

**ACCT 3110 – Professor Mayper**  
**EXAM IC PART I AND II      SPRING 2003**

**Part I**

**I. Matching (16 points)**

Match each of the items below to the most appropriate description that follows:

- |   |                       |  |                    |
|---|-----------------------|--|--------------------|
| A. Asset                                      | B. Comparability      | C. Comprehensive Income                        | D. Consistency     |
| E. Conservatism                               | F. Cost Benefit       | G. Entity                                      | H. Expense         |
| I. Extraordinary Gain                         | J. Extraordinary Loss | K. FASB  | L. Full Disclosure |
| M. GAAP                                       | N. Going Concern      | O. Historic Cost                               | P. IASB            |
| Q. Liability                                  | R. Matching           | S. Materiality                                 | T. Monetary Unit   |
| U. Net Income                                 | V. Ordinary Gain      | W. Ordinary Loss                               | X. Owners=Equity   |
| Y. Periodicity                                | Z. Relevance          | 2. Reliability                                 |                    |
| 3. Revenue Recognition                        | 4. Revenue            | 5. SEC   |                    |
| 6. Statement of Financial Accounting Concepts |                       | 7. Statement of Financial Accounting Standards |                    |

\_\_\_\_\_ The qualitative characteristic that supports the use of historic cost since it is verifiable is called \_\_\_\_\_.

\_\_\_\_\_ An incurred cost of the current accounting period, in which no economic benefits are received in the current accounting period, and is an infrequent event but not unusual is a (an) \_\_\_\_\_.

\_\_\_\_\_ The intent of full disclosure is to allow users to evaluate one company against another company, by allowing for standardizing across the companies. This is a reflection of what secondary quality?

\_\_\_\_\_ The FASB is the only regulatory body that currently issues these rules which corporations are required to follow .

\_\_\_\_\_ A critical assumption of a cost basis for accounting is that the firm will exist in the future in order for the costs to be matched with the recognized revenue of the future periods. This future existence is a reflection of what assumption?

\_\_\_\_\_ This number reflects changes in the wealth of the entity due to the recognized revenue, expense, gain, and loss events of an accounting period.

\_\_\_\_\_ A current obligation of the firm to give up assets in the future is called a (an) \_\_\_\_\_.

\_\_\_\_\_ When it is assumed that the personal affairs of the investors are accounted for separately from the business affairs of the firm, this is a description of the \_\_\_\_\_ assumption.

## II. The Adjusting Process [15 points]

AGM Wholesale BBQ, Inc.  
Pre-adjusted Trial Balance  
December 31, 2002

Cash.....	\$ 128,295	
Accounts Receivable.....	96,000	
Allowance for Uncollectible Accounts	200	
Prepaid Insurance.....	9,800	
Prepaid Rent.....	6,600	
Supplies.....	150	
Inventory .....	15,200	
Building.....	420,000	
Accumulated Depreciation-Building....		57,500
Accounts Payable.....		35,000
Unearned Revenue.....		14,000
Notes Payable.....		150,000
Common Stock.....		185,000
Dividends.....	655	
Retained Earnings (1/1/02).....		149,170
Sales Revenue .....		216,250
Sales Returns and Allowances.....	1,250	
Cost of Goods Sold.....	105,370	
Insurance Expense.....	19,200	
Supplies Expense.....	4,200	
	\$ 806,920	\$ 806,920
	=====	=====

**Additional Information:**

1. On 12/1/02 received a \$14,000 advance payment from UNT Partiers. 35% of the BBQ was delivered to UNT in December, 2002; the remainder will be delivered in January 2003.
2. The Company uses the *aging of accounts receivable* method to estimate the allowance for uncollectible accounts. The estimated amount of uncollectible accