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- (b) Liabilities are overstated.
- (c) Liabilities are understated.
- (d) Expenses are understated.
- (e) Assets are overstated.
- (f) Revenue is understated.

**20.**

One-half of the adjusting entry is given below. Indicate the account title for the other half of the entry.

- (a) Salaries and Wages Expense is debited.
- (b) Depreciation Expense is debited.
- (c) Interest Payable is credited.
- (d) Supplies is credited.
- (e) Accounts Receivable is debited.
- (f) Unearned Service Revenue is debited.

**21.**

“An adjusting entry may affect more than one balance sheet or income statement account.” Do you agree? Why or why not?

**22.**



Which balance sheet account provides evidence that **Tootsie Roll** records sales on an accrual basis rather than a cash basis? Explain.

**23.**

Why is it possible to prepare financial statements directly from an adjusted trial balance?

**24.**



- (a) What information do accrual-basis financial statements provide that cash-basis statements do not?
- (b) What information do cash-basis financial statements provide that accrual-basis statements do not?

**25.**

What is the relationship, if any, between the amount shown in the adjusted trial balance column for an account and that account's ledger balance?

**26.**

Identify the account(s) debited and credited in each of the four closing entries, assuming the company has net income for the year.

**27.**



Some companies employ technologies that allow them to do a so-called “virtual close.” This enables them to close their books nearly instantaneously any time during the year. What advantages does a “virtual close” provide?

**28. PRINTED BY: jromero0950@email.phoenix.edu. Printing is for personal, private use only. No part of this book may be reproduced or transmitted without publisher's prior permission. Violators will be prosecuted.**  
Describe the nature of the Income Summary account, and identify the types of summary data that may be posted to this account.

**29.**

What items are disclosed on a post-closing trial balance, and what is its purpose?

**30.**

Which of these accounts would not appear in the post-closing trial balance? Interest Payable, Equipment, Depreciation Expense, Dividends, Unearned Service Revenue, Accumulated Depreciation—Equipment, and Service Revenue.

**31.**

Indicate, in the sequence in which they are made, the three required steps in the accounting cycle that involve journalizing.

**32.**

Identify, in the sequence in which they are prepared, the three trial balances that are required in the accounting cycle.

**33.**



Explain the terms earnings management and quality of earnings.

**34.**



Give examples of how companies manage earnings.

**\*35.**

What is the purpose of a worksheet?

**\*36.**

What is the basic form of a worksheet?

## Brief Exercises

### BE4-1

Transactions that affect earnings do not necessarily affect cash. Identify the effect, if any, that each of the following transactions would have upon cash and net income. The first transaction has been completed as an example.

*Identify impact of transactions on cash and net income.*

(LO 2, 9), C

Cash    Net Income

(b) Recorded an adjusting entry to record use of \$20 of the above supplies.

Cash    Net Income

(c) Made sales of \$1,300, all on account.

(d) Received \$800 from customers in payment of their accounts.

(e) Purchased equipment for cash, \$2,500.

(f) Recorded depreciation of building for period used, \$600.

### BE4-2

The ledger of Berkman Company includes the following accounts. Explain why each account may require adjustment.

*Indicate why adjusting entries are needed.*

(LO 3), C

- (a) Prepaid Insurance.
- (b) Depreciation Expense.
- (c) Unearned Service Revenue.
- (d) Interest Payable.

### BE4-3

Molina Company accumulates the following adjustment data at December 31. Indicate (1) the type of adjustment (prepaid expense, accrued revenue, and so on) and (2) the status of the accounts before adjustment (overstated or understated).

*Identify the major types of adjusting entries.*

(LO 3), AN



- (a) Supplies of \$400 are on hand. Supplies account shows \$1,600 balance.
- (b) Services performed but unbilled total \$700.
- (c) Interest of \$300 has accumulated on a note payable.
- (d) Rent collected in advance totaling \$1,100 has been earned.

### BE4-4

Foley Advertising Company's trial balance at December 31 shows Supplies \$8,800 and Supplies Expense \$0. On December 31, there are \$1,100 of supplies on hand. Prepare the adjusting entry at December 31 and, using T-accounts, enter the balances in the accounts, post the adjusting entry, and indicate the adjusted balance in each account.

*Prepare adjusting entry for supplies.*

(LO 4), AP

**BE4-5**

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 At the end of its first year, the trial balance of Boyer Company shows Equipment \$22,000 and zero balances in Accumulated Depreciation—Equipment and Depreciation Expense. Depreciation for the year is estimated to be \$2,750. Prepare the adjusting entry for depreciation at December 31, post the adjustments to T-accounts, and indicate the balance sheet presentation of the equipment at December 31.

*Prepare adjusting entry for depreciation.*

(LO 4), AP

**BE4-6**

On July 1, 2014, Seng Co. pays \$12,400 to Nance Insurance Co. for a 2-year insurance contract. Both companies have fiscal years ending December 31. For Seng Co., journalize and post the entry on July 1 and the adjusting entry on December 31.

*Prepare adjusting entry for prepaid expense.*

(LO 4), AP

**BE4-7**

Using the data in BE4-6, journalize and post the entry on July 1 and the adjusting entry on December 31 for Nance Insurance Co. Nance uses the accounts Unearned Service Revenue and Service Revenue.

*Prepare adjusting entry for unearned revenue.*

(LO 4), AP

**BE4-8**

The bookkeeper for Beltran Company asks you to prepare the following accrual adjusting entries at December 31. Use these account titles: Service Revenue, Accounts Receivable, Interest Expense, Interest Payable, Salaries and Wages Expense, and Salaries and Wages Payable.

*Prepare adjusting entries for accruals.*

(LO 5), AP

- (a) Interest on notes payable of \$300 is accrued.
- (b) Services performed but unbilled totals \$1,700.
- (c) Salaries of \$780 earned by employees have not been recorded.

**BE4-9**

The trial balance of Goodwin Company includes the following balance sheet accounts. Identify the accounts that might require adjustment. For each account that requires adjustment, indicate (1) the type of adjusting entry (prepaid expenses, unearned revenues, accrued revenues, and accrued expenses) and (2) the related account in the adjusting entry.

*Analyze accounts in an adjusted trial balance.*

(LO 6), AN



- (a) Accounts Receivable.

- (b) Prepaid Insurance.
- (c) Equipment.
- (d) Accumulated Depreciation—Equipment.
- (e) Notes Payable.
- (f) Interest Payable.
- (g) Unearned Service Revenue.

#### BE4-10

The adjusted trial balance of Ravine Corporation at December 31, 2014, includes the following accounts: Retained Earnings \$17,200; Dividends \$6,000; Service Revenue \$32,000; Salaries and Wages Expense \$14,000; Insurance Expense \$1,800; Rent Expense \$3,900; Supplies Expense \$1,500; and Depreciation Expense \$1,000. Prepare an income statement for the year.

*Prepare an income statement from an adjusted trial balance.*

(LO 6), AP

#### BE4-11

Partial adjusted trial balance data for Ravine Corporation are presented in **BE4-10**. The balance in Retained Earnings is the balance as of January 1. Prepare a retained earnings statement for the year assuming net income is \$10,400.

*Prepare a retained earnings statement from an adjusted trial balance.*

(LO 6), AP

#### BE4-12

The following selected accounts appear in the adjusted trial balance for Baden Company. Indicate the financial statement on which each account would be reported.

*Identify financial statement for selected accounts.*

(LO 6), K

- (a) Accumulated Depreciation.
- (b) Depreciation Expense.
- (c) Retained Earnings (beginning).
- (d) Dividends.
- (e) Service Revenue.
- (f) Supplies.
- (g) Accounts Payable.

#### BE4-13

Using the data in BE4-12, identify the accounts that would be included in a post-closing trial balance.

*Identify post-closing trial balance accounts.*

(LO 7), K

#### BE4-14

The income statement for the Four Oaks Golf Club Inc. for the month ended July 31 shows Service Revenue \$16,000; Salaries and Wages Expense \$8,400; Maintenance and Repairs Expense \$2,500; and Income Tax Expense \$1,000. The statement of retained earnings shows an opening balance for Retained Earnings of \$20,000 and Dividends \$1,300.

- (a) Prepare closing journal entries.
- (b) What is the ending balance in Retained Earnings?

**BE4-15**

The required steps in the accounting cycle are listed in random order below. List the steps in proper sequence.

List required steps in the accounting cycle sequence.

(LO 8), K

- (a) Prepare a post-closing trial balance.
- (b) Prepare an adjusted trial balance.
- (c) Analyze business transactions.
- (d) Prepare a trial balance.
- (e) Journalize the transactions.
- (f) Journalize and post closing entries.
- (g) Prepare financial statements.
- (h) Journalize and post adjusting entries.
- (i) Post to ledger accounts.

**Do it!** Review

**Do it!** 4-1

The ledger of Columbia, Inc. on March 31, 2014, includes the following selected accounts before adjusting entries.

Prepare adjusting entries for deferrals.

(LO 4), AP

	<u>Debit</u>	<u>Credit</u>
Supplies	2,500	
Prepaid Insurance	2,400	
Equipment	30,000	
Unearned Service Revenue	<u>Debit</u>	<u>10,000</u> <u>credit</u>

An analysis of the accounts shows the following.

1. Insurance expires at the rate of \$300 per month.  
 2. Supplies on hand total \$900.  
 3. The equipment depreciates \$200 per month.  
 4. During March, services were performed for two-fifths of the unearned service revenue.

Prepare the adjusting entries for the month of March.

**Do it!** 4-2

Kathy Gannon is the new owner of Kathy’s Computer Services. At the end of July 2014, her first month of ownership, Kathy is trying to prepare monthly financial statements. She has the following information for the month.

*Prepare adjusting entries for accruals.*

(LO 5), AP

- 1. At July 31, Kathy owed employees \$1,100 in salaries that the company will pay in August.
- 2. On July 1, Kathy borrowed \$20,000 from a local bank on a 10-year note. The annual interest rate is 9%.
- 3. Service revenue unrecorded in July totaled \$1,600.

Prepare the adjusting entries needed at July 31, 2014.

**Do it!** 4-3

Indicate in which financial statement each of the following adjusted trial balance accounts would be presented.

*Prepare financial statements from adjusted trial balance.*

(LO 6), C

- |                 |                          |
|-----------------|--------------------------|
| Service Revenue | Accounts Receivable      |
| Notes Payable   | Accumulated Depreciation |
| Common Stock    | Utilities Expense        |

**Do it!** 4-4

After closing revenues and expense, Alomar Company shows the following account balances.

*Prepare closing entries.*

(LO 7), AP

- |                   |          |
|-------------------|----------|
| Dividends         | \$22,000 |
| Retained Earnings | 70,000   |

Prepare the remaining closing entries at December 31.

## Exercises

### E4-1

The following independent situations require professional judgment for determining when to recognize revenue from the transactions.

*Identify point of revenue recognition.*

(LO 1), C



- (a) **Southwest Airlines** sells you an advance-purchase airline ticket in September for your flight home at Christmas.
- (b) **Ultimate Electronics** sells you a home theater on a “no money down and full payment in three months” promotional deal.
- (c) The **Toronto Blue Jays** sell season tickets online to games in the Skydome. Fans can purchase the tickets at any time, although the season doesn’t officially begin until April. The major league baseball season runs from April through October.
- (d) You borrow money in August from **RBC Financial Group**. The loan and the interest are repayable in full in November.
- (e) In August, you order a sweater from **Sears** using its online catalog. The sweater arrives in September, which you charged to your Sears credit card. You receive and pay the Sears bill in October.

### Instructions

Identify when revenue should be recognized in each of the above situations.

### E4-2

These accounting concepts were discussed in this and previous chapters.

*Identify accounting assumptions, principles, and constraint.*

(LO 1), K

- 1. Economic entity assumption.
- 2. Expense recognition principle.
- 3. Monetary unit assumption.
- 4. Periodicity assumption.
- 5. Historical cost principle.
- 6. Materiality.
- 7. Full disclosure principle.
- 8. Going concern assumption.
- 9. Revenue recognition principle.
- 10. Cost constraint.

### Instructions

Identify by number the accounting concept that describes each situation below. Do not use a number more than once.



	<u>2014</u>	<u>2013</u>
Unpaid wages owed	2,000	2,400
Other unpaid expenses	1,400	1,100

***Instructions***

Determine the company's net earnings on an accrual basis for 2014. Show all your calculations in an orderly fashion.

**E4-5**

In its first year of operations, Ramirez Company recognized \$28,000 in service revenue, \$6,000 of which was on account and still outstanding at year-end. The remaining \$22,000 was received in cash from customers.

*Determine cash-basis and accrual-basis earnings.*

(LO 2, 9), AP



The company incurred operating expenses of \$15,800. Of these expenses, \$12,000 were paid in cash; \$3,800 was still owed on account at year-end. In addition, Ramirez prepaid \$2,400 for insurance coverage that would not be used until the second year of operations.

***Instructions***

- (a) Calculate the first year's net earnings under the cash basis of accounting, and calculate the first year's net earnings under the accrual basis of accounting.
- (b) Which basis of accounting (cash or accrual) provides more useful information for decision-makers?

**E4-6**

Kaffen Company, a ski tuning and repair shop, opened on November 1, 2013. The company carefully kept track of all its cash receipts and cash payments. The following information is available at the end of the ski season, April 30, 2014.

*Convert earnings from cash to accrual basis; prepare accrual-based financial statements.*

(LO 2, 4, 5, 9), AP



	<u>Cash Receipts</u>	<u>Cash Payments</u>
Issuance of common shares	\$20,000	

	<u>Cash Receipts</u>	<u>Cash Payments</u>
Payment to purchase repair shop equipment		\$ 9,200
Rent payments		1,225
Newspaper advertising payment		375
Utility bill payments		970
Part-time helper's wage payments		2,600
Income tax payment		10,000
Cash receipts from ski and snowboard repair services	<u>32,150</u>	—
Subtotals	52,150	24,370
Cash balance	—	<u>27,780</u>
Totals	\$52,150	\$52,150

The repair shop equipment was purchased on November 1 and has an estimated useful life of 4 years. The company rents space at a cost of \$175 per month on a one-year lease. The lease contract requires payment of the first and last months' rent in advance, which was done. The part-time helper is owed \$420 at April 30, 2014, for unpaid wages. At April 30, 2014, customers owe Kaffen Company \$540 for services they have received but have not yet paid for.

***Instructions***

- (a) Prepare an accrual-basis income statement for the 6 months ended April 30, 2014.
- (b) Prepare the April 30, 2014, classified balance sheet.

**E4-7**

VidGam, a consulting firm, has just completed its first year of operations. The company's sales growth was explosive. To encourage clients to hire its services, VidGam offered 180-day financing—meaning its largest customers do not pay for nearly 6 months. Because VidGam is a new company, its equipment suppliers insist on being paid cash on delivery. Also, it had to pay up front for 2 years of insurance. At the end of the year, VidGam owed employees for one full month of salaries, but due to a cash shortfall, it promised to pay them the first week of next year.

*Identify differences between cash and accrual accounting.*

- (a) Explain how cash and accrual accounting would differ for each of the events listed above and describe the proper accrual accounting.
- (b) Assume that at the end of the year, VidGam reported a favorable net income, yet the company’s management is concerned because the company is very short of cash. Explain how VidGam could have positive net income and yet run out of cash.

**E4-8**

Kwun Company accumulates the following adjustment data at December 31.

*Identify types of adjustments and accounts before adjustment.*

(LO 3, 4, 5), AN

- (a) Services performed but unbilled totals \$600.
- (b) Store supplies of \$160 are on hand. The supplies account shows a \$1,900 balance.
- (c) Utility expenses of \$275 are unpaid.
- (d) Services performed of \$490 collected in advance.
- (e) Salaries of \$620 are unpaid.
- (f) Prepaid insurance totaling \$400 has expired.

**Instructions**

For each item, indicate (1) the type of adjustment (prepaid expense, unearned revenue, accrued revenue, or accrued expense) and (2) the status of the accounts before adjustment (overstated or understated).

**E4-9**

The ledger of Beckett Rental Agency on March 31 of the current year includes the selected accounts below before adjusting entries have been prepared.

*Prepare adjusting entries from selected account data.*

(LO 4, 5), AP

	<u>Debit</u>	<u>Credit</u>
Supplies	\$ 3,000	
Prepaid Insurance	3,600	
Equipment	25,000	
Accumulated Depreciation—Equipment		\$ 8,400
Notes Payable		20,000

	<u>Debit</u>	<u>Credit</u>
Unearned Rent Revenue		12,400
Rent Revenue		60,000
Interest Expense	0	
Salaries and Wages Expense	14,000	

An analysis of the accounts shows the following.

- 1. The equipment depreciates \$280 per month.
- 2. Half of the unearned rent revenue was earned during the quarter.
- 3. Interest of \$400 is accrued on the notes payable.
- 4. Supplies on hand total \$850.
- 5. Insurance expires at the rate of \$400 per month.

### ***Instructions***

Prepare the adjusting entries at March 31, assuming that adjusting entries are made quarterly. Additional accounts are Depreciation Expense, Insurance Expense, Interest Payable, and Supplies Expense.

### **E4-10**

Jim Haight, D.D.S., opened an incorporated dental practice on January 1, 2014. During the first month of operations, the following transactions occurred.

*Prepare adjusting entries.*

### **(LO 4, 5), AP**

- 1. Performed services for patients who had dental plan insurance. At January 31, \$760 of such services was completed but not yet billed to the insurance companies.
- 2. Utility expenses incurred but not paid prior to January 31 totaled \$450.
- 3. Purchased dental equipment on January 1 for \$80,000, paying \$20,000 in cash and signing a \$60,000, 3-year note payable (interest is paid each December 31). The equipment depreciates \$400 per month. Interest is \$500 per month.
- 4. Purchased a 1-year malpractice insurance policy on January 1 for \$24,000.
- 5. Purchased \$1,750 of dental supplies (recorded as increase to Supplies). On January 31, determined that \$550 of supplies were on hand.

### ***Instructions***

Prepare the adjusting entries on January 31. Account titles are Accumulated Depreciation—Equipment, Depreciation Expense, Service Revenue, Accounts Receivable, Insurance Expense, Interest Expense, Interest Payable, Prepaid Insurance, Supplies, Supplies Expense, Utilities Expense, and Accounts Payable.

