1**  
**(10 min.)**

- a. What forms of organization will enable the owners of Hudson Signs, Inc., to limit their risk of loss to the amounts they have invested in the business?
- b. What form of business organization will give Alley Hudson the most freedom to manage the business as she wishes?
- c. What form of organization will give creditors the maximum protection in the event that Hudson Signs, Inc., fails and cannot pay its debts?

***Solution:***

- a. Corporation, limited partners of a Limited-liability partnership (LLP) and Limited-liability company (LLC). If any of these businesses fails and cannot pay its liabilities, creditors cannot force the owners to pay the business's debts from the owners' personal assets. Creditors can go after the general partner of a limited liability partnership.
- b. Proprietorship. There is a single owner of the business, so the owner is answerable to no other owner.
- c. Partnership. If the partnership fails and cannot pay its liabilities, creditors can force the partners to pay the business's debts from their personal assets. A partnership affords more protection for creditors than a proprietorship because there are two or more owners to share this liability.

## FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-2**  
**(5 min.)**

1. Which accounting assumption governs this situation?
2. How can the proper application of this accounting assumption give Osmond and others a realistic view of Simple Treats, Inc.? Explain in detail.

***Solution:***

1. The entity assumption applies.
2. Application of the entity assumption will separate Osmond's personal assets from the assets of Simple Treats, Inc. This will help Osmond, investors, and lenders know how much assets, liabilities and equity the business has, and this knowledge will help all parties evaluate the business realistically.

## FINANCIAL ACCOUNTING - Twelfth Edition

S 1-3

(5-10 min.)

- a. Inflation has been about 2.5% for some time. Village Realtors is considering measuring its land values in inflation-adjusted amounts.
- b. You get an especially good buy on a laptop, paying only \$300 when it normally costs \$800. What is your accounting value for this laptop?
- c. Burger King, , the restaurant chain, sold a store location to McDonald's. How can Burger King determine the sale price of the store—by a professional appraisal, Burger King's original cost, or the amount actually received from the sale?
- d. General Motors wants to determine which division of the company—Chevrolet or Cadillac—is more profitable.

### ***Solution:***

- a. Stable-monetary-unit assumption
- b. Historical cost principle; \$300 is the accounting value of the laptop
- c. Historical cost principle; the sale price is the amount actually received from the sale
- d. Entity assumption

# FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-4**  
**(10 min.)**

Identify the missing amount for each of the following situations:

<b>Computed amounts in boxes</b>				
Total Assets	=	Total Liabilities	+	Stockholders' Equity
a. <input type="text" value="\$ 660,000"/>	=	\$ 300,000	+	\$ 360,000
b. \$ 85,000	=	\$ 50,000	+	<input type="text" value="\$ 35,000"/>
c. \$ 350,000	=	<input type="text" value="\$ 75,000"/>	+	\$ 275,000

## FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-5**  
**(5 min.)**

1. If you know the assets and the equity of a business, how can you measure its liabilities? Give the equation.
2. Use the accounting equation to show how to determine the amount of a company's stock-holders' equity. How would your answer change if you were analyzing your own household?

***Solution:***

1.  $\text{Liabilities} = \text{Assets} - \text{Owners' Equity}$
2.  $\text{Owners' Equity} = \text{Assets} - \text{Liabilities}$   
This way of determining the amount of owners' equity applies to any company or your household.

## FINANCIAL ACCOUNTING - Twelfth Edition

S 1-6

(5 - 10 min.)

Classify the following items as an asset (A), a liability (L), or stockholders' equity (S) for Target Corporation, a large retailer:

**Solution:**

a.	A
b.	L
c.	A
d.	A
e.	L
f.	L
g.	S
h.	A
i.	L
j.	A
k.	A
l.	S

## FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-7**

**(5-10 min.)**

1. How do the assets and stockholders' equity of Nike, Inc., differ from each other? Which one (assets or stockholders' equity) must be at least as large as the other? Which one can be smaller than the other?
2. How are Nike, Inc.'s, liabilities and stockholders' equity similar? Different?

***Solution:***

1. Assets are the economic resources of a business that are expected to produce a benefit in the future.  
Owners' (stockholders') equity represents the insider claims of a business, the owners' interest in its assets.  
Assets and owners' equity differ in that assets are resources and owners' equity is a claim to assets.  
Assets must be at least as large as owners' equity, so equity can be smaller than assets.
2. Both liabilities and owners' (stockholders') equity are claims to assets. Liabilities are the outsider claims to the assets of a business; they are obligations to pay creditors.  
Owners' equity represents the insider claims to the assets of the business; they are the owners' interest in its assets.

## FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-8**  
**(5 min.)**

1. Identify the two basic categories of items on an income statement.
2. What do we call the bottom line of the income statement?

***Solution:***

1. Revenues and expenses
2. Net income (or net loss)



## FINANCIAL ACCOUNTING - Twelfth Edition

### S 1-9 (10 min.)

Suppose you are analyzing the financial statements of Corley, Inc. Identify each item with its appropriate financial statement, using the following abbreviations: Income statement (I), Statement of retained earnings (R), Balance sheet (B), and Statement of cash flows (C). Three items appear on two financial statements, and one item shows up on three statements.

#### **Solution:**

a.	I
b.	R, C
c.	B
d.	I, R, C
e.	B
f.	B
g.	I
h.	B, C
i.	R, B
j.	B
k.	C
l.	C
m.	I
n.	C

**S 1-10**  
**(15-20 min.)**

- a. How can a business earn large profits but have a small balance of retained earnings?
- b. Give two reasons why a business can have a steady stream of net income over a five-year period and still experience a cash shortage.
- c. If you could pick a single source of cash for your business, what would it be? Why?
- d. How can a business be unprofitable several years in a row and still have plenty of cash?

***Solution:***

- a. Paying large dividends will cause retained earnings to be low.
- b. Heavy investing activity and paying off debts can result in a cash shortage even if net income has been high.
- c. The single best source of cash for a business is operating activities. This source of cash is best because it results from the core operations of the business. Operating activities should be the main source of cash for a business.
- d. a. Borrowing, issuing stock, and selling land, buildings, and equipment can bring in cash even when the company has experienced losses. Reducing accounts receivable and inventory can also increase cash flow.

**FINANCIAL ACCOUNTING - Twelfth Edition**

**S 1-11  
(5 min.)**

For each of the following questions, indicate which financial statement would most likely be used to provide the information. Use the following abbreviations: Income statement (I), Statement of retained earnings (R), Balance sheet (B), and Statement of cash flows (C).

***Solution:***

a.	I
b.	B
c.	C
d.	R
e.	B
f.	I
g.	R
h.	C
i.	B

**FINANCIAL ACCOUNTING - Twelfth Edition**

**S 1-12**  
**(5 min.)**

Prepare the company's income statement for the year ended December 31, 2018, complete with an appropriate heading.

**Solution:**

<b>MacKensie Services, Inc.</b>	
<b>Income Statement</b>	
<b>Year Ended December 31, 2018</b>	
	(millions)
Revenues	\$ 394
Expenses	\$ 171
Net income	\$ 223

S 1-13  
(5 min.)

What was the company's ending balance of retained earnings?

**Solution:**

<b>Journey Corp</b>	
<b>Statement of Retained Earnings</b>	
<b>Year Ended December 31, 2018</b>	
	(millions)
Retained earnings, December 31, 2017	\$ 270
Add: Net income (\$460 – \$380)	80
Less: Dividends declared	(64)
Retained earnings, December 31, 2018	<u>\$ 286</u>

## FINANCIAL ACCOUNTING - Twelfth Edition

### S 1-14 (10 - 15 min.)

Prepare Jackson Corporation's balance sheet at December 31, 2018, complete with its proper heading.

#### **Solution:**

<b>Jackson Corporation</b>	
<b>Balance Sheet</b>	
<b>December 31, 2018</b>	
ASSETS	(in millions)
Current assets:	
Cash	\$ 52
Accounts receivable	23
Total current assets	75
Long-term assets	45
Total assets	\$ 120
LIABILITIES	
Current liabilities:	
Accounts payable	\$ 21
Total current liabilities	21
Long-term liabilities:	
Long-term notes payable	31
Total liabilities	52
STOCKHOLDERS' EQUITY	
Common stock	28
Retained earnings	40
Total stockholders' equity	68
Total liabilities and stockholders' equity	\$ 120

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**S 1-15**  
**(10 - 15 min.)**

Solve for the company's ending retained earnings and then prepare Sullivan Corporation's balance sheet at September 30, 2018. Use a proper heading on the balance sheet.

**Solution:**

<b>Sullivan Corporation</b>	
<b>Balance Sheet</b>	
<b>September 30, 2018</b>	
<b>ASSETS</b>	(in millions)
Current assets:	
Cash	\$ 78
Accounts receivable	27
Total current assets	105
Property and equipment	27
Other long-term assets	21
Total assets	<u>\$ 153</u>
<b>LIABILITIES</b>	
Current liabilities	
Accounts payable	\$ 34
Total current liabilities	34
Long-term liabilities:	
Long-term notes payable	17
Total liabilities	<u>51</u>
<b>STOCKHOLDERS' EQUITY</b>	
Common stock	31
Retained earnings	71
Total stockholders' equity	<u>102</u>
Total liabilities and stockholders' equity	<u>\$ 153</u>

Computation of retained earnings: Total assets (\$153) – total liabilities (\$51) – common stock (\$31) = \$71  
 Or, total stockholders' equity (\$102) – common stock (\$31) = \$71

**FINANCIAL ACCOUNTING - Twelfth Edition**

**S 1-16**  
**(10-15 min.)**

Prepare Python's statement of cash flows for the year ended December 31, 2018, complete with its proper heading.

**Solution:**

<b>Python Legal Services, Inc.</b>		
<b>Statement of Cash Flows</b>		
<b>Year Ended December 31, 2018</b>		
Cash flows from operating activities:		
Net income		\$ 115,000
Adjustments to reconcile net income to net cash provided by operating activities		<u>(9,000)</u>
Net cash provided by operating activities		106,000
Cash flows from investing activities:		
Purchases of equipment	<u>\$ (20,000)</u>	
Net cash used for investing activities		(20,000)
Cash flows from financing activities:		
Payment of dividends	<u>\$ (15,000)</u>	
Net cash used for financing activities		<u>(15,000)</u>
Net increase in cash		71,000
Cash balance, December 31, 2017		<u>16,000</u>
Cash balance, December 31, 2018		<u>\$ 87,000</u>



## FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-17**  
**(10 - 15 min.)**

Complete the financial statements. All amounts are in millions.

***Solution:***

Solve in this order:

a.	\$	82
b.	\$	82
c.	\$	149
f.	\$	149
g.	\$	182
h.	\$	230
e.	\$	230
d.	\$	112

**S 1-18**  
**(5 min.)**

How should ethics be incorporated into making accounting judgments? Why is ethics important?

***Solution:***

Ethics is a factor that should be included in every business and accounting decision, beyond the potential economic and legal consequences. Ideally, for each decision, honesty and truthfulness should prevail, considering the rights of others. The decision guidelines at the end of the chapter spell out the considerations we should take when making decisions. Simply, we might ask ourselves three questions: (1) Is the action legal? (2) Who will be affected by the decision? (3) How will the decision make me feel afterward?

## FINANCIAL ACCOUNTING - Twelfth Edition

**S 1-19**  
**(10-15 min.)**

Match the following definitions with one of the terms listed here.

***Solution:***

Asset	m
Balance sheet	l
Bookkeeping	k
Corporation	f
Equity	r
Ethical duties	d
Expenses	h
Financial accounting	b
Historical cost principle	j
Income statement	o
Investors and creditors	n
Liability	g
Managerial accounting	c
Net income	a
Partnership	q
Proprietorship	i
Revenues	e
Statement of cash flows	p

## FINANCIAL ACCOUNTING - Twelfth Edition

E 1-20A

(10-15 min.)

Which company appears to have the strongest financial position? Explain your reasoning.

**Solution:**

	Assets	=	Liabilities	+	Stockholders' Equity
Synthe Real Estate	\$73		\$41		\$32
Odessa Florals	\$26		\$11		\$15
Hometown Bank	\$29		\$14		\$15

Odessa Florals appears to have the strongest financial position because its liabilities make up the smallest percentage of company assets ( $\$11/\$26 = .42$ ). Stated differently, Odessa Florals' equity is the highest percentage of company assets ( $\$15/\$26 = .58$ ).

Liabilities as a percent of total assets:

Smythe Real Estate:  $\$41/\$73 = 0.56$

Odessa Florals:  $\$11/\$26 = 0.42$

Hometown Bank:  $\$14/\$29 = 0.48$

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-21A**  
**(10-15 min.)**

1. Use these data to write Willow's accounting equation.
2. How much in resources does Willow have to work with?
3. How much does Willow owe creditors?
4. How much of the company's assets do the Willow stockholders actually own?

**Solution:**

**Req. 1**

<i>(Amounts in millions)</i>					
	Assets	=	Liabilities	+	Stockholders' Equity
	\$220		\$160		
	320		380		
	130				
<b>Total</b>	\$670	=	\$540	+	\$130

**Req. 2**

Resources to work with \$670

**Req. 3**

Amount owed to creditors \$540

**Req. 4**

Actually owned by company stockholders \$130

## FINANCIAL ACCOUNTING - Twelfth Edition

E 1-22A

(10-20 min.)

1. Collinswood issued \$11 million of stock and declared no dividends.
2. Collinswood issued no stock but declared dividends of \$20 million.
3. Collinswood issued \$15 million of stock and declared dividends of \$75 million.

**Solution:**

	Situation		
	1	2	3
	<i>(Millions)</i>		
Total stockholders' equity, January 31, 2018 (\$47 - \$19)	\$ 28	\$ 28	\$ 28
Add: Issuances of stock	11	0	15
Net income	13*	44*	84*
Less: Dividends declared	0	(20)	(75)
Net loss	0	0	0
Total stockholders' equity, January 31, 2019 (\$77 - \$25)	\$ 52	\$ 52	\$ 52

\*Must solve net income

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-23A**  
**(10-15 min.)**

Identify the financial statement where these decision makers can find the following information about Butler Tech, Inc. In some cases, more than one statement will report the needed data.

**Solution:**

a.	Income statement
b.	Balance sheet
c.	Balance sheet
d.	Balance sheet
e.	Statement of retained earnings, Statement of cash flows
f.	Balance sheet, Statement of cash flows
g.	Statement of cash flows
h.	Statement of cash flows
i.	Income statement
j.	Balance sheet, Statement of retained earnings
k.	Income statement
l.	Balance sheet
m.	Income statement, Statement of retained earnings, Statement of cash flows
n.	Balance sheet

E 1-24A  
(10-20 min.)

Prepare Landy's balance sheet at December 31, 2018, complete with its proper heading. Use the accounting equation to compute retained earnings.

**Solution:**

<b>Landy Products Balance Sheet December 31, 2018</b>			
<b>ASSETS</b>		<b>LIABILITIES</b>	
Current assets:		Current liabilities:	
Cash	\$ 24,000	Accounts payable	<u>\$ 22,000</u>
Receivables	18,000	Total current liabilities	22,000
Inventory	<u>80,000</u>	Long-term liabilities:	
Total current assets	122,000	Long-term notes payable	<u>172,000</u>
Equipment	<u>182,000</u>	Total liabilities	194,000
Total assets	<u>\$ 304,000</u>		
		STOCKHOLDERS' EQUITY	
		Common stock	34,500
		Retained earnings	<u>75,500</u>
		Total stockholders' equity	<u>110,000</u>
		Total liabilities and stockholders' equity	304,000

Computation of retained earnings: Total assets (\$304,000) – current liabilities (\$22,000) – long-term notes payable (\$172,000) – common stock (\$34,500) = \$75,500
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**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-25A**  
**(10-20 min.)**

Construct the balance sheet of Jill Carlson Realty Company at January 31, 2018. Use the accounting equation to compute ending retained earnings.

**Solution:**

<b>Jill Carlson Realty Company</b>			
<b>Balance Sheet</b>			
<b>January 31, 2018</b>			
<b>ASSETS</b>		<b>LIABILITIES</b>	
Cash	\$ 57.2	Current liabilities	\$ 2.9
Receivables	0.5	Long-term liabilities	<u>102.6</u>
Investment assets (long-term)	79.4	Total liabilities	105.5
Property and equipment, net	1.6	STOCKHOLDERS'	
Other assets (long-term)	<u>9.3</u>	EQUITY	
Total assets	\$ 148.0	Common stock	39.2
		Retained earnings	<u>3.3</u>
		Total stockholders' equity	<u>42.5</u>
		Total liabilities and stockholders' equity	<u>\$ 148.0</u>

Computation of retained earnings: Total assets (\$148.0) – Total liabilities (\$105.5) – Common stock (\$39.2) = \$3.3
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**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-26A**  
**(15-25 min.)**

1. Prepare the income statement of Jill Carlson Realty Company for the year ended January 31, 2018.
2. What amount of dividends did Jill Carlson declare during the year ended January 31, 2018?

**Solution:**

**Req. 1**

<b>Jill Carlson Realty Company Income Statement Year Ended January 31, 2018</b>		
(Amounts in millions)		
Total revenue		\$ 25.7
Expenses:		
Salary and other employee expenses	\$ 13.7	
Other expenses	7.6	
Interest expense	<u>1.5</u>	
Total expenses		<u>\$ 22.8</u>
Net income		<u>\$ 2.9</u>

**Req. 2**

The statement of retained earnings helps to compute dividends, as follows:

<b>Jill Carlson Realty Company Statement of Retained Earnings Year Ended January 31, 2018</b>	
Retained earnings, beginning of year	\$ 2.6
Add: Net income for the year (Req. 1)	<u>2.9</u>
Subtotal	5.5
Less: Dividends declared*	<u>2.2</u>
Retained earnings, end of year (from Exercise 1-25A)	<u>\$ 3.3</u>
*(\$5.5 - \$3.3 = \$2.2)	

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-27A**  
**(15-20 min.)**

1. Prepare the income statement and the statement of retained earnings of Giada Coffee Roasters Corp., for the month ended August 31, 2019.

**Solution:**

<b>Giada Roasters Corp.</b> <b>Income Statement</b> <b>For the Month Ended August 31, 2019</b>		
Revenue:		
Service revenue		\$ 278,700
Expenses:		
Salary expense	\$ 78,500	
Utilities expense	5,100	
Rent expense	<u>1,800</u>	
Total expenses		<u>85,400</u>
Net income		<u>\$ 193,300</u>

<b>Giada Coffee Roasters Corp.</b> <b>Statement of Retained Earnings</b> <b>For the Month Ended August 31, 2019</b>	
Retained earnings, August 1, 2019	\$ -
Add: Net income for the month	<u>193,300</u>
Subtotal	193,300
Less: Dividends declared	<u>(2,800)</u>
Retained earnings, August 31, 2019	<u>\$ 190,500</u>

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-28A**  
**(15-20 min.)**

1. Prepare the balance sheet of Giada Coffee Roasters Corp., for August 31, 2019.

**Solution:**

<b>Giada Coffee Roasters Corp.</b>			
<b>Balance Sheet</b>			
<b>31-Aug-19</b>			
<b>Assets</b>		<b>Liabilities</b>	
Cash	\$ 5,300	Accounts payable	\$ 8,800
Office supplies	7,400		
Equipment	<u>201,500</u>	<b>Stockholders' Equity</b>	
Total assets	\$ 214,200	Common stock	14,900
		Retained earnings	<u>190,500</u>
		Total stockholders' equity	<u>205,400</u>
		Total liabilities and stockholders' equity	<u>\$ 214,200</u>

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-29A  
(15-20 min.)**

1. Prepare the statement of cash flows of Giada Coffee Roasters Corp., for the month ended August 31, 2019. Using Exhibit 1-11 as a model, show with arrows the relationships among the income statement, statement of retained earnings, balance sheet, and statement of cash flows.

**Solution:**

<b>Giada Coffee Roasters Corp.</b> <b>Statement of Cash Flows</b> <b>For the Month Ended August 31, 2019</b>		
Cash flows from operating activities:		
Net income		\$ 193,300
Adjustments to reconcile net income to net cash provided by operating activities		1,400
Net cash provided by operating activities		194,700
Cash flows from investing activities:		
Acquisition of equipment	\$ (201,500)	
Net cash used for investing activities		(201,500)
Cash flows from financing activities:		
Issuance (sale) of stock to owners	\$ 14,900	
Payment of dividends	(2,800)	
Net cash provided by financing activities		12,100
Net increase in cash		\$ 5,300
Cash balance, August 1, 2019		0
Cash balance, August 31, 2019		\$ 5,300

## FINANCIAL ACCOUNTING - Twelfth Edition

### E 1-30A (10-15 min.)

Complete the report giving him your opinion of net income, dividends, financial position, and cash flows during his first month of operations.

#### **Solution:**

TO: Owner of Giada Coffee Roasters Corp.

FROM: Student Name

SUBJECT: Opinion of net income, dividends, financial position, and cash flows

Your first month of operations was successful. Revenues totaled \$278,700 and net income was \$193,300. These operating results look very strong.

The company was able to pay a \$2,800 dividend, and this should make you happy with so quick a return on your investment. Your financial position looks secure, with assets of \$214,200 and liabilities of only \$8,800. Your stockholders' equity is \$205,400.

Operating activities generated cash of \$194,700, which is respectable. Operating activities are the main source of cash, which is expected for a thriving company. You ended the month with cash of \$5,300. Based on the above facts, I believe you should stay in business.

E 1-31A  
(20-25 min.)

Prepare the following financial statements (with proper headings) for 2018: 1) Income statement, 2) Statement of retained earnings, 3) Balance sheet.

Solution:

Req. 1

Edwin Company Income Statement For the Year Ended December 31, 2018		
Revenue:		<i>(millions)</i>
Revenues		\$ 150
Expenses:		
Salary expense	\$ 34	
Rent expense	23	
Utilities expense	16	
Total expenses		73
Net income		\$ 77

Req. 2

Edwin Company Statement of Retained Earnings Year Ended December 31, 2018	
Retained earnings, December 31, 2017	<i>(millions)</i> 73
Add: Net income (\$150 - \$73)	77
Less: Dividends declared	(16)
Retained earnings, December 31, 2018	\$ 134

Req. 3

Edwin Company Balance Sheet December 31, 2018			
ASSETS		LIABILITIES	
Current assets:		Current liabilities:	
Cash	\$ 185	Accounts payable	\$ 56
Accounts receivable	70	Total current liabilities	56
Total current assets	255	Long-term liabilities	
Property and equipment	35	Long-term notes payable	26
Other long-term assets	22	Total liabilities	82
Total assets	\$ 312		
		STOCKHOLDERS' EQUITY	
		Common stock*	96
		Retained earnings	134
		Total stockholders' equity	230
		Total liabilities and stockholders' equity	\$ 312

\*Common stock = Total stockholders' equity (\$230) – Retained earnings (\$134) = \$96

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-32B**

**(10-15 min.)**

Which company appears to have the strongest financial position? Explain your reasoning.

**Solution:**

	Assets	=	Liabilities	+	Stockholders' Equity
Water Street Bank	\$78		\$43		\$35
Pufferbelly Restaurant	\$30		\$7		\$23
Blake Gift Shop	\$34		\$7		\$27

Blake Gift Shop appears to have the strongest financial position because its liabilities make up the smallest percentage of company assets ( $\$7/\$34 = .21$ ). Stated differently, Blake Gift Shop's equity is the highest percentage of company assets ( $\$27/\$34 = .79$ ).

Liabilities as a percent of total assets:

Waterstreet Bank:  $\$43/\$78 = 0.55$

Pufferbelly Restaurant:  $\$7/\$30 = 0.23$

Blake Gift Shop:  $\$7/\$34 = 0.21$



**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-33B**  
**(10-15 min.)**

1. Use these data to write Brandeberry's accounting equation.
2. How much in resources does Brandeberry have to work with?
3. How much does Brandeberry owe creditors?
4. How much of the company's assets do the Brandeberry stockholders actually own?

**Solution:**

**Req. 1**

<i>(Amounts in millions)</i>					
	Assets	=	Liabilities	+	Stockholders' Equity
	\$240		\$100		
	390		360		
	130				
<b>Total</b>	\$760	=	\$460	+	\$300

**Req. 2**

Resources to work with \$760

**Req. 3**

Amount owed to creditors \$460

**Req. 4**

Actually owned by company stockholders \$300

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-34B  
(10-20 min.)**

1. Pillser issued \$3 million of stock and declared no dividends.
2. Pillser issued no stock but declared dividends of \$4 million.
3. Pillser issued \$20 million of stock and declared dividends of \$8 million.

**Solution:**

	Situation		
	1	2	3
	<i>(Millions)</i>		
Total stockholders' equity, January 31, 2018 (\$49 - \$17)	\$32	\$32	\$32
Add: Issuances of stock	3	0	20
Net income	14	21	5
Less: Dividends declared	0	(4)	(8)
Net loss	0	0	0
Total stockholders' equity, January 31, 2019 (\$72 - \$23)	\$49	\$49	\$49

\*must solve for net income

## FINANCIAL ACCOUNTING - Twelfth Edition

### E 1-35B (10-15 min.)

Identify the financial statement where these decision makers can find the following information about Flurry, Inc. In some cases, more than one statement will report the needed data.

#### **Solution:**

a.	Balance sheet, Statement of cash flows
b.	Statement of cash flows
c.	Balance sheet
d.	Balance sheet
e.	Income statement, Statement of retained earnings, Statement of cash flows
f.	Income statement
g.	Balance sheet
h.	Income statement
i.	Balance sheet
j.	Statement of cash flows
k.	Income statement
l.	Balance sheet
m.	Statement of retained earnings, Statement of cash flows
n.	Balance sheet, Statement of retained earnings

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-36B**  
**(10-20 min.)**

Prepare Patterson's balance sheet at December 31, 2018, complete with its proper heading. Use the accounting equation to compute retained earnings.

**Solution:**

<b>Patterson Products Balance Sheet December 31, 2018</b>			
<b>ASSETS</b>		<b>LIABILITIES</b>	
Current assets:		Current liabilities:	
Cash	\$ 20,000	Accounts payable	<u>\$ 22,000</u>
Receivables	17,600	Total current liabilities	22,000
Inventory	<u>78,000</u>	Long-term liabilities:	
Total current assets	115,600	Long-term notes payable	<u>173,000</u>
Equipment	186,000	Total liabilities	195,000
Total assets	\$ 301,600		
		STOCKHOLDERS' EQUITY	
		Common stock	28,500
		Retained earnings	<u>78,100</u>
		Total stockholders' equity	106,600
		Total liabilities and stockholders' equity	<u>\$ 301,600</u>

Computation of retained earnings: Total assets (\$301,600) – current liabilities (\$22,000) – long-term notes payable (\$173,000) – common stock (\$28,500) = \$78,100
--

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-37B**  
**(10-20 min.)**

Construct the balance sheet of Mary Burke Realty Company at March 31, 2018. Use the accounting equation to compute ending retained earnings.

**Solution:**

<b>Mary Burke Realty Company</b>			
<b>Balance Sheet</b>			
<b>March 31, 2018</b>			
<b>ASSETS</b>		<b>LIABILITIES</b>	
Cash	\$ 1.6	Current Liabilities	\$ 2.7
Receivables	0.1	Long-term liabilities	102.3
Investment assets	135.1	Total liabilities	105.0
Property and equipment, net	1.4	STOCKHOLDERS'	
Other assets	<u>10.3</u>	EQUITY	
Total assets	<u>\$ 148.5</u>	Common stock	27.9
		Retained earnings	<u>15.6</u>
		Total stockholders' equity	<u>43.5</u>
		Total liabilities and stockholders' equity	<u>\$ 148.5</u>

Computation of retained earnings: Total assets (\$148.5) – Total liabilities (\$105.0) – Common stock (\$27.9) = \$15.6
--

**FINANCIAL ACCOUNTING - Twelfth Edition**

**E 1-38B**  
**(15-25 min.)**

1. Prepare the income statement of Mary Burke Realty Company for the year ended March 31, 2018.
2. What amount of dividends did Mary Burke Realty Company declare during the year ended March 31, 2018?

**Solution:**

**Req. 1**

<b>Mary Burke Realty Company Income Statement Year Ended March 31, 2018</b>		
<i>(Amounts in millions)</i>		
Total revenue		\$ 40.4
Expenses:		
Salary and other employee expenses	\$ 15.2	
Other expenses	6.6	
Interest expense	<u>0.4</u>	
Total expenses		<u>22</u>
Net income		<u>\$ 18.2</u>

**Req. 2**

The statement of retained earnings helps to compute dividends, as follows:

<b>Mary Burke Realty Company Statement of Retained Earnings Year Ended March 31, 2018</b>	
<i>(Amounts in millions)</i>	
Retained earnings, beginning of year	\$ 17.2
Add: Net income for the year (Req. 1)	18.2
Subtotal	<u>35.4</u>
Less: Dividends declared*	19.8
Retained earnings, end of year (from Exercise 1-37B)	<u>\$ 15.6</u>

\*(\$35.4 – \$15.6 = \$19.8)

**E 1-39B**  
**(15-20 min.)**

1. Prepare the income statement and the statement of retained earnings of Island Coffee Roasters Corporation for the month ended August 31, 2019.

**Solution:**

<b>Island Coffee Roasters Corporation</b> <b>Income Statement</b> <b>For the Month Ended August 31, 2019</b>		
Revenue:		
Service revenue		\$ 279,300
Expenses:		
Salary expense	\$ 78,100	
Utilities expense	5,800	
Rent expense	<u>1,800</u>	
Total expenses		<u>85,700</u>
Net income		<u>\$ 193,600</u>

<b>Island Coffee Roasters Corporation</b> <b>Statement of Retained Earnings</b> <b>For the Month Ended August 31, 2019</b>	
Retained earnings, August 1, 2019	\$ -
Add: Net income	<u>193,600</u>
Subtotal	193,600
Less: Dividends declared	<u>(2,700)</u>
Retained earnings, August 31, 2019	<u>\$ 190,900</u>

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**E 1-40B**  
**(15-20 min.)**

1. Prepare the balance sheet of Island Coffee Roasters Corporation for August 31, 2019.

**Solution:**

<b>Island Coffee Roasters Corporation</b>			
<b>Balance Sheet</b>			
<b>August 31, 2019</b>			
<b>Assets</b>		<b>Liabilities</b>	
Cash	\$ 6,000	Accounts payable	\$ 8,900
Office supplies	7,500		
Equipment	<u>200,000</u>	<b>Stockholders' Equity</b>	
Total assets	\$ 213,500	Common stock	13,700
		Retained earnings	<u>190,900</u>
		Total stockholders' equity	<u>204,600</u>
		Total liabilities and stockholders'	<u>\$ 213,500</u>



**E 1-41B**  
**(15-20 min.)**

1. Prepare the statement of cash flows of Island Coffee Roasters Corporation for the month ended August 31, 2019. Using Exhibit 1-11 as a model, show with arrows the relationships among the income statement, statement of retained earnings, balance sheet, and statement of cash flows.

**Solution:**

<b>Island Coffee Roasters Corporation</b> <b>Statement of Cash Flows</b> <b>For the Month Ended August 31, 2019</b>		
Cash flows from operating activities:		
Net income		\$ 193,600
Adjustments to reconcile net income to net cash provided by operations		1,400
Net cash provided by operating activities		195,000
Cash flows from investing activities:		
Acquisition of equipment	\$ (200,000)	
Net cash used for investing activities		(200,000)
Cash flows from financing activities:		
Issuance (sale) of stock to owners	\$ 13,700	
Payment of dividends	(2,700)	
Net cash provided by financing activities		11,000
Net increase in cash		\$ 6,000
Cash balance, August 1, 2019		0
Cash balance, August 31, 2019		\$ 6,000

## FINANCIAL ACCOUNTING - Twelfth Edition

E 1-42B

(10-20 min.)

Complete the report giving her your opinion of net income, dividends, financial position, and cash flows during her first month of operations.

**Solution:**

TO: Owner of Island Coffee Roasters Corporation

FROM: Student Name

SUBJECT: Opinion of net income, dividends, financial position, and cash flows

Your first month of operations was successful. Revenues totaled \$279,300 and net income was \$193,600. These operating results look very strong.

The company was able to pay a \$2,700 dividend, and this should make you happy with so quick a return on your investment. Your financial position looks secure, with assets of \$213,500 and liabilities of only \$8,900. Your stockholders' equity is \$204,600.

Operating activities generated cash of \$195,000, which is respectable. Operating activities are the main source of cash, which is expected for a thriving company. You ended the month with cash of \$6,000. Based on the above facts, I believe you should stay in business.

E 1-43B  
(20-25 min.)

Prepare the following financial statements (with proper headings) for 2018: 1) Income statement, 2) Statement of retained earnings, 3) Balance sheet.

**Solution:**

**Req. 1**

<b>Brewster Company Income Statement For the Year Ended December 31, 2018</b>		
Revenue:		<i>(millions)</i>
Revenues		\$ 146
Expenses:		
Salary expense	\$ 28	
Rent expense	23	
Utilities expense	19	
Total expenses		70
Net income		<u>\$ 76</u>

**Req. 2**

<b>Brewster Company Statement of Retained Earnings Year Ended December 31, 2018</b>	
	<i>(millions)</i>
Retained earnings, December 31, 2017	\$ 76
Add: Net income (\$146 - \$70)	76
Less: Dividends declared	(15)
Retained earnings, December 31, 2018	<u>\$ 137</u>

**Req. 3**

<b>Brewster Company Balance Sheet December 31, 2018</b>			
ASSETS		LIABILITIES	
Current assets:		Current liabilities:	
Cash	\$ 175	Accounts payable	56
Accounts receivable	85	Total current liabilities	56
Total current assets	260	Long-term liabilities:	
Property and equipment	39	Long-term notes payable	33
Other long-term assets	25	Total liabilities	89
Total assets	<u>\$ 324</u>		
		STOCKHOLDERS' EQUITY	
		Common stock*	98
		Retained earnings	137
		Total stockholders' equity	235
		Total liabilities and stockholders' equity	<u>\$ 324</u>

Common stock = Total stockholders' equity (\$235) – Retained earnings (\$137) = \$98
--



**FINANCIAL ACCOUNTING - Twelfth Edition**

**P 1-62A**  
**(30 min.)**

- 1) Compute the missing amount (?) for each company—amounts in millions.
- 2) At the end of the year, which company has the highest net income? Highest percent of net income to revenues?

