

Required

1. Prepare a multiple-step income statement for the year ended December 31, 2012.
2. What advantages do you see in this form for the income statement?
3. Compute Corbin's profit margin.
4. Comment on Corbin's profitability. What other factors need to be taken into account to assess Corbin's profitability?

Problem 2-8A Statement of Cash Flows**L08**

Wisconsin Corporation was organized on January 1, 2012, with the investment of \$400,000 in cash by its stockholders. The company immediately purchased a manufacturing facility for \$300,000, paying \$150,000 in cash and signing a five-year promissory note for the balance. Wisconsin signed another five-year note at the bank for \$50,000 during 2012 and received cash in the same amount. During its first year, Wisconsin collected \$310,000 from its customers. It paid \$185,000 for inventory, \$30,100 in salaries and wages, and another \$40,000 in taxes. Wisconsin paid \$4,000 in cash dividends.

Required

1. Prepare a statement of cash flows for the year ended December 31, 2012.
2. What does this statement tell you that an income statement does not?

Problem 2-9A Basic Elements of Financial Reports**L09**

Comparative income statements for Thesaurus Inc. are as follows:

	2012	2011
Operating revenues	\$500,000	\$200,000
Operating expenses	<u>120,000</u>	<u>100,000</u>
Operating income	\$380,000	\$100,000
Gain on the sale of subsidiary	—	400,000
Net income	<u>\$380,000</u>	<u>\$500,000</u>

Required

The president and management believe that the company performed better in 2012 than it did in 2011. Write the president's letter to be included in the 2012 annual report. Explain why the company is financially sound and why shareholders should not be alarmed by the reduction in income in a year when operating revenues increased significantly.

ALTERNATE MULTI-CONCEPT PROBLEMS**Problem 2-10A Comparing Starwood Hotels & Resorts and Hyatt Hotels Corporation and Subsidiaries****L02 • 4**

The following current items, listed in alphabetical order, are taken from the consolidated balance sheets of **Starwood Hotels & Resorts Worldwide, Inc.** as of December 31, 2010, and **Hyatt Hotels Corporation and Subsidiaries** as of December 31, 2010. (All amounts are in millions of dollars.)

Starwood Hotels & Resorts Worldwide, Inc.

Accounts payable	\$ 138	Current maturities of long-term securitized vacation ownership debt	\$ 127
Accounts receivable, net of allowance for doubtful accounts of \$45	513	Prepaid expenses and other	126
Accrued expenses	1,104	Restricted cash	53
Accrued salaries, wages and benefits	410	Securitized vacation ownership notes receivable, net of allowance for doubtful accounts of \$10	59
Accrued taxes and other	373	Short-term borrowings and current maturities of long-term debt	9
Cash and cash equivalents	753		
Inventories	802		

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Hyatt Hotels Corporation and Subsidiaries

Accounts payable	\$ 145	Deferred tax assets	\$ 29
Accrued compensation and benefits	108	Inventories	100
Accrued expenses and other current liabilities	286	Prepays and other assets	73
Assets held for sale	18	Prepaid income taxes	6
Cash and cash equivalents	1,110	Receivables, net of allowances of \$15	199
Current maturities of long-term debt	57	Restricted cash	106
		Short-term investments	524

Required

1. Compute working capital and the current ratio for both companies.
2. On the basis of your answers to (1), which company appears to be more liquid?
3. Other factors affect a company's liquidity besides working capital and current ratio. Comment on the *composition* of each company's current assets and ways this composition affects liquidity.

L02 • 5 Problem 2-11A Comparability and Consistency in Income Statements

The following income statements were provided by Chisholm Company, a wholesale food distributor:

	2012	2011
Sales	\$1,700,000	\$1,500,000
Cost of sales	\$ 612,000	\$ 450,000
Sales salaries	427,000	398,000
Delivery expense	180,000	175,000
Office supplies	55,000	54,000
Depreciation—truck	40,000	40,000
Total expenses	<u>23,000</u>	<u>20,000</u>
Net income	<u>\$ 1,337,000</u>	<u>\$1,137,000</u>
	<u>\$ 363,000</u>	<u>\$ 363,000</u>

Required

1. Identify each income statement as either single- or multiple-step format.
2. Restate each item in the income statements as a percentage of sales. Why did net income remain unchanged when sales increased in 2012?

L01 • 4 • 8 Problem 2-12A Cash Flow

Roosevelt Inc., a consulting service, has a history of paying annual dividends of \$1 per share. Management is trying to determine whether the company will have adequate cash on December 31, 2013, to pay a dividend if one is declared by the board of directors. The following additional information is available:

- All sales are on account, and accounts receivable are collected one month after the sale. Sales volume has been decreasing 5% each month.
- Operating expenses are paid in cash in the month incurred. Average monthly expenses are \$10,000 (excluding the biweekly payroll).
- Biweekly payroll is \$4,500, and it will be paid December 15 and December 31.
- Unearned revenue is expected to be earned in December. This amount was taken into consideration in the expected sales volume.