**E4-11** PRINTED BY: jromero0950@email.phoenix.edu. Printing is for personal, private use only. No part of this book may be reproduced or transmitted without publisher's prior permission. Violators will be prosecuted. The unadjusted trial balance for Sierra Corp. is shown in [Illustration 4-4 \(page 168\)](#). Instead of the adjusting entries shown in the text at October 31, assume the following adjustment data.

*Prepare adjusting entries.*

(LO 4, 5), AP

- 1. Supplies on hand at October 31 total \$500.
- 2. Expired insurance for the month is \$100.
- 3. Depreciation for the month is \$75.
- 4. As of October 31, services worth \$800 related to the previously recorded unearned revenue had been performed.
- 5. Services performed but unbilled (and no receivable has been recorded) at October 31 are \$280.
- 6. Interest expense accrued at October 31 is \$70.
- 7. Accrued salaries at October 31 are \$1,400.

### ***Instructions***

Prepare the adjusting entries for the items above.

### **E4-12**

The income statement of Garska Co. for the month of July shows net income of \$2,000 based on Service Revenue \$5,500; Salaries and Wages Expense \$2,100; Supplies Expense \$900; and Utilities Expense \$500. In reviewing the statement, you discover the following:

*Prepare a correct income statement.*

(LO 1, 4, 5, 6), AP



- 1. Insurance expired during July of \$350 was omitted.
- 2. Supplies expense includes \$200 of supplies that are still on hand at July 31.
- 3. Depreciation on equipment of \$150 was omitted.
- 4. Accrued but unpaid wages at July 31 of \$360 were not included.
- 5. Services performed but unrecorded totaled \$700.

### ***Instructions***

Prepare a correct income statement for July 2014.

### **E4-13**

This is a partial adjusted trial balance of Barone Company.

*Analyze adjusted data.*

(LO 1, 4, 5, 6), AN



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**BARONE COMPANY**

**Adjusted Trial Balance**

**January 31, 2014**

	<u>Debit</u>	<u>Credit</u>
Supplies	\$ 700	
Prepaid Insurance	1,560	
Salaries and Wages Payable		\$1,060
Unearned Service Revenue		750
Supplies Expense	950	
Insurance Expense	520	
Salaries and Wages Expense	1,800	
Service Revenue		4,000

***Instructions***

Answer these questions, assuming the year begins January 1.

- (a) If the amount in Supplies Expense is the January 31 adjusting entry, and \$300 of supplies was purchased in January, what was the balance in Supplies on January 1?
- (b) If the amount in Insurance Expense is the January 31 adjusting entry, and the original insurance premium was for 1 year, what was the total premium and when was the policy purchased?
- (c) If \$2,500 of salaries was paid in January, what was the balance in Salaries and Wages Payable at December 31, 2013?
- (d) If \$1,800 was received in January for services performed in January, what was the balance in Unearned Service Revenue at December 31, 2013?

PRINTED BY: jromer00950@email.phoenix.edu. Printing is for personal, private use only. No part of this book may be reproduced or transmitted without publisher's prior permission. Violators will be prosecuted. Prepare closing entries.

(LO 7), AP

**Instructions**

Prepare the closing entries at January 31, 2014.

**E4-15**

Selected accounts of Castle Company are shown here.

Journalize basic transactions and adjusting entries.

(LO 4, 5, 6), AN

**Supplies Expense**

July 31      750

**Salaries and Wages Payable**

July 31      1,000

**Salaries and Wages Expense**

July 15      1,000

31            1,000

**Accounts Receivable**

July 31      500

**Service Revenue**

July 14      3,800

31            900

31            500

**Unearned Service Revenue**

July 31      900      July 1      Bal. 1,500

20            600

**Supplies**

July 1      Bal. 1,100

10            200

July 31      750

**Instructions**

After analyzing the accounts, journalize (a) the July transactions and (b) the adjusting entries that were made on July 31. (Hint: July transactions were for cash.)

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**E4-16**

The trial balances shown below are before and after adjustment for Bere Company at the end of its fiscal year.

Prepare adjusting entries from analysis of trial balance.

(LO 4, 5, 6), AP



**BERE COMPANY**

**Trial Balance**

**August 31, 2014**

	Before Adjustment		After Adjustment	
	<u>Dr.</u>	<u>Cr.</u>	<u>Dr.</u>	<u>Cr.</u>
Cash	\$10,900		\$10,900	
Accounts Receivable	8,800		9,400	
Supplies	2,500		500	
Prepaid Insurance	4,000		2,500	
Equipment	16,000		16,000	
Accumulated Depreciation—Equipment		\$ 3,600		\$ 4,800
Accounts Payable		5,800		5,800
Salaries and Wages Payable		0		1,100

**BERE COMPANY**

**Trial Balance**

**August 31, 2014**

	Before Adjustment		After Adjustment	
	<u>Dr.</u>	<u>Cr.</u>	<u>Dr.</u>	<u>Cr.</u>
Unearned Rent Revenue		1,800		800
Common Stock		10,000		10,000
Retained Earnings		5,500		5,500
Dividends	2,800		2,800	
Service Revenue		34,000		34,600
Rent Revenue		12,100		13,100
Salaries and Wages Expense	17,000		18,100	
Supplies Expense	0		2,000	
Rent Expense	10,800		10,800	
Insurance Expense	0		1,500	
Depreciation Expense	<u>0</u>	<u>—</u>	<u>1,200</u>	<u>—</u>
	\$72,800	\$72,800	\$75,700	\$75,700

***Instructions***

Prepare the adjusting entries that were made.

**E4-17** PRINTED BY: jromero0950@email.phoenix.edu. Printing is for personal, private use only. No part of this book may be reproduced or transmitted without publisher's prior permission. Violators will be prosecuted. The adjusted trial balance for Bere Company is given in E4-16.

Prepare financial statements from adjusted trial balance.

(LO 6), AP

**Instructions**

Prepare the income and retained earnings statements for the year and the classified balance sheet at August 31.

**E4-18**

The adjusted trial balance for Bere Company is given in E4-16.

Prepare closing entries.

(LO 7), AP

**Instructions**

Prepare the closing entries for the temporary accounts at August 31.

## Exercises: Set B and Challenge Exercises

Visit the book's companion website, at [www.wiley.com/college/kimmel](http://www.wiley.com/college/kimmel), and choose the Student Companion site to access Exercise Set B and Challenge Exercises.

## Problems: Set A

**P4-1A**

The following selected data are taken from the comparative financial statements of American Curling Club. The club prepares its financial statements using the accrual basis of accounting.

Record transactions on accrual basis; convert revenue to cash receipts.

(LO 2, 4, 9), AP

September 30	<u>2014</u>	<u>2013</u>
-----		
Accounts receivable for member dues	\$ 15,000	\$ 19,000
Unearned sales revenue	<del>20,000</del> <u>2014</u>	<del>23,000</del> <u>2013</u>
-----		
Service revenue (from member dues)	151,000	135,000

Dues are billed to members based upon their use of the club's facilities. Unearned sales revenues arise from the sale of tickets to events, such as the Skins Game.

*Instructions*

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(*Hint: You will find it helpful to use T-accounts to analyze the following data. You must analyze these data sequentially, as missing information must first be deduced before moving on. Post your journal entries as you progress, rather than waiting until the end.*)

- (a) Prepare journal entries for each of the following events that took place during 2014.
  - 1. Dues receivable from members from 2013 were all collected during 2014.
  - 2. During 2014, goods were provided for all of the unearned sales revenue at the end of 2013.
  - 3. Additional tickets were sold for \$44,000 cash during 2014; a portion of these were used by the purchasers during the year. The entire balance remaining in Unearned Sales Revenue relates to the upcoming Skins Game in 2014.
  - 4. Dues for the 2013–2014 fiscal year were billed to members.
  - 5. Dues receivable for 2014 (i.e., those billed in item (4) above) were partially collected.
- (b) Determine the amount of cash received by American from the above transactions during the year ended September 30, 2014.

(b) Cash received                      \$199,000

*Prepare adjusting entries, post to ledger accounts, and prepare an adjusted trial balance.*

(LO 4, 5, 6), AP



**P4-2A**

Ken Lumas started his own consulting firm, Lumas Consulting, on June 1, 2014. The trial balance at June 30 is as follows.

**LUMAS CONSULTING**

**Trial Balance**

**June 30, 2014**

	<u>Debit</u>	<u>Credit</u>
Cash	\$ 6,850	
Accounts Receivable	7,000	
Supplies	2,000	

**LUMAS CONSULTING**

**Trial Balance**

**June 30, 2014**

	<u>Debit</u>	<u>Credit</u>
Prepaid Insurance	2,880	
Equipment	15,000	
Accounts Payable		\$ 4,230
Unearned Service Revenue		5,200
Common Stock		22,000
Service Revenue		8,300
Salaries and Wages Expense	4,000	
Rent Expense	<u>2,000</u>	—
	\$39,730	\$39,730

In addition to those accounts listed on the trial balance, the chart of accounts for Lumas also contains the following accounts: Accumulated Depreciation—Equipment, Salaries and Wages Payable, Depreciation Expense, Insurance Expense, Utilities Expense, and Supplies Expense.