**Solution:**

**Req. 1**

	<b>Kennedy Corp.</b>	<b>Caring Co.</b>	<b>Childress, Inc.</b>
<b>BALANCE SHEET</b>			
Beginning:			
Assets	\$ 76	\$ 30	\$ 17
Liabilities	51	21	1
Common stock	7	7	6
Retained earnings	18	2	10
Ending:			
Assets	\$ 86	\$ 48	\$ 20
Liabilities	53	32	0
Common stock	7	12	8
Retained earnings	26	4	12
<b>INCOME STATEMENT</b>			
Revenues	\$ 227	\$ 165	\$ 22
Expenses	218	157	18
Net income	9	8	4
<b>STATEMENT OF RETAINED EARNINGS</b>			
Beginning RE	\$ 18	\$ 2	\$ 10
+ Net income	9	8	4
- Dividends declared	(1)	(6)	(2)
= Ending RE	\$ 26	\$ 4	\$ 12

**Req. 2**

	<b>Kennedy Corp.</b>	<b>Caring Co.</b>	<b>Childress, Inc.</b>
Net income	\$9 <i>Highest</i>	(Millions) \$8	\$4
% of net income to revenues	$\frac{\$9}{\$227} = 4\%$	$\frac{\$8}{\$165} = 4.8\%$	$\frac{\$4}{\$22} = 18.2\%$ <i>Highest</i>

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**P 1-63A**  
**(20-25 min.)**

1. Prepare the correct balance sheet and date it properly. Compute total assets, total liabilities, and stockholders' equity.
2. Is City News actually in better (or worse) financial position than the erroneous balance sheet reports? Give the reason for your answer.
3. Identify the accounts listed on the incorrect balance sheet that should not be reported on the balance sheet. State why you excluded them from the correct balance sheet you prepared for Requirement 1. On which financial statement should these accounts appear?

**Solution:**

**Req. 1**

<b>City News, Inc.</b>			
<b>Balance Sheet</b>			
<b>May 31, 2018</b>			
<b>Assets</b>		<b>Liabilities</b>	
Cash	\$ 10,000	Accounts payable	\$ 6,500
Accounts receivable	2,600	Note payable	50,000
Notes receivable	15,800	Total liabilities	56,500
Office supplies	700	<b>Stockholders' equity</b>	
Land	81,000	Stockholders' equity*	89,200
Equipment	35,600	Total liabilities and stockholders' equity	\$ 145,700
Total assets	<u>\$ 145,700</u>		

\*Total assets (\$145,700) – Total liabilities (\$56,500) = Stockholders' equity (\$89,200).

**Req. 2**

City News, Inc. is in better (not worse) financial position than the erroneous balance sheet reports. Total assets (\$145,700) are \$7,800 higher than originally reported (\$137,900), liabilities are \$14,700 lower than originally reported, and stockholders' equity is \$22,500 higher than reported originally.

**Req. 3**

The following accounts are not reported on the balance sheet because they are expenses. These accounts are reported on the income statement.

- Utilities expense
- Advertising expense
- Salary expense
- Interest expense

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**P 1-64A**  
**(20-25 min.)**

1. Prepare the balance sheet of the real estate business of Brandon Hilton Realtor, Inc., at June 30, 2019.
2. Does it appear that the realty business can pay its debts? How can you tell?
3. Identify the personal items given in the preceding facts that should not be reported on the balance sheet of the business.

**Solution:**

**Req. 1**

<b>Brandon Hilton Realtor, Inc.</b>			
<b>Balance Sheet</b>			
<b>June 30, 2019</b>			
<b>Assets</b>		<b>Liabilities</b>	
Cash	\$ 55,000	Accounts payable	\$ 16,000
Office supplies	8,000	Note payable	112,000
Land	165,000	Total liabilities	128,000
Furniture	30,000	<b>Stockholders' equity</b>	
Franchise	20,000	Common stock	65,000
		Retained earnings	85,000
		Total stockholders' equity	150,000
Total assets	<u>\$ 278,000</u>	Total liabilities and stockholders' equity	<u>\$ 278,000</u>

\*Total assets (\$278,000) – Total liabilities (\$128,000) – Common stock (\$65,000) = Retained earnings (\$85,000).

**Req. 2**

It appears that the business can pay its debts. Total assets exceed total liabilities.

**Req. 3**

Personal items not reported on the balance sheet of the business:  
 a. Personal cash (\$15,000)  
 b. Personal account payable (\$3,400)  
 g. Personal residence (\$334,000) and mortgage payable (\$182,000)

**P 1-65A**  
**(30-45 min.)**

1. Prepare the income statement of Oak Hill Garden Supply, Inc., for the year ended December 31, 2018.
2. Prepare the company's statement of retained earnings for the year.
3. Prepare the company's balance sheet at December 31, 2018.
4. Analyze Oak Hill Garden Supply, Inc., by answering these questions:
  - a. Was Oak Hill Garden Supply profitable during 2018? By how much?
  - b. Did retained earnings increase or decrease? By how much?
  - c. Which is greater, total liabilities or total stockholders' equity? Who has a greater claim to Oak Hill's assets: its creditors or its stockholders?

**Solution:**

**Req. 1**

Oak Hill Garden Supply, Inc. Income Statement Year Ended December 31, 2018		
Revenue		
Service revenue		\$ 452,600
Expenses		
Salary expense	\$ 108,400	
Rent expense	41,200	
Interest expense	10,300	
Utilities expense	8,800	
Property tax expense	7,400	
Total expenses		176,100
Net income		\$ 276,500

**Req. 2**

Oak Hill Garden Supply, Inc. Statement of Retained Earnings Year Ended December 31, 2018	
Retained earnings, December 31, 2017	\$ 364,600
Add: Net income	276,500
Subtotal	641,100
Less: Dividends declared	(107,000)
Retained earnings, December 31, 2018	\$ 534,100

**Req. 3**

Oak Hill Garden Supply, Inc. Balance Sheet December 31, 2018			
ASSETS		LIABILITIES	
Cash	\$ 44,000	Accounts payable	\$ 26,000
Accounts receivable	84,900	Interest payable	2,700
Supplies	6,300	Note payable	99,600
Land	25,000	Total liabilities	128,300
Building	406,000		
Equipment	110,000		
		STOCKHOLDERS' EQUITY	
		Common stock	13,800
		Retained earnings	534,100
		Total stockholders' equity	547,900
Total assets	\$ 676,200	Total liabilities and stockholders' equity	\$ 676,200

**Req. 4**

- a. Oak Hill Garden Supply was profitable; net income was \$276,500.
  - b. Retained earnings increased by \$169,500 — from \$364,600 to \$534,100.
  - c. Stockholders' equity (\$547,900) exceeds liabilities (\$128,300).
- The stockholders have a greater claim against Oak Hill Garden Supply's assets than do the company's creditors.



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**P 1-66A**  
**(20 min.)**

1. Prepare Mitchell Company's cash flow statement for the year ended March 31, 2019. Not all items listed will appear on the cash flow statement.
2. What activities provided the largest source of cash? Is this a sign of financial strength or weakness?

**Solution:**

**Req. 1**

<b>Mitchell Company</b>		
<b>Statement of Cash Flows</b>		
<b>Year Ended March 31, 2019</b>		
	<i>Millions</i>	
<b>Cash flows from operating activities:</b>		
Net income		\$ 3,020
Adjustments to reconcile net income to net cash provided by operating activities		<u>2,420</u>
Net cash provided by operating activities		5,440
<b>Cash flows from investing activities:</b>		
Purchases of property, plant, and equipment	\$ (2,640)	
Sales of property, plant, and equipment	25	
Other investing cash payments	<u>(195)</u>	
Net cash used for investing activities		(2,810)
<b>Cash flows from financing activities:</b>		
Issuance of common stock	\$ 190	
Payment of dividends	<u>(265)</u>	
Net cash used for financing activities		<u>(75)</u>
Net increase in cash		\$ 2,555
Cash, beginning		<u>220</u>
Cash, ending		<u>\$ 2,775</u>

**Req. 2**

Operating activities provided the largest amount of cash. This signals financial strength because operations should be the main source of cash.

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**P 1-67A**  
**(40-50 min.)**

1. Complete Calabasa Corporation's financial statements by determining the missing amounts denoted by the letters. If necessary, round numbers up to the nearest whole dollar.