- d. The bank acts as a collection agency for checks returned for insufficient funds. The March bank statement indicates that one such check in the amount of \$45.00 was collected and deposited and a collection fee of \$4.50 was charged.
- e. Interest earned on the checking account and added to Karen's account during March was \$4.30. Miscellaneous bank service charges amounted to \$22.
- f. A comparison between the deposits listed on the bank statement and the company's books revealed that a customer's check in the amount of \$1,250 appears on the bank statement in March but was never added to the customer's account on the company's books.
- g. The comparison of checks cleared per the bank statement with those per the books revealed that the wrong amount was charged to the company's account for a check. The amount of the check was \$990. The proof machine encoded the check in the amount of \$909, the amount charged against the company's account.

Required

1. Determine the balance on the books before any adjustments as well as the corrected balance to be reported on the balance sheet.
2. What would you recommend Karen's do as a result of the bank error in (g)? Why?

Problem 6-2A Internal Control Procedures**L04**

The loan department in a bank is subject to regulation. Internal auditors work for the bank to ensure that the loan department complies with requirements. The internal auditors must verify that each car loan file has a note signed by the maker, verification of insurance, and a title issued by the state that names the bank as co-owner.

Required

1. Explain why the bank and the regulatory agency are concerned with these documents.
2. Describe the internal control procedures that should be in place to ensure that these documents are obtained and safeguarded.

Problem 6-3A The Design of Internal Control Documents**L05**

Tiger's Group is a newly formed company that produces and sells children's movies about an imaginary character. The movies are in such great demand that they are shipped to retail outlets as soon as they are produced. The company must pay a royalty to several actors for each movie that it sells to retail outlets.

Required

1. Describe some internal control features that should be in place to ensure that all royalties are paid to the actors.
2. Design the shipping form that Tiger's Group should use for the movies. Make sure you include authorizations and indicate the number of copies and the routing of the copies.

ALTERNATE MULTI-CONCEPT PROBLEMS**Problem 6-4A Cash and Liquid Assets on the Balance Sheet****L01 • 2**

The following accounts are listed in a company's general ledger:

	December 31, 2012	December 31, 2011
Accounts Receivable	\$12,300	\$10,000
Certificates of Deposit (three months)	10,000	10,000
Marketable Securities	4,500	4,000
Petty Cash Fund	1,200	1,500
Money Market Fund	25,800	28,000
Cash in Checking Account	6,000	6,000

(Continued)

Required

1. Which items are cash equivalents?
2. Explain where items that are not cash equivalents should be classified on the balance sheet.
3. What are the amount and the direction of change in cash and cash equivalents for 2012? Is the company as liquid at the end of 2012 as it was at the end of 2011? Explain your answer.

L03 • 4 Problem 6-5A Internal Control

Abbott Inc. is expanding and needs to hire more personnel in the accounting office. Barbara Barker, the chief accounting clerk, knew that her cousin Cheryl was looking for a job. Barbara and Cheryl are also roommates. Barbara offered Cheryl a job as her assistant. Barbara will be responsible for Cheryl's performance reviews and training.

Required

1. List some problems with the proposed personnel situations in the accounting department.
2. Explain why accountants are concerned with the hiring of personnel. What suggestions would you make to improve internal control at Abbott?
3. How would you explain to Barbara and Cheryl that they personally are not the problem?

DECISION CASES

L01 Reading and Interpreting Financial Statements**Decision Case 6-1 Comparing Two Companies in the Same Industry: Kellogg's and General Mills**

Refer to the financial information for **Kellogg's** and **General Mills** reproduced at the end of this book.

Required

1. What is the balance in Cash and cash equivalents on the balance sheet of each company at the end of the most recent year? What is the amount of increase or decrease in this balance from the end of the prior year?
2. On what other statement in each company's annual report does the increase or decrease in Cash and cash equivalents appear? Explain why it appears on this statement.
3. According to the notes to their financial statements, how does each company define "Cash and cash equivalents"? Are there any differences in their definitions?

L03 Decision Case 6-2 Reading and Interpreting IBM's Report of Management

IBM's 2010 annual report includes the following selected paragraphs from its Report of Management found on page 60:

IBM maintains an effective internal control structure. It consists, in part, of organizational arrangements with clearly defined lines of responsibility and delegation of authority, and comprehensive systems and control procedures. An important element of the control environment is an ongoing internal audit program. Our system also contains self-monitoring mechanisms, and actions are taken to correct deficiencies as they are identified. . . .

PricewaterhouseCoopers LLP, an independent registered public accounting firm, is retained to audit IBM's Consolidated Financial Statements and the effectiveness of the internal control over financial reporting. Its accompanying report is based on audits conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States). . . .