Other data:

- 1. Supplies on hand at June 30 total \$720.
- 2. A utility bill for \$180 has not been recorded and will not be paid until next month.
- 3. The insurance policy is for a year.
- 4. Services were performed for \$4,100 of unearned service revenue by the end of the month.
- 5. Salaries of \$1,250 are accrued at June 30.
- 6. The equipment has a 5-year life with no salvage value and is being depreciated at \$250 per month for 60 months.
- 7. Invoices representing \$3,900 of services performed during the month have not been recorded as of June 30.

***Instructions***

- (a) Prepare the adjusting entries for the month of June.
- (b) Post the adjusting entries to the ledger accounts. Enter the totals from the trial balance as beginning account balances. (Use T-accounts.)
- (b) Service rev. \$16,300

- (c) Prepare an adjusted trial balance at June 30, 2014.

(c) Tot. trial balance \$45,310

**P4-3A**

The Solo Hotel opened for business on May 1, 2014. Here is its trial balance before adjustment on May 31.

*Prepare adjusting entries, adjusted trial balance, and financial statements.*

(LO 4, 5, 6, 7), AP



**SOLO HOTEL**  
**Trial Balance**  
**May 31, 2014**

	<u>Debit</u>	<u>Credit</u>
Cash	\$ 2,500	
Supplies	2,600	
Prepaid Insurance	1,800	
Land	15,000	
Buildings	70,000	
Equipment	16,800	
Accounts Payable		\$ 4,700
Unearned Rent Revenue		3,300

SOLO HOTEL

Trial Balance

May 31, 2014

	<u>Debit</u>	<u>Credit</u>
Mortgage Payable		36,000
Common Stock		60,000
Rent Revenue		9,000
Salaries and Wages Expense	3,000	
Utilities Expense	800	
Advertising Expense	<u>500</u>	<u>    </u>
	\$113,000	\$113,000

Other data:

- 1. Insurance expires at the rate of \$450 per month.
- 2. A count of supplies shows \$1,050 of unused supplies on May 31.
- 3. Annual depreciation is \$3,600 on the building and \$3,000 on equipment.
- 4. The mortgage interest rate is 6%. (The mortgage was taken out on May 1.)
- 5. Unearned rent of \$2,500 has been earned.
- 6. Salaries of \$900 are accrued and unpaid at May 31.

**Instructions**

- (a) Journalize the adjusting entries on May 31.
- (b) Prepare a ledger using T-accounts. Enter the trial balance amounts and post the adjusting entries.
- (c) Prepare an adjusted trial balance on May 31.

(c) Rent revenue \$11,500

Tot. adj. trial balance \$114,630

- (d) Prepare an income statement and a retained earnings statement for the month of May and a classified balance sheet at May 31.

- (e) Identify which accounts should be closed on May 31.

**P4-4A**

Wolf Creek Golf Inc. was organized on July 1, 2014. Quarterly financial statements are prepared. The trial balance and adjusted trial balance on September 30 are shown here.

*Prepare adjusting entries and financial statements; identify accounts to be closed.*

(LO 4, 5, 6, 7), AP



**WOLF CREEK GOLF INC.**

**Trial Balance**

**September 30, 2014**

	Unadjusted		Adjusted	
	<u>Dr.</u>	<u>Cr.</u>	<u>Dr.</u>	<u>Cr.</u>
Cash	\$ 6,700		\$ 6,700	
Accounts Receivable	400		1,000	
Supplies	1,200		180	
Prepaid Rent	1,800		900	
Equipment	15,000		15,000	
Accumulated Depreciation—Equipment				\$ 350
Notes Payable		\$ 5,000		5,000
Accounts Payable		1,070		1,070

**WOLF CREEK GOLF INC.**

**Trial Balance**

**September 30, 2014**

	<b>Unadjusted</b>		<b>Adjusted</b>	
	<u><b>Dr.</b></u>	<u><b>Cr.</b></u>	<u><b>Dr.</b></u>	<u><b>Cr.</b></u>
Salaries and Wages Payable			600	
Interest Payable			50	
Unearned Rent Revenue		1,000	800	
Common Stock		14,000	14,000	
Retained Earnings		0	0	
Dividends	600		600	
Service Revenue		14,100	14,700	
Rent Revenue		700	900	
Salaries and Wages Expense	8,800		9,400	
Rent Expense	900		1,800	
Depreciation Expense			350	
Supplies Expense			1,020	
Utilities Expense	470		470	

WOLF CREEK GOLF INC.

Trial Balance

September 30, 2014

	Unadjusted		Adjusted	
	<u>Dr.</u>	<u>Cr.</u>	<u>Dr.</u>	<u>Cr.</u>
Interest Expense	—	—	<u>50</u>	—
	\$35,870	\$35,870	\$37,470	\$37,470

**Instructions**

- (a) Journalize the adjusting entries that were made.
- (b) Prepare an income statement and a retained earnings statement for the 3 months ending September 30 and a classified balance sheet at September 30.

(b) Net income                      \$2,510

Tot. assets                              \$23,430

- (c) Identify which accounts should be closed on September 30.
- (d) If the note bears interest at 12%, how many months has it been outstanding?

**P4-5A**

A review of the ledger of Dempsey Company at December 31, 2014, produces these data pertaining to the preparation of annual adjusting entries.

*Prepare adjusting entries.*

**(LO 4, 5), AP**

- 1. Prepaid Insurance \$15,200. The company has separate insurance policies on its buildings and its motor vehicles. Policy B4564 on the building was purchased on July 1, 2013, for \$9,600. The policy has a term of 3 years. Policy A2958 on the vehicles was purchased on January 1, 2014, for \$7,200. This policy has a term of 18 months.
- 2. Unearned Rent Revenue \$429,000. The company began subleasing office space in its new building on November 1. At December 31, the company had the following rental contracts that are paid in full for the entire term of the lease.

2. Rent revenue                              \$84,000

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<b>Date</b>	<b>Term (in months)</b>	<b>Monthly Rent</b>	<b>Number of Leases</b>
Nov. 1	9	\$5,000	5
Dec. 1	6	\$8,500	4

- 3. Notes Payable \$40,000. This balance consists of a note for 6 months at an annual interest rate of 7%, dated October 1.
- 4. Salaries and Wages Payable \$0. There are eight salaried employees. Salaries are paid every Friday for the current week. Five employees receive a salary of \$600 each per week, and three employees earn \$700 each per week. Assume December 31 is a Wednesday. Employees do not work weekends. All employees worked the last 3 days of December.

### ***Instructions***

Prepare the adjusting entries at December 31, 2014.

### **P4-6A**

Astromech Travel Court was organized on July 1, 2013, by Jessica Browning. Jessica is a good manager but a poor accountant. From the trial balance prepared by a part-time bookkeeper, Jessica prepared the following income statement for her fourth quarter, which ended June 30, 2014.

*Prepare adjusting entries and a corrected income statement.*

(LO 4, 5), AN

## **ASTROMECH TRAVEL COURT**

### **Income Statement**

**For the Quarter Ended June 30, 2014**

#### Revenues

Rent revenue \$212,000

#### Operating expense

Advertising expense \$ 3,800

Salaries and wages expense 80,500

**ASTROMECH TRAVEL COURT**

**Income Statement**

**For the Quarter Ended June 30, 2014**

Utilities expense	900	
Depreciation expense	2,700	
Maintenance and repairs expense	<u>4,300</u>	
Total operating expenses		<u>92,200</u>
Net income		\$119,800

Jessica suspected that something was wrong with the statement because net income had never exceeded \$30,000 in any one quarter. Knowing that you are an experienced accountant, she asks you to review the income statement and other data.

You first look at the trial balance. In addition to the account balances reported above in the income statement, the trial balance contains the following additional selected balances at June 30, 2014.

Supplies	\$ 8,200
Prepaid Insurance	14,400
Notes Payable	14,000

You then make inquiries and discover the following.

- 1. Travel court rental revenues include advanced rental payments received for summer occupancy, in the amount of \$57,000.
- 2. There were \$1,800 of supplies on hand at June 30.
- 3. Prepaid insurance resulted from the payment of a one-year policy on April 1, 2014.
- 4. The mail in July 2014 brought the following bills: advertising for the week of June 24, \$110; repairs made June 18, \$4,450; and utilities for the month of June, \$215.
- 5. There are three employees who receive wages that total \$300 per day. At June 30, four days' wages have been incurred but not paid.
- 6. The note payable is a 6% note dated May 1, 2014, and due on July 31, 2014.
- 7. Income tax of \$13,400 for the quarter is due in July but has not yet been recorded.

***Instructions***

(b) Net income \$33,285

- (c) Explain to Jessica the generally accepted accounting principles that she did not recognize in preparing her income statement and their effect on her results.

**P4-7A**

On November 1, 2014, the following were the account balances of Rijo Equipment Repair.

*Journalize transactions and follow through accounting cycle to preparation of financial statements.*

(LO 4, 5, 6), AP



	<u>Debit</u>		<u>Credit</u>
Cash	\$ 2,790	Accumulated Depreciation—Equipment	\$ 500
Accounts Receivable	2,910	Accounts Payable	2,300
Supplies	1,120	Unearned Service Revenue	400
Equipment	10,000	Salaries and Wages Payable	620
		Common Stock	10,000
	—	Retained Earnings	<u>3,000</u>
	\$16,820		\$16,820

During November, the following summary transactions were completed.

- Nov. 8 Paid \$1,220 for salaries due employees, of which \$600 is for November and \$620 is for October salaries payable.
- 10 Received \$1,800 cash from customers in payment of account.
- 12 Received \$3,700 cash for services performed in November.

- 17 Purchased supplies on account \$1,300.
- 20 Paid creditors \$2,500 of accounts payable due.
- 22 Paid November rent \$480.
- 25 Paid salaries \$1,000.
- 27 Performed services on account worth \$900 and billed customers.
- 29 Received \$750 from customers for services to be provided in the future.

Adjustment data:

- 1. Supplies on hand are valued at \$1,100.
- 2. Accrued salaries payable are \$480.
- 3. Depreciation for the month is \$250.
- 4. Services were performed to satisfy \$500 of unearned service revenue.

### ***Instructions***

- (a) Enter the November 1 balances in the ledger accounts. (Use T-accounts.)
- (b) Journalize the November transactions.
- (c) Post to the ledger accounts. Use Service Revenue, Depreciation Expense, Supplies Expense, Salaries and Wages Expense, and Rent Expense.
- (d) Prepare a trial balance at November 30.
- (e) Journalize and post adjusting entries.
- (f) Prepare an adjusted trial balance.

(f) Cash \$3,840

Tot. adj. trial balance \$24,680

- (g) Prepare an income statement and a retained earnings statement for November and a classified balance sheet at November 30.

(g) Net income \$970

### **P4-8A**

Mike Greenberg opened Clean Window Washing Inc. on July 1, 2014. During July, the following transactions were completed.

*Complete all steps in accounting cycle.*



- July 1 Issued 12,000 shares of common stock for \$12,000 cash.
- 1 Purchased used truck for \$8,000, paying \$2,000 cash and the balance on account.
- 3 Purchased cleaning supplies for \$900 on account.
- 5 Paid \$1,800 cash on a 1-year insurance policy effective July 1.
- 12 Billed customers \$3,700 for cleaning services.
- 18 Paid \$1,000 cash on amount owed on truck and \$500 on amount owed on cleaning supplies.
- 20 Paid \$2,000 cash for employee salaries.
- 21 Collected \$1,600 cash from customers billed on July 12.
- 25 Billed customers \$2,500 for cleaning services.
- 31 Paid \$290 for maintenance of the truck during month.
- 31 Declared and paid \$600 cash dividend.

The chart of accounts for Clean Window Washing contains the following accounts: Cash, Accounts Receivable, Supplies, Prepaid Insurance, Equipment, Accumulated Depreciation—Equipment, Accounts Payable, Salaries and Wages Payable, Common Stock, Retained Earnings, Dividends, Income Summary, Service Revenue, Maintenance and Repairs Expense, Supplies Expense, Depreciation Expense, Insurance Expense, Salaries and Wages Expense.

**Instructions**

- (a) Journalize the July transactions.
- (b) Post to the ledger accounts. (Use T-accounts.)
- (c) Prepare a trial balance at July 31.
- (d) Journalize the following adjustments.
  - (1) Services performed but unbilled and uncollected at July 31 were \$1,700.
  - (2) Depreciation on equipment for the month was \$180.
  - (3) One-twelfth of the insurance expired.
  - (4) An inventory count shows \$320 of cleaning supplies on hand at July 31.
  - (5) Accrued but unpaid employee salaries were \$400.
- (e) Post adjusting entries to the T-accounts.

(f) Prepare an adjusted trial balance.  
(f) Cash \$5,410

- (g) Prepare the income statement and a retained earnings statement for July and a classified balance sheet at July 31.

(g) Tot. assets \$21,500

- (h) Journalize and post closing entries and complete the closing process.
- (i) Prepare a post-closing trial balance at July 31.

## Problems: Set B

### P4-1B

The following data are taken from the comparative balance sheets of Golfview Inn, which prepares its financial statements using the accrual basis of accounting.

December 31	2014	2013
Accounts receivable for member fees	\$18,000	\$20,000
Unearned service revenue	17,000	10,000

Fees are billed to members based upon their use of the club's facilities. Unearned service revenues arise from the sale of gift certificates, which members can apply to their future use of club facilities. The 2014 income statement for the club showed that service revenue of \$190,000 was recognized during the year.

*Record transactions on accrual basis; convert revenue to cash receipts.*

**(LO 2, 4, 9), AP**

### Instructions

*(Hint: You will find it helpful to use T-accounts to analyze these data.)*

- (a) Prepare journal entries for each of the following events that took place during 2014.
  - 1. Fees receivable from 2013 were all collected during 2014.
  - 2. Gift certificates outstanding at the end of 2013 were all redeemed during 2014.
  - 3. An additional \$40,000 worth of gift certificates were sold during 2014; a portion of these were used by the recipients during the year; the remainder were still outstanding at the end of 2014.
  - 4. Fees for 2014 were billed to members.
  - 5. Fees receivable for 2014 (i.e., those billed in item (4) above) were partially collected.
- (b) Determine the amount of cash received by the club with respect to fees during 2014.

(b) Cash received \$199,000

*Prepare adjusting entries, post to ledger accounts, and prepare an adjusted trial balance.*

Pat Okendo started her own consulting firm, Okendo Consulting, on May 1, 2014. The trial balance at May 31 is as shown on the next page.

### OKENDO CONSULTING

#### Trial Balance

May 31, 2014

	<u>Debit</u>	<u>Credit</u>
Cash	\$ 7,500	
Accounts Receivable	3,000	
Supplies	2,500	
Prepaid Insurance	3,600	
Equipment	12,000	
Accounts Payable		\$ 3,500
Unearned Service Revenue		4,000
Common Stock		19,100
Service Revenue		7,500
Salaries and Wages Expense	4,000	
Rent Expense	<u>1,500</u>	—
	\$34,100	\$34,100

In addition to those accounts listed on the trial balance, the chart of accounts for Okendo Consulting also contains the following accounts: Accumulated Depreciation—Equipment, Salaries and Wages Payable, Depreciation Expense,

Other data:

- 1. \$1,000 of supplies have been used during the month.
- 2. Utility costs incurred but not paid are \$300.
- 3. The insurance policy is for 3 years.
- 4. \$1,500 of the balance in the Unearned Service Revenue account remains unearned at the end of the month.
- 5. Assume May 31 is a Tuesday and employees are paid on Fridays. Okendo Consulting has two employees that are paid \$600 each for a 5-day work week.
- 6. The equipment has a 5-year life with no salvage value and is being depreciated at \$200 per month for 60 months.
- 7. Invoices representing \$1,500 of services performed during the month have not been recorded as of May 31.

**Instructions**

- (a) Prepare the adjusting entries for the month of May.
- (b) Post the adjusting entries to the ledger accounts. Enter the totals from the trial balance as beginning account balances. (Use T-accounts.)
- (c) Prepare an adjusted trial balance at May 31, 2014.

(c) Tot. trial balance                      \$36,580

**P4-3B**

Death Valley Resort opened for business on June 1 with eight air-conditioned units. Its trial balance before adjustment on August 31 is presented here.

*Prepare adjusting entries, adjusted trial balance, and financial statements.*

(LO 4, 5, 6, 7), AP



**DEATH VALLEY RESORT**

**Trial Balance**

**August 31, 2014**

	<u>Debit</u>	<u>Credit</u>
Cash	\$ 24,600	
Supplies	4,300	
Prepaid Insurance	5,400	

**DEATH VALLEY RESORT**

**Trial Balance**

**August 31, 2014**

	<u>Debit</u>	<u>Credit</u>
Land	40,000	
Buildings	132,000	
Equipment	36,000	
Accounts Payable		\$ 6,500
Unearned Rent Revenue		6,800
Mortgage Payable		120,000
Common Stock		100,000
Dividends	5,000	
Rent Revenue		80,000
Salaries and Wages Expense	53,000	
Utilities Expense	9,400	
Maintenance and Repairs Expense	<u>3,600</u>	<u>      </u>
	\$313,300	\$313,300

Other data:

- 1. Insurance expires at the rate of \$500 per month.
- 2. A count of supplies on August 31 shows \$900 of supplies on hand.



ABDULLA ADVERTISING AGENCY

Trial Balance

December 31, 2014

	Unadjusted		Adjusted	
	<u>Dr.</u>	<u>Cr.</u>	<u>Dr.</u>	<u>Cr.</u>
Prepaid Insurance	3,350		1,790	
Equipment	60,000		60,000	
Accumulated Depreciation—Equipment		\$ 25,000		\$ 30,000
Notes Payable		8,000		8,000
Accounts Payable		2,000		2,000
Interest Payable		0		560
Unearned Service Revenue		5,000		3,100
Salaries and Wages Payable		0		820
Common Stock		20,000		20,000
Retained Earnings		5,500		5,500
Dividends	10,000		10,000	
Service Revenue		57,600		62,500
Salaries and Wages Expense	9,000		9,820	

ABDULLA ADVERTISING AGENCY

Trial Balance

December 31, 2014

	Unadjusted		Adjusted	
	<u>Dr.</u>	<u>Cr.</u>	<u>Dr.</u>	<u>Cr.</u>
Insurance Expense			1,560	
Interest Expense			560	
Depreciation Expense			5,000	
Supplies Expense			2,400	
Rent Expense	<u>4,350</u>	<u>    </u>	<u>4,350</u>	<u>    </u>
	\$123,100	\$123,100	\$132,480	\$132,480

**Instructions**

- (a) Journalize the annual adjusting entries that were made.
- (b) Prepare an income statement and a retained earnings statement for the year ended December 31, and a classified balance sheet at December 31.

(b) Net income                      \$38,810

Tot. assets                              \$68,790

- (c) Identify which accounts should be closed on December 31.
- (d) If the note has been outstanding 10 months, what is the annual interest rate on that note?
- (e) If the company paid \$10,000 in salaries in 2014, what was the balance in Salaries and Wages Payable on December 31, 2013?

**P4-5B**

A review of the ledger of Garner Company at December 31, 2014, produces these data pertaining to the preparation of annual adjusting entries.

- 1. Prepaid Insurance \$16,400. The company has separate insurance policies on its buildings and its motor vehicles. Policy B4564 on the building was purchased on January 1, 2013, for \$11,400. The policy has a term of 3 years. Policy A2958 on the vehicles was purchased on July 1, 2014, for \$8,800. This policy has a term of 2 years.
- 2. Unearned Rent Revenue \$450,000. The company began subleasing office space in its new building on November 1. At December 31, the company had the following rental contracts that are paid in full for the entire term of the lease.

<u>Date</u>	<u>Term (in months)</u>	<u>Monthly Rent</u>	<u>Number of Leases</u>
Nov. 1	9	\$6,000	5
Dec. 1	6	\$7,500	4

2. Rent revenue \$90,000

- 3. Notes Payable \$20,000. This balance consists of a note for 8 months at an annual interest rate of 9%, dated August 1.
- 4. Salaries and Wages Payable \$0. There are six salaried employees. Salaries are paid every Friday for the current week. Four employees receive a salary of \$480 each per week, and two employees earn \$600 each per week. December 31 is a Thursday. Employees do not work weekends. All employees worked the last 4 days of December.

**Instructions**

Prepare the adjusting entries at December 31, 2014.

**P4-6B**

Tutors-Plus Test Prep was organized on May 1, 2013, by Jan Cooper. Jan is a good manager but a poor accountant. From the trial balance prepared by a part-time bookkeeper, Jan prepared the following income statement for her fourth quarter, which ended April 30, 2014.

Prepare adjusting entries and a corrected income statement.

(LO 4, 5) AN

**TUTORS-PLUS TEST PREP**  
**Income Statement**  
**For the Quarter Ended April 30, 2014**

Revenues

Service revenue	\$240,000
-----------------	-----------

**TUTORS-PLUS TEST PREP**

**Income Statement**

**For the Quarter Ended April 30, 2014**

Operating expenses

Advertising expense	\$ 6,400	
Salaries and wages expense	92,000	
Utilities expense	1,300	
Depreciation expense	2,400	
Maintenance and repairs expense	<u>1,700</u>	
Total operating expenses		<u>103,800</u>
Net income		\$136,200

Jan suspected that something was wrong with the statement because net income had never exceeded \$40,000 in any one quarter. Knowing that you are an experienced accountant, she asks you to review the income statement and other data.

You first look at the trial balance. In addition to the account balances reported above in the income statement, the ledger contains the following additional selected balances at April 30, 2014.

Supplies	\$ 9,800
Prepaid Insurance	12,000
Notes Payable	15,000

You then make inquiries and discover the following.

- 1. Service revenue includes advance payments received for summer classes, in the amount of \$75,000.
- 2. There were \$2,600 of supplies on hand at April 30.
- 3. Prepaid insurance resulted from the payment of a one-year policy on February 1, 2014.

4. The mail in May 2014 brought the following bills: advertising for the week of April 24, \$80; repairs made April 18, \$2,560; and utilities for the month of April, \$530.

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- 5. There are six employees who receive wages that total \$1,380 per day. At April 30, three days' wages have been incurred but not paid.
  - 6. The note payable is a 8% note dated February 1, 2014, and due on May 31, 2014.
  - 7. Income tax of \$15,200 for the quarter is due in May but has not yet been recorded.

**Instructions**

- (a) Prepare any adjusting journal entries required as at April 30, 2014.
- (b) Prepare a correct income statement for the quarter ended April 30, 2014.

(b) Net income                      \$28,190

- (c) Explain to Jan the generally accepted accounting principles that she did not recognize in preparing her income statement and their effect on her results.

**P4-7B**

On August 1, 2014, the following were the account balances of D&D Repair Services.

*Journalize transactions and follow through accounting cycle to preparation of financial statements.*

(LO 4, 5, 6), AP



	<u>Debit</u>		<u>Credit</u>
Cash	\$ 6,040	Accumulated Depreciation—Equipment	\$ 600
Accounts Receivable	2,910	Accounts Payable	2,300
Supplies	1,030	Unearned Service Revenue	1,260
Equipment	10,000	Salaries and Wages Payable	1,420
		Common Stock	10,000
	—	Retained Earnings	<u>4,400</u>
	\$19,980		\$19,980

During August, the following summary transactions were completed.

Aug 5 Received \$1,200 cash from customers in payment of account.

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10 Paid \$3,120 for salaries due employees, of which \$1,700 is for August and \$1,420 is for July salaries payable.

12 Received \$2,800 cash for services performed in August.

15 Purchased store equipment on account \$2,000.

17 Purchased supplies on account \$860.

20 Paid creditors \$2,000 of accounts payable due.

22 Paid August rent \$380.

25 Paid salaries \$2,900.

27 Performed services worth \$3,130 on account and billed customers.

29 Received \$780 from customers for services to be provided in the future.

Adjustment data:

- 1. Supplies on hand are valued at \$960.
- 2. Accrued salaries payable are \$1,540.
- 3. Depreciation for the month is \$320.
- 4. Services were performed to satisfy \$800 of unearned service revenue.

### ***Instructions***

- (a) Enter the August 1 balances in the ledger accounts. (Use T-accounts.)
- (b) Journalize the August transactions.
- (c) Post to the ledger accounts. Use Service Revenue, Depreciation Expense, Supplies Expense, Salaries and Wages Expense, and Rent Expense.
- (d) Prepare a trial balance at August 31.
- (e) Journalize and post adjusting entries.
- (f) Prepare an adjusted trial balance.

(f) Cash \$2,420

Tot. adj. trial balance \$27,990

- (g) Prepare an income statement and a retained earnings statement for August and a classified balance sheet at August 31.

(g) Net loss \$1,040

Geog Lav opened Geog Cleaners on March 1, 2014. During March, the following transactions were completed.

*Complete all steps in accounting cycle.*

(LO 4, 5, 6, 7, 8), AP



- Mar. 1 Issued 10,000 shares of common stock for \$15,000 cash.
  
- 1 Purchased used truck for \$8,000, paying \$3,000 cash and the balance on account.
  
- 3 Purchased cleaning supplies for \$2,000 on account.
  
- 5 Paid \$2,400 cash on a 6-month insurance policy effective March 1.
  
- 14 Billed customers \$3,700 for cleaning services.
  
- 18 Paid \$1,500 cash on amount owed on truck and \$500 on amount owed on cleaning supplies.
  
- 20 Paid \$1,750 cash for employee salaries.
  
- 21 Collected \$1,600 cash from customers billed on March 14.
  
- 28 Billed customers \$4,200 for cleaning services.
  
- 31 Paid \$350 for gas and oil used in truck during month (use Maintenance and Repairs Expense).
  
- 31 Declared and paid a \$900 cash dividend.

The chart of accounts for Geog Cleaners contains the following accounts: Cash, Accounts Receivable, Supplies, Prepaid Insurance, Equipment, Accumulated Depreciation—Equipment, Accounts Payable, Salaries and Wages Payable, Common Stock, Retained Earnings, Dividends, Income Summary, Service Revenue, Maintenance and Repairs Expense, Supplies Expense, Depreciation Expense, Insurance Expense, Salaries and Wages Expense.

***Instructions***

- (a) Journalize the March transactions.
- (b) Post to the ledger accounts. (Use T-accounts.)





- Dec.  
1 Natalie hires an assistant at an hourly wage of \$8 to help with cookie making and some administrative duties.
- 5 Natalie teaches the class that was booked on November 25. The balance outstanding is received.
- 8 Cookie Creations receives a check for the amount due from the neighborhood school for the class given on November 30.
- 9 Cookie Creations receives \$750 in advance from the local school board for five classes that the company will give during December and January.
- 15 Pays the cell phone invoice outstanding at November 30.
- 16 Issues a check to Natalie's brother for the amount owed for the design of the website.
- 19 Receives a deposit of \$60 on a cookie class scheduled for early January.
- 23 Additional revenue during the month for cookie-making classes amounts to \$4,000. (Natalie has not had time to account for each class individually.) \$3,000 in cash has been collected and \$1,000 is still outstanding. (This is in

- 23 Additional baking supplies purchased during the month for sugar, flour, and chocolate chips amount to \$1,250 cash.
- 23 Issues a check to Natalie's assistant for \$800. Her assistant worked approximately 100 hours from the time in which she was hired until December 23.
- 28 Pays a dividend of \$500 to the common shareholder (Natalie).

As of December 31, Cookie Creations' year-end, the following adjusting entry data are provided.

- 1. A count reveals that \$45 of brochures and posters were used.
- 2. Depreciation is recorded on the baking equipment purchased in November. The baking equipment has a useful life of 5 years. Assume that 2 months' worth of depreciation is required.
- 3. Amortization (which is similar to depreciation) is recorded on the website. (Credit the Website account directly for the amount of the amortization.) The website is amortized over a useful life of 2 years and was available for use on December 1.
- 4. Interest on the note payable is accrued. (Assume that 1.5 months of interest accrued during November and December.) Round to the nearest dollar.
- 5. One month's worth of insurance has expired.
- 6. Natalie is unexpectedly telephoned on December 28 to give a cookie class at the neighborhood community center on December 31. In early January, Cookie Creations sends an invoice for \$450 to the community center.
- 7. A count reveals that \$1,025 of baking supplies were used.
- 8. A cell phone invoice is received for \$75. The invoice is for services provided during the month of December and is due on January 15.
- 9. Because the unexpected cookie-making class on December 31 was for such a large group of children, Natalie's assistant helps out. Her assistant worked 7 hours at a rate of \$8 per hour.
- 10. An analysis of the Unearned Service Revenue account reveals that two of the five classes paid for by the local school board on December 9 still have not been taught by the end of December. The \$60 deposit received on December 19 for another class also remains unearned.

### ***Instructions***

Using the information that you have gathered and the general ledger accounts that you have prepared through [Chapter 3](#), plus the new information above, do the following.

- (a) Journalize the above transactions.
- (b) Post the December transactions. (Use the general ledger accounts prepared in [Chapter 3](#).)
- (c) Prepare a trial balance at December 31, 2014.

(c) Totals                    \$8,160

- (d) Prepare and post adjusting journal entries for the month of December.
- (e) Prepare an adjusted trial balance as of December 31, 2014.

(e) Totals                    \$8,804

- (f) Prepare an income statement and a retained earnings statement for the 2-month period ending December 31, 2014, and a classified balance sheet as of December 31, 2014.

(f) Net income                \$3,211

(h) Totals \$6,065

## Broadening Your Perspective

### Financial Reporting and Analysis

#### FINANCIAL REPORTING PROBLEM: *Tootsie Roll Industries, Inc.*

##### BYP4-1

The financial statements of *Tootsie Roll* are presented in [Appendix A](#) at the end of this textbook.



##### Instructions

- (a) Using the consolidated income statement and balance sheet, identify items that may result in adjusting entries for deferrals.
- (b) Using the consolidated income statement, identify two items that may result in adjusting entries for accruals.
- (c) What was the amount of depreciation expense for 2011 and 2010? (You will need to examine the notes to the financial statements or the statement of cash flows.) Where was accumulated depreciation reported?
- (d) What was the cash paid for income taxes during 2011, reported at the bottom of the consolidated statement of cash flows? What was income tax expense (provision for income taxes) for 2011?

#### COMPARATIVE ANALYSIS PROBLEM: *Tootsie Roll vs. Hershey*

##### BYP4-2

The financial statements of *The Hershey Company* are presented in [Appendix B](#), following the financial statements for *Tootsie Roll* in [Appendix A](#).



##### Instructions

- (a) Identify two accounts on Hershey's balance sheet that provide evidence that Hershey uses accrual accounting. In each case, identify the income statement account that would be affected by the adjustment process.
- (b) Identify two accounts on Tootsie Roll's balance sheet that provide evidence that Tootsie Roll uses accrual accounting (different from the two you listed for Hershey). In each case, identify the income statement account that would be affected by the adjustment process.

## RESEARCH CASE

**BYP4-3**

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The February 13, 2010, issue of the *Wall Street Journal* includes an article by Scott Thurm entitled "For Some Firms, a Case of 'Quadrophobia'."

### **Instructions**

Read the article and answer the following.

- (a) What method did the study's authors use to determine that companies were "managing" their earnings per share calculation?
- (b) For the average company in the study, how much would the company have to boost earnings in order to increase earnings per share by 1/10 of a cent?
- (c) What examples did the authors cite of accounting adjustments that companies can make to boost net income enough that they can round up to the next highest cent? Why aren't these methods of adjustment considered illegal?
- (d) What is an earnings restatement? What relationship did the authors identify about companies that restate earnings?
- (e) What incentive do companies have to round up their earnings per share to the next highest cent?

## **INTERPRETING FINANCIAL STATEMENTS**

**BYP4-4**

**Laser Recording Systems**, founded in 1981, produces disks for use in the home market. The following is an excerpt from Laser Recording Systems' financial statements (all dollars in thousands).

### **LASER RECORDING SYSTEMS**

#### **Management Discussion**

Accrued liabilities increased to \$1,642 at January 31, from \$138 at the end of the previous fiscal year. Compensation and related accruals increased \$195 due primarily to increases in accruals for severance, vacation, commissions, and relocation expenses. Accrued professional services increased by \$137 primarily as a result of legal expenses related to several outstanding contractual disputes. Other expenses increased \$35, of which \$18 was for interest payable.

### **Instructions**

#### **LASER RECORDING SYSTEMS**

#### **Management Discussion**

- (a) Can you tell from the discussion whether Laser Recording Systems has prepaid its legal expenses and is now making an adjustment to the asset account Prepaid Legal Expenses, or whether the company is handling the legal expense via an accrued expense adjustment?
- (b) Identify each of the adjustments Laser Recording Systems is discussing as one of the four types of possible adjustments discussed in the chapter. How is net income ultimately affected by each of the adjustments?
- (c) What journal entry did Laser Recording make to record the accrued interest?

## **REAL-WORLD FOCUS**

**BYP4-5**

**Purpose:** To learn about the functions of the Securities and Exchange Commission (SEC).

**Address:** [www.sec.gov/about/whatwedo.shtml](http://www.sec.gov/about/whatwedo.shtml), or go to [www.wiley.com/college/kimmel](http://www.wiley.com/college/kimmel)

*Instructions*

PRINTED BY: jromero0950@email.phoenix.edu. Printing is for personal, private use only. No part of this book may be reproduced or transmitted without publisher's prior permission. Violators will be prosecuted. Use the information in this site to answer the following questions.

- (a) What event spurred the creation of the SEC? Why was the SEC created?
- (b) What are the five divisions of the SEC? Briefly describe the purpose of each.
- (c) What are the responsibilities of the chief accountant?

## Critical Thinking

### DECISION-MAKING ACROSS THE ORGANIZATION

#### BYP4-6

Lincoln Park was organized on April 1, 2013, by Judy Tercek. Judy is a good manager but a poor accountant. From the trial balance prepared by a part-time bookkeeper, Judy prepared the following income statement for the quarter that ended March 31, 2014.

#### LINCOLN PARK

#### Income Statement

For the Quarter Ended March 31, 2014

#### Revenues

Rent revenue	\$83,000
--------------	----------

#### Operating expenses

Advertising expense	\$ 4,200
---------------------	----------

Salaries and wages expense	27,600
----------------------------	--------

Utilities expense	1,500
-------------------	-------

Depreciation expense	800
----------------------	-----

Maintenance and repairs expense	<u>2,800</u>
---------------------------------	--------------

Total operating expenses	<u>36,900</u>
--------------------------	---------------

Net income	\$46,100
------------	----------

Judy knew that something was wrong with the statement because net income had never exceeded \$20,000 in any one quarter. Knowing that you are an experienced accountant, she asks you to review the income statement and other data.

You first look at the trial balance. In addition to the account balances reported in the income statement, the ledger contains these selected balances at March 31, 2014.

Supplies	\$ 4,500
Prepaid Insurance	7,200
Notes Payable	20,000

You then make inquiries and discover the following.

- 1. Rent revenue includes advanced rentals for summer-month occupancy, \$21,000.
- 2. There were \$600 of supplies on hand at March 31.
- 3. Prepaid insurance resulted from the payment of a 1-year policy on January 1, 2014.
- 4. The mail on April 1, 2014, brought the following bills: advertising for week of March 24, \$110; repairs made March 10, \$1,040; and utilities \$240.
- 5. There are four employees who receive wages totaling \$290 per day. At March 31, 3 days' wages have been incurred but not paid.
- 6. The note payable is a 3-month, 7% note dated January 1, 2014.

### *Instructions*

With the class divided into groups, answer the following.

- (a) Prepare a correct income statement for the quarter ended March 31, 2014.
- (b) Explain to Judy the generally accepted accounting principles that she did not follow in preparing her income statement and their effect on her results.

## COMMUNICATION ACTIVITY

### **BYP4-7**

On numerous occasions, proposals have surfaced to put the federal government on the accrual basis of accounting. This is no small issue because if this basis were used, it would mean that billions in unrecorded liabilities would have to be booked and the federal deficit would increase substantially.

### *Instructions*

- (a) What is the difference between accrual-basis accounting and cash-basis accounting?
- (b) Comment on why politicians prefer a cash-basis accounting system over an accrual-basis system.
- (c) Write a letter to your senators explaining why you think the federal government should adopt the accrual basis of accounting.

## ETHICS CASE

### **BYP4-8**

Eaton Company is a pesticide manufacturer. Its sales declined greatly this year due to the passage of legislation outlawing the sale of several of Eaton's chemical pesticides. During the coming year, Eaton will have environmentally

safe and competitive replacement chemicals to replace these discontinued products. Sales in the next year are expected to greatly exceed those of any prior year. Therefore, the decline in this year's sales and profits appears to be a one-year aberration.

Even so, the company president believes that a large dip in the current year's profits could cause a significant drop in the market price of Eaton's stock and make it a takeover target. To avoid this possibility, he urges Mark Trane, controller, to accrue every possible revenue and to defer as many expenses as possible in making this period's year-end adjusting entries. The president says to Mark, "We need the revenues this year, and next year we can easily absorb expenses deferred from this year. We can't let our stock price be hammered down!" Mark didn't get around to recording the adjusting entries until January 17, but he dated the entries December 31 as if they were recorded then. Mark also made every effort to comply with the president's request.

### *Instructions*

- (a) Who are the stakeholders in this situation?
- (b) What are the ethical considerations of the president's request and Mark's dating the adjusting entries December 31?
- (c) Can Mark accrue revenues and defer expenses and still be ethical?

## **ALL ABOUT YOU**

### **BYP4-9**

Companies prepare balance sheets in order to know their financial position at a specific point in time. This enables them to make a comparison to their position at previous points in time and gives them a basis for planning for the future. In order to evaluate *your* financial position, you can prepare a personal balance sheet. Assume that you have compiled the following information regarding your finances. (*Hint:* Some of the items might not be used in your personal balance sheet.)

Amount owed on student loan balance (long-term)	\$5,000
Balance in checking account	1,200
Certificate of deposit (6-month)	3,000
Annual earnings from part-time job	11,300
Automobile	7,000
Balance on automobile loan (current portion)	1,500
Balance on automobile loan (long-term portion)	4,000
Home computer	800
Amount owed to you by younger brother	300

Annual tuition	6,400
Video and stereo equipment	1,250
Balance owed on credit card (current portion)	150
Balance owed on credit card (long-term portion)	1,650

### *Instructions*

Prepare a personal balance sheet using the format you have learned for a classified balance sheet for a company. For the equity account, use M. Y. Own, Capital.

## FASB CODIFICATION ACTIVITY

### **BYP4-10**

If your school has a subscription to the FASB Codification, go to <http://aaahq.org/ascLogin.cfm> to log in and prepare responses to the following.

### *Instructions*

Access the glossary (“Master Glossary”) to answer the following.

- (a) What is the definition of revenue?
- (b) What is the definition of compensation?

## Answers to Insight and Accounting Across the Organization Questions

**p. 166 Reporting Revenue Accurately Q:** In the past, why was it argued that Apple should spread the recognition of iPhone revenue over a two-year period, rather than recording it upfront?

**A:** Apple promises to provide software updates over the life of the phone’s use. Because this represents an unfulfilled performance obligation, it was argued that Apple should spread its revenue recognition over a two-year estimated life of the phone.

**p. 167 Cashing In on Accrual Accounting Q:** Accrual accounting is often considered superior to cash accounting. Why, then, were some people critical of China’s use of accrual accounting in this instance? **A:** In this case, some people were critical because, in general, China uses cash accounting. By switching to accrual accounting for this transaction, China was not being consistent in its accounting practices. Lack of consistency reduces the transparency and usefulness of accounting information.

**p. 174 Turning Gift Cards into Revenue Q:** Suppose that Robert Jones purchases a \$100 gift card at Best Buy on December 24, 2013, and gives it to his wife, Mary Jones, on December 25, 2013. On January 3, 2014, Mary uses the card to purchase \$100 worth of CDs. When do you think Best Buy should recognize revenue and why? **A:** According to the revenue recognition principle, companies should recognize revenue when the performance obligation is satisfied. In this case, revenue results when Best Buy provides the goods. Thus, when Best Buy receives cash in exchange for the gift card on December 24, 2013, it should recognize a liability, Unearned Sales Revenue, for \$100.

**p. 180 Got Junk? Q:** What accounting issue might this cause for companies? **A:** The balance sheet should provide a fair representation of what a company owns and what it owes. If significant obligations of the company are not reported on the balance sheet, the company's net worth (its equity) will be overstated. While it is true that it is not possible to estimate the exact amount of future environmental cleanup costs, it is becoming clear that companies will be held accountable. Therefore, it doesn't seem reasonable to not accrue for environmental costs. Recognition of these liabilities provides a more accurate picture of the company's financial position. It also has the potential to improve the environment. As companies are forced to report these amounts on their financial statements, they will start to look for more effective and efficient means to reduce toxic waste and therefore reduce their costs.

**p. 186 Cooking the Books? Q:** What motivates sales executives and finance and accounting executives to participate in activities that result in inaccurate reporting of revenues? **A:** Sales executives typically receive bonuses based on their ability to meet quarterly sales targets. In addition, they often face the possibility of losing their jobs if they miss those targets. Executives in accounting and finance are very aware of the earnings targets of Wall Street analysts and investors. If they fail to meet these targets, the company's stock price will fall. As a result of these pressures, executives sometimes knowingly engage in unethical efforts to misstate revenues. As a result of the Sarbanes-Oxley Act, the penalties for such behavior are now much more severe.

## Answers to Self-Test Questions

1. c 2. a 3. d 4. d 5. d 6. c ( $\$1,350 - \$600 = \$750$ ) 7. a 8. c 9. c 10. b 11. b 12. c 13. a 14. a 15. d



## A Look at IFRS

It is often difficult for companies to determine in what time period they should report particular revenues and expenses. Both the IASB and FASB are working on a joint project to develop a common conceptual framework, as well as a revenue recognition project, that will enable companies to better use the same principles to record transactions consistently over time.

## LEARNING OBJECTIVE 11

## KEY POINTS

- In this chapter, you learned accrual-basis accounting applied under GAAP. Companies applying IFRS also use accrual-basis accounting to ensure that they record transactions that change a company's financial statements in the period in which events occur.
- Similar to GAAP, cash-basis accounting is not in accordance with IFRS.
- IFRS also divides the economic life of companies into artificial time periods. Under both GAAP and IFRS, this is referred to as the **periodicity assumption**.
- IFRS requires that companies present a complete set of financial statements, including comparative information annually.
- GAAP has more than 100 rules dealing with revenue recognition. Many of these rules are industry-specific. In contrast, revenue recognition under IFRS is determined primarily by a single standard. Despite this large disparity in the amount of detailed guidance devoted to revenue recognition, the **general** revenue recognition principles required by GAAP that are used in this textbook are similar to those under IFRS.
- Revenue recognition fraud is a major issue in U.S. financial reporting. The same situation occurs in other countries, as evidenced by revenue recognition breakdowns at Dutch software company **Baan NV**, Japanese electronics giant **NEC**, and Dutch grocer **AHold NV**.
- A specific standard exists for revenue recognition under IFRS (*IAS 18*). In general, the standard is based on the **probability that the economic benefits associated with the transaction will flow to the company** selling the goods, providing the service, or receiving investment income. In addition, the revenues and costs **must be capable of being measured reliably**.
- Under IFRS, revaluation of items such as land and buildings is permitted. IFRS allows depreciation based on revaluation of assets, which is not permitted under GAAP.
- The terminology used for revenues and gains, and expenses and losses, differs somewhat between IFRS and GAAP. For example, income under IFRS is defined as:
  - Increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from shareholders.

Income includes **both** revenues, which arise during the normal course of operating activities, and gains, which arise from activities outside of the normal sales of goods and services. The term **income** is not used this way under GAAP. Instead, under GAAP income refers to the net difference between revenues and expenses.

Expenses under IFRS are defined as:

- Decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity other than those relating to distributions to shareholders.

Note that under IFRS expenses include both those costs incurred in the normal course of operations, as well as losses that are not part of normal operations. This is in contrast to GAAP, which defines each separately.

- The procedures of the closing process are applicable to all companies whether they are using IFRS or GAAP.

## LOOKING TO THE FUTURE

The IASB and FASB are now involved in a joint project on revenue recognition. The purpose of this project is to develop comprehensive guidance on when to recognize revenue. Presently, the Boards are considering an approach that focuses on changes in assets and liabilities (rather than on earned and realized) as the basis for revenue recognition. It is hoped that this approach will lead to more consistent accounting in this area. For more on this topic, see [www.fasb.org/project/revenue\\_recognition.shtml](http://www.fasb.org/project/revenue_recognition.shtml).

## IFRS PRACTICE

## IFRS SELF-TEST QUESTIONS

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GAAP:

- (a) provides very detailed, industry-specific guidance on revenue recognition, compared to the general guidance provided by IFRS.
- (b) provides only general guidance on revenue recognition, compared to the detailed guidance provided by IFRS.
- (c) allows revenue to be recognized when a customer makes an order.
- (d) requires that revenue not be recognized until cash is received.

2.

Which of the following statements is **false**?

- (a) IFRS employs the periodicity assumption.
- (b) IFRS employs accrual accounting.
- (c) IFRS requires that revenues and costs must be capable of being measured reliably.
- (d) IFRS uses the cash basis of accounting.

3.

As a result of the revenue recognition project being undertaken by the FASB and IASB:

- (a) revenue recognition will place more emphasis on when revenue is earned.
- (b) revenue recognition will place more emphasis on when revenue is realized.
- (c) revenue recognition will place more emphasis on when changes occur in assets and liabilities.
- (d) revenue will no longer be recorded unless cash has been received.

4.

Which of the following is **false**?

- (a) Under IFRS, the term **income** describes both revenues and gains.
- (b) Under IFRS, the term **expenses** includes losses.