**Solution:**

<b>INCOME STATEMENT</b>		<b>2019</b>	<b>2018</b>	
Revenues	13,920	= \$ k	\$ 14,750	
Cost of goods sold		(11,100)	a	= (11,680)
Other expenses		(1,300)	(1,200)	
Income before income taxes		1,520	1,870	
Income taxes (35% tax rate)	532	= l	(655)	
Net income	988	= \$ m	\$ b	= 1,215
<b>STATEMENT OF RETAINED EARNINGS</b>				
Beginning balance	3,825	= \$ n	\$ 2,680	
Net income	988	= o	c	= 1,215
Dividends declared		(92)	(70)	
Ending balance	4,721	= \$ p	\$ d	= 3,825
<b>BALANCE SHEET</b>				
Assets:				
Cash	1,020	= \$ q	\$ e	= 1,180
Property, plant and equipment		1,547	1,316	
Other assets	11,959	= r	11,104	
Total assets	14,526	= \$ s	13,600	
Liabilities:				
Current liabilities	4,815	= \$ t	5,660	
Long-term debt		4,350	3,370	
Other liabilities		35	180	
Total liabilities		9,200	f	= 9,210
<b>Stockholders' Equity:</b>				
Common stock		425	425	
Retained earnings	4,721	= u	g	= 3,825
Other stockholders' equity		180	140	
Total stockholders' equity	5,326	= v	4,390	
Total liabilities and stockholders' equity				
stockholders' equity	14,526	= \$ w	\$ h	= 13,600
<b>STATEMENT OF CASH FLOWS</b>				
Net cash provided by operating activities	630	= \$ x	875	
Net cash used for investing activities		(270)	(425)	
Net cash used for financing activities		(520)	(520)	
Increase (decrease) in cash		(160)	i	= (70)
Cash at beginning of year	1,180	= y	1,250	
Cash at end of year	1,020	= \$ z	\$ j	= 1,180

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**P 1-68 B**  
**(30 min.)**

Which company has the highest net income? Highest percent of net income to revenues?

**Solution:**

**Req. 1**

	<b>Babble Co.</b>	<b>Floralities, Inc.</b>	<b>Drake Co.</b>
<b>BALANCE SHEET</b>		<i>Millions</i>	
Beginning:			
Assets	\$ 79	\$ 35	\$ 13
Liabilities	51	15	5
Common stock	1	5	2
Retained earnings	27	15	6
Ending:			
Assets	\$ 88	\$ 53	\$ 15
Liabilities	52	27	4
Common stock	1	12	5
Retained earnings	35	14	6
<b>INCOME STATEMENT</b>			
Revenues	\$ 227	\$ 163	\$ 27
Expenses	218	153	23
Net income	9	10	4
<b>STATEMENT OF RETAINED EARNINGS</b>			
Beginning RE	\$ 27	\$ 15	\$ 6
+ Net income	9	10	4
- Dividends declared	(1)	(11)	(4)
= Ending RE	\$ 35	\$ 14	\$ 6

**Req. 2**

	<b>Babble Co.</b>	<b>Floralities, Inc.</b>	<b>Drake Co.</b>
		<i>Millions</i>	
Net income	\$9	\$10 <i>Highest</i>	\$4
% of net income to revenues	<u>\$9</u> \$227 = 4.0%	<u>\$10</u> \$163 = 6.1%	<u>\$4</u> \$27 = 14.8% <i>Highest</i>

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**P 1-69 B**  
**(20-25 min.)**

1. Prepare the correct balance sheet and date it properly. Compute total assets, total liabilities, and stockholders' equity.
2. Is Parker Design, Inc., in better (or worse) financial position than the erroneous balance sheet reports? Give the reason for your answer.
3. Identify the accounts listed on the incorrect balance sheet that should not be reported on the balance sheet. State why you excluded them from the correct balance sheet you prepared for Requirement 1. On which financial statement should these accounts appear?

**Solution:**

**Req. 1**

<b>Parker Design, Inc.</b>			
<b>Balance Sheet</b>			
<b>March 31, 2018</b>			
<b>Assets</b>		<b>Liabilities</b>	
Cash	\$ 8,000	Accounts payable	\$ 3,500
Accounts receivable	3,900	Note payable	53,000
Notes receivable	13,000	Total liabilities	56,500
Office supplies	1,400	<b>Stockholders' equity</b>	
Land	86,000	Stockholders' equity*	94,800
Equipment	39,000	Total liabilities and stockholders' equity	\$ 151,300
Total assets	<u>\$ 151,300</u>		<u>\$ 151,300</u>

\*Total assets (\$151,300) – Total liabilities (\$56,500) = Stockholders' equity (\$94,800)

**Req. 2**

Parker Design, Inc. is in a better financial position than the erroneous balance sheet reports. Assets are \$9,800 greater and liabilities are \$16,300 less than originally reported, and equity is \$26,100 greater than reported originally.

**Req. 3**

The following accounts are not reported on the balance sheet because they are expenses. Expenses are reported on the income statement.

- Utilities expense
- Advertising
- Salary expense
- Interest expense

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**P 1-70 B**  
**(20-25 min.)**

1. Prepare the balance sheet of the real estate business of Hudson Alvarez Realtor, Inc., at June 30, 2019.
2. Does it appear that the realty business can pay its debts? How can you tell?
3. Identify the personal items given in the preceding facts that should not be reported on the balance sheet of the business.

**Solution:**

**Req. 1**

<b>Hudson Alvarez Realtor, Inc.</b>			
<b>Balance Sheet</b>			
<b>June 30, 2019</b>			
<b>Assets</b>		<b>Liabilities</b>	
Cash	\$ 44,000	Accounts payable	\$ 9,000
Office supplies	4,000	Note payable	102,000
Land	162,000	Total liabilities	111,000
Furniture	17,600	<b>Stockholders' equity</b>	
Franchise	16,000	Common stock	75,000
		Retained earnings	57,600
		Total stockholders' equity	132,600
Total assets	<u>\$ 243,600</u>	Total liabilities and stockholders' equity	<u>\$ 243,600</u>

\*Total assets (\$243,600) – Total liabilities (\$111,000) – Common stock (\$75,000) = Retained earnings (\$57,600).

**Req. 2**

It appears that Hudson Alvarez's business can pay its debts. Total assets far exceed total liabilities.

**Req. 3**

Personal items not reported on the balance sheet of the business:  
 a. Personal cash (\$17,000)  
 b. Personal account payable (\$6,500)  
 g. Personal residence (\$419,000) and personal mortgage (\$179,000)

**P 1-71 B**  
**(30-45 min.)**

1. Prepare the income statement of Full Moon Products, Inc., for the year ended December 31, 2018.
2. Prepare the company's statement of retained earnings for the year.
3. Prepare the company's balance sheet at December 31, 2018.
4. Analyze Full Moon Products, Inc., by answering these questions:
  - a. Was Full Moon profitable during 2018? By how much?
  - b. Did retained earnings increase or decrease? By how much?
  - c. Which is greater, total liabilities or total stockholders' equity? Who has a greater claim to Full Moon Products's assets: its creditors or its stockholders?

**Solution:**

**Req. 1**

Full Moon Products, Inc. Income Statement Year Ended December 31, 2018		
Revenue:		
Service revenue		\$ 451,600
Expenses:		
Salary expense	\$ 108,900	
Rent expense	41,000	
Interest expense	10,000	
Utilities expense	8,100	
Property tax expense	7,300	
Total expenses		175,300
Net income		\$ 276,300

**Req. 2**

Full Moon Products, Inc. Statement of Retained Earnings Year Ended December 31, 2018	
Retained earnings, December 31, 2017	\$ 364,800
Add: Net income	276,300
Subtotal	641,100
Less: Dividends declared	(108,000)
Retained earnings, December 31, 2018	\$ 533,100

**Req. 3**

Full Moon Products, Inc. Balance Sheet December 31, 2018			
ASSETS		LIABILITIES	
Cash	\$ 46,000	Accounts payable	\$ 25,000
Accounts receivable	85,000	Interest payable	2,800
Supplies	6,200	Note payable	99,200
Land	29,000	Total liabilities	127,000
Building	405,000		
Equipment	115,000		
		STOCKHOLDERS' EQUITY	
		Common stock	26,100
		Retained earnings	533,100
		Total stockholders' equity	559,200
Total assets	\$ 686,200	Total liabilities and stockholders' equity	\$ 686,200

**Req. 4**

- a. Full Moon Products was profitable; net income was \$276,300.
  - b. Retained earnings increased by \$168,300 — from \$364,800 to \$533,100.
  - c. Total equity (\$559,200) exceeds total liabilities (\$127,000).
- Therefore, the stockholders have a greater claim against the company's assets than do the creditors.

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**P 1-72 B**  
**(20 min.)**

1. Prepare Tidal Wave Company's cash flow statement for the year ended March 31, 2019. Not all the items listed will appear on the cash flow statement.
2. Which activities provided the largest source of cash? Is this a sign of financial strength or weakness?

**Solution:**

**Req. 1**

<b>Tidal Wave Company</b>		
<b>Statement of Cash Flows</b>		
<b>Year Ended March 31, 2019</b>		
Millions		
Cash flows from operating activities:		
Net income		\$ 3,050
Adjustments to reconcile net income to net cash provided by operating activities		<u>2,380</u>
Net cash provided by operating activities		5,430
Cash flows from investing activities:		
Purchases of property, plant, and equipment	\$ (3,500)	
Sales of property, plant, and equipment	60	
Other investing cash payments	<u>(200)</u>	
Net cash used for investing activities		<u>(3,640)</u>
Cash flows from financing activities:		
Issuance of common stock	\$ 200	
Payment of dividends	<u>(360)</u>	
Net cash used for financing activities		<u>(160)</u>
Net increase in cash		\$ 1,630
Cash, beginning		<u>270</u>
Cash, ending		<u>\$ 1,900</u>

**Req. 2**

Operating activities provided the bulk of Tidal Wave Company's cash. This is a sign of strength because operations should be the main source of cash.

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**P 1-73 B**  
**(40-50 min.)**

1. Complete Weaverton Corporation's financial statements by determining the missing amounts denoted by the letters. If necessary, round numbers up to the nearest whole dollar.

**Solution:**

<b>INCOME STATEMENT</b>		<b>2019</b>	<b>2018</b>	
Revenues	13,800	= \$ k	\$ 16,175	
Cost of goods sold		(11,020)	a =	(13,115)
Other expenses		(1,250)	(1,220)	
Income before income taxes		1,530	1,840	
Income taxes (35% tax rate)	536	=	l	(644)
Net income	994	=	\$ m	\$ b = 1,196
<b>STATEMENT OF RETAINED EARNINGS</b>				
Beginning balance	3,726	=	\$ n	2,670
Net income	994	=	o	c = 1,196
Dividends declared			(98)	(140)
Ending balance	4,622	=	\$ p	\$ d = 3,726
<b>BALANCE SHEET</b>				
Assets:				
Cash	980	=	\$ q	\$ e = 1,090
Property, plant and equipment			1,487	1,316
Other assets	12,205	=	r	12,060
Total assets	14,672	=	\$ s	14,466
Liabilities:				
Current liabilities	3,955	=	\$ t	5,610
Long-term debt			4,450	3,360
Other liabilities			995	1,140
Total liabilities			9,400	f = 10,110
<b>Stockholders' Equity:</b>				
Common stock			\$450	450
Retained earnings	4,622	=	u	g = 3,726
Other stockholders' equity			200	180
Total stockholders' equity	5,272	=	v	4,356
Total liabilities and stockholders' equity	14,672	=	\$ w	\$ h = 14,466
stockholders' equity		=		
<b>STATEMENT OF CASH FLOWS</b>				
Net cash provided by operating activities	700	=	\$ x	\$875
Net cash used for investing activities			(300)	(575)
Net cash used for financing activities			(510)	(500)
Increase (decrease) in cash			(110)	i = (200)
Cash at beginning of year	1,090	=	y	1,290
Cash at end of year	980	=	\$ z	\$ j = 1,090



**Serial Case**  
**(15-20 min.)**

1. What form of business organization is The Cheesecake Factory? How do you know?
2. Identify what line item flows from the income statement to the statement of retained earnings.
3. Identify the line item that flows from the statement of retained earnings to the balance sheet.
4. Identify the line item that flows from the statement of cash flows to the balance sheet.
5. Did The Cheesecake Factory have net income or net loss for its fiscal year 2016? (The Cheesecake Factory's 2016 fiscal year end is January 3, 2017.) Over what period of time was this amount earned?
6. Write The Cheesecake Factory's accounting equation as of January 3, 2017.
7. How much in total resources does The Cheesecake Factory have to work with at January 3, 2017? How much does The Cheesecake Factory owe to creditors at January 3, 2017?

**Solution**

**Req. 1**

1. The Cheesecake Factory is organized as a corporation, per the name of the business ("Incorporated").

**Req. 2**

2. Net income flows from the Income Statement to the Statement of Retained Earnings.

**Req. 3**

3. Ending retained earnings flows from the Statement of Retained Earnings to the Balance Sheet.

**Req. 4**

4. Cash and cash equivalents flows from the Statement of Cash Flows to the Balance Sheet.

**Req. 5**

5. The Cheesecake Factory earned net income of \$139,494 (in thousands) in fiscal 2016. This income was earned from December 29, 2015 to January 3, 2017.

**Req. 6**

Assets = Liabilities + Shareholders' Equity

\$1,293,319 = \$690,112\* + \$603,207

**Req. 7**

7. Cheesecake Factory had \$1,293,319 (Total Assets) to work with and owes \$690,112\* (Total Liabilities) to creditors. (Numbers in thousands)

\*(\$376,526 + \$313,586 = \$690,112)

**Decision Case 1**  
**(30-40 min.)**

1. Using only these balance sheets, to which entity would you be more comfortable lending money? Explain fully, citing specific items and amounts from the respective balance sheets.

***Solution:***

Based solely on these balance sheets, Insley Sales Co. appears to be the better credit risk because:

1. Queens Service has more assets (\$150,000) than Insley Sales (\$65,000), but Queens Service owes much more in liabilities (\$130,000 versus \$15,000 for Insley Sales). Insley Sales' stockholders' equity is far greater than that of Queens Service (\$50,000 compared to \$20,000). Insley Sales is not heavily in debt, but Queens Service is.

2. You would be better off granting the loan to Insley Sales. You should consider what will happen if the borrower cannot pay you back as planned. Queens Service has far more liabilities to pay, and it may be hard for Queens Service to come up with the money to pay you. On the other hand, Insley Sales has little debt to pay to others before paying you.

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**Decision Case 2  
(20-30 min.)**

1. Prepare corrected financial statements.
2. Use your corrected statements to evaluate Flowers Unlimited's results of operations and financial position.
3. Will you invest in Flowers Unlimited? Give your reason.

**Solution:**

**Req. 1**

<b>Flowers Unlimited, Inc. Income Statement Year Ended Dec. 31, 2018</b>	
Revenue <sup>1</sup> .....	\$ 140,000
Expenses <sup>2</sup> .....	<u>140,000</u>
Net income .....	<u>\$ -</u>

<b>Flowers Unlimited, Inc. Balance Sheet Dec. 31, 2018</b>			
Cash	\$ 6,000	Liabilities <sup>4</sup>	\$ 70,000
Other assets <sup>3</sup>	<u>\$ 90,000</u>	S/H Equity <sup>5</sup>	<u>26,000</u>
Total assets	<u>\$ 96,000</u>	Total liabilities and S/H Equity	<u>\$ 96,000</u>

<sup>1</sup> \$100,000 + \$40,000 = \$140,000
<sup>2</sup> \$80,000 + \$50,000 + \$10,000 = \$140,000
<sup>3</sup> \$100,000 - \$50,000 + \$40,000 = \$90,000
<sup>4</sup> \$60,000 + \$10,000 = \$70,000
<sup>5</sup> \$96,000 - \$70,000 = \$26,000

**Req. 2**

The company's financial position is much weaker than originally reported. Assets and stockholders' equity are lower and liabilities are higher. Results of operations are worse than reported. The company did not earn any profit.

**Req. 3**

Based on the actual figures, I would not invest in Flowers Unlimited for reasons given in Req. 2.

**Ethical Issues**

(40-50 min.)

1. What is the ethical issue in this situation?
2. Who are the stakeholders? What are the possible consequences to each?
3. Analyze the alternatives from the following standpoints: (a) economic, (b) legal, and (c) ethical.
4. What would you do? How would you justify your decision? How would your decision make you feel afterward?
5. How is this similar to a business situation?

**Solution:**

**Req. 1**

The fundamental ethical issue in this situation is whether you should accept a copy of the old exam from your friend.

**Req. 2**

The stakeholders are:

- a. You
- b. Your friend
- c. The remainder of students in the class
- d. The professor
- e. The University
- f. Your family

**Req. 3**

Analysis of the problem:

Economic perspective: If use of the old exam turns out to help you (it may not) you might improve your grade and allow you to retain your scholarship. This might help you and your family financially. If you use the exam to your unfair advantage, and you are reported, you and possibly your friend might receive grades of F in the class although you might otherwise have passed. This could cause adverse economic consequences to you, your friend and your families.

Legal perspective: Although it may not violate local or federal law, giving or accepting copies of old exams may violate the university's honor code, which serves the same purpose as a legal code in this case. If you use the old exam and it turns out that you violated the University's honor code, both you and your friend could be in trouble. Your family and your friend's family could also be impacted by any adverse consequences to you or her. Academic institutions establish policies against academic dishonesty because cheating hurts everyone—the student who commits the act, the other students in the class whose rights to fair treatment are violated by cheating, and the professor who must endure hours of investigating, reporting, and perhaps testifying.

Ethical perspective: Receiving questionable help from others in the face of policies that prohibit it is, at best, risky, and at worst, downright wrong. Cheating is similar to stealing, since it is stealing the work of another without their permission. It is usually accompanied by lying to cover it up, or at least, not revealing the truth. Cheating violates other students' rights to fair and equal treatment. It violates the instructor's rights to run a course as a "fair game" for all participants. Because the students and faculty are hurt by cheating, the university is hurt too. If cheating goes unpunished, grades are inflated, ultimately damaging the academic reputation of the institution and eroding the value of its degrees. Parents of students who are caught cheating have to endure the agony of working through the problem with their son or daughter, and perhaps the social stigma that comes from adverse publicity.

These are just some of the arguments against cheating. Of course, there is a question in this case as to whether taking the test actually violates the professor's or the university's policies.

**Req. 4**

It would be helpful to find out what the professor's policies are with respect to the use of fraternity and sorority test files. The university might have a blanket policy on this. (Some students might spend a little time researching this by reading the university's honor code on their web site; just reading the honor code will be an eye-opening experience for most students). Advise your students to research the use of fraternity and sorority test files on the university web site, or to discuss the issue with the head of the department or the chair of the university honor council.

Unfortunately, in this case, there is not much time. Researching the issue in the university's honor code takes valuable time away from studying for the exam, which, if you do, could help you raise your grade and solve the whole problem!

Probably the best solution to this problem is "when in doubt, don't." You may not do well on the test, but at least you won't have to live with the terrible consequences of being accused as a cheater. It should make you feel better in the long run that, although you may not make the highest grades in the class, at least you are not a cheater.

**Req. 5**

Cheating is very closely related to stealing, which is a form of fraud. When employees steal from their companies, they steal property that belongs to others. There are economic, legal, and ethical consequences to the company, the employee and their families, and customers (who ultimately have to pay for fraud through higher prices). We will study fraud in depth in Chapter 4.

**Apple Inc.**  
(20-30 min.)

1. Go online and do some research on Apple Inc. and its industry. Use one or more popular websites like <http://finance.yahoo.com> or <http://www.google.com/finance>. Write a paragraph (about 100 words) that describes the industry, some current developments, and a projection for future growth.
2. Read Part I, Item 1 (Business) of Apple's annual report. What do you learn here and why is it important?
3. Name at least one of Apple's competitors. Why is this information important in evaluating Apple's financial performance?
4. Suppose you own stock in Apple. If you could pick one item on the company's Consolidated Statements of Operations to increase year after year, what would it be? Why is this item so important? Did this item increase or decrease during fiscal 2016? Is this good news or bad news for the company?
5. What was Apple's largest expense in 2014 - 2016? In your own words, explain the meaning of this item. Give specific examples of items that make up this expense. The chapter gives another title for this expense. What is it?
6. Use the Consolidated Balance Sheets of Apple in Appendix A to answer these questions: At the end of fiscal 2016, how much in total resources did Apple have to work with? How much did the company owe? How much of its assets did the company's stockholders actually own? Use these amounts to write Apple's accounting equation at September 24, 2016.
7. How much cash and cash equivalents did Apple have at September 26, 2015? How much cash and cash equivalents did Apple have at September 24, 2016?

**Solution:**

1. Students can emphasize a variety of points regarding Apple Inc., and its industry. For example, a discussion on the product innovation and competitive changes in technology would be appropriate. Additionally, discussing recent news articles related to Apple or its competitors would also be appropriate. Student answers will vary.
2. Some important information in this portion of the financials is the description of their distribution channels (third-party resellers), competitors (product innovation, market opportunities, etc.), and supply chain (shortages, component availability, outsourcing, etc.). Additionally, the seasonality of Apple's business is important to note given that it has higher sales in its first quarter relative to the last three. Lastly, it may come as a surprise that Apple employs approximately 116,000 full-time employees. (Student answers will vary.)
3. Samsung, Google, Sony, or HP are some of Apple Inc.'s competitors. It is important to identify competitors because competitors tend to have similar business dynamics to one another, meaning that their financial statements can be compared to and benchmarked against each other. Student answers will vary.
4. Net income, because it shows the overall result of all the revenues minus all the expenses for a period. In effect, net income gives the results of operations in a single figure and shows whether the company has been profitable. Apple's net income after taxes decreased from \$53.4 billion in 2015 to \$45.7 billion in 2016, which is unfavorable.
5. Apple Inc.'s largest expense is cost of sales. This is the cost of the products that the company sells, such as iPhones, iPads, Apple TVs, software, and Mac desktops. Another title of this account is cost of goods sold.
6. Total resources (total assets) at September 24, 2016.....\$321,686 million  
 Amount owed (total liabilities) at September 24, 2016....\$193,437 million  
 Portion of the company's assets owned by the stockholders (stockholders' equity) at September 24, 2016.....\$128,249 million  
 Apple Inc.'s accounting equation (*in millions*):  

Assets	=	Liabilities	+	Stockholders' Equity
\$321,686	=	\$193,437	+	\$128,249
7. At September 26, 2015, Apple Inc. had \$21,120 million of cash and cash equivalents. At September 24, 2016, Apple Inc. had \$20,484 million of cash and cash equivalents.

**Under Armour, Inc.**  
(30 min.)

1. Go online and do some research on Under Armour and its industry. Use one or more popular websites like <http://finance.yahoo.com> or <http://www.google.com/finance>. Write a paragraph (about 100 words) that describes the industry, some current developments, and a projection for where the industry is headed.
2. Read Note 1—(Description of Business) of Under Armour’s annual report. What do you learn here and why is it important?
3. Name two of Under Armour’s competitors. Why is this information important in evaluating Under Armour’s financial performance?
4. Write Under Armour’s accounting equation at December 31, 2016 (express all items in millions and round to the nearest \$1 million). Does Under Armour’s financial condition look strong or weak? How can you tell?
5. What was the result of Under Armour’s operations during 2016? Identify both the name and the dollar amount of the result of operations for 2016. Does an increase (or decrease) signal good news or bad news for the company and its stockholders?
6. Examine retained earnings in the Consolidated Statements of Shareholders’ Equity. What caused retained earnings to increase during 2016?
7. Which statement reports cash and cash equivalents as part of Under Armour’s financial position? Which statement tells why cash and cash equivalents increased (or decreased) during the year? Which activities caused the company’s cash and cash equivalents to change during 2016, and how much did each activity provide or use?

**Solution:**

1. Under Armour, Inc. is an athletic apparel company. Students can emphasize a variety of points regarding Under Armour, Inc. and its industry. For example, a discussion on the brand, new product development, etc. would be appropriate. Additionally, discussing recent news articles related to Under Armour or its competitors would also be appropriate. (Student answers will vary.)
2. Note 1 states Under Armour is a developer, marketer and distributor of branded performance apparel, footwear, and accessories. These products are sold worldwide and worn by athletes of all levels and consumers with active lifestyles.
3. Nike, Adidas, and Columbia Sportswear are some of Under Armour, Inc.’s competitors. It is important to identify competitors because competitors tend to have similar business dynamics to one another, meaning that their financial statements can be compared to and benchmarked against each other. (Student answers will vary.)
4. Under Armour, Inc.’s Accounting Equation (in millions):  

$$\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}$$

$$\$3,644 = \$1,613 + \$2,031$$

Under Armour, Inc. appears to be in strong financial condition. Total assets are significantly higher than the amount of total liabilities. This suggests that the company will have no difficulty paying its debts and will have money to expand.
5. The result of operations for 2016 was a net income of \$256,979 thousand. This is good news for Under Armour, Inc. Revenue exceeded expenses for fiscal 2016, and there is a positive trend in earnings over the past two years (\$208,042 thousand, \$232,573 thousand, and \$256,979 thousand in fiscal 2014, 2015, and 2016, respectively). The increase in net income signals good news.
6. According to Under Armour, Inc.’s Consolidated Statements of Stockholders’ Equity, the cause of the company’s large increase in retained earnings during 2016 was comprehensive income of \$256,979 thousand. (Comprehensive income is closely related to net income.)
7. The Consolidated Balance Sheets report cash and cash equivalents as part of the company’s financial position. The Consolidated Statements of Cash Flows tell why cash and cash equivalents increased or decreased. Operating activities provided \$304,487 thousand, investing activities used \$381,139 thousand, and financing activities provided \$205,995 thousand.