The Audit Committee of the Board of Directors is composed solely of independent, non-management directors, and is responsible for recommending to the Board the independent registered public accounting firm to be retained for the coming year, subject to stockholder ratification. The Audit Committee meets periodically and privately with the independent registered

Required

Determine the amount that should be distributed to each partner assuming the following business net incomes:

1. \$15,000
2. \$50,000
3. \$80,000

L011 Problem 11-10 Sole Proprietorships (Appendix)

On May 1, Chong Yu deposited \$120,000 of his own savings in a separate bank account to start a printing business. He purchased copy machines for \$42,000. Expenses for the year, including depreciation on the copy machines, were \$84,000. Sales for the year, all in cash, were \$108,000. Chong withdrew \$12,000 during the year.

Required

1. What is the balance in Chong's capital account at the end of the year?
2. Explain why the balance in Chong's capital account is different from the amount of cash on hand.

L011 Problem 11-11 Partnerships (Appendix)

Kirin Nerise and Milt O'Brien agreed to form a partnership to operate a sandwich shop. Kirin contributed \$25,000 cash and will manage the store. Milt contributed computer equipment worth \$8,000 and \$92,000 cash. Milt will keep the financial records. During the year, sales were \$90,000 and expenses (including a salary to Kirin) were \$76,000. Kirin withdrew \$500 per month. Milt withdrew \$4,000 (total). Their partnership agreement specified that Kirin would receive a salary of \$7,200 for the year. Milt would receive 6% interest on his initial capital investment. All remaining income or loss would be equally divided.

Required

Calculate the ending balance in each partner's equity account.

MULTI-CONCEPT PROBLEMS**L01 • 4 Problem 11-12 Analysis of Stockholders' Equity**

The Stockholders' Equity section of the December 31, 2012, balance sheet of Eldon Company appeared as follows:

Preferred stock, \$30 par value, 5,000 shares authorized, ? shares issued	\$120,000
Common stock, ? par, 10,000 shares authorized, 7,000 shares issued	70,000
Additional paid-in capital—Preferred	6,000
Additional paid-in capital—Common	560,000
Additional paid-in capital—Treasury stock	1,000
Total contributed capital	<u>\$757,000</u>
Retained earnings	40,000
Less: Treasury stock, preferred, 100 shares	(3,200)
Total stockholders' equity	<u>\$?</u>

Required

Determine the following items based on Eldon's balance sheet.

1. The number of shares of preferred stock issued
2. The number of shares of preferred stock outstanding
3. The average per-share sales price of the preferred stock when issued
4. The par value of the common stock
5. The average per-share sales price of the common stock when issued

6. The cost of the treasury stock per share
7. The total stockholders' equity
8. The per-share book value of the common stock assuming that there are no dividends in arrears and that the preferred stock can be redeemed at its par value

Problem 11-13 Effects of Stockholders' Equity Transactions on the Balance Sheet

L03 • 4 • 7

The following transactions occurred at Horton Inc. during its first year of operation:

- a. Issued 100,000 shares of common stock at \$5 each; 1,000,000 shares are authorized at \$1 par value.
- b. Issued 10,000 shares of common stock for a building and land. The building was appraised for \$20,000, but the value of the land is undeterminable. The stock is selling for \$10 on the open market.
- c. Purchased 1,000 shares of its own common stock on the open market for \$16 per share.
- d. Declared a dividend of \$0.10 per share on outstanding common stock. The dividend is to be paid after the end of the first year of operations. Market value of the stock is \$26.
- e. Declared a 2-for-1 stock split. The market value of the stock was \$37 before the stock split.
- f. Reported \$180,000 of income for the year.

Required

1. Indicate each transaction's effect on the assets, liabilities, and stockholders' equity of Horton Inc.
2. Prepare the Stockholders' Equity section of the balance sheet.
3. Write a paragraph that explains the number of shares of stock issued and outstanding at the end of the year.

Problem 11-14 Stockholders' Equity Section of the Balance Sheet

L01 • 4

The newly hired accountant at Ives Inc. prepared the following balance sheet:

Assets	
Cash	\$ 3,500
Accounts receivable	5,000
Treasury stock	500
Plant, property, and equipment	108,000
Retained earnings	1,000
Total assets	<u>\$118,000</u>
Liabilities	
Accounts payable	\$ 5,500
Dividends payable	1,500
Stockholders' Equity	
Common stock, \$1 par, 100,000 shares issued	100,000
Additional paid-in capital	11,000
Total liabilities and stockholders' equity	<u>\$118,000</u>

Required

1. Prepare a corrected balance sheet. Write a short explanation for each correction.
2. Why does the Retained Earnings account have a negative balance?

ALTERNATE PROBLEMS

Problem 11-1A Stockholders' Equity Category

L01

Kebler Company was incorporated as a new business on January 1, 2012. The corporate charter approved on that date authorized the issuance of 2,000 shares of \$100 par, 7% cumulative,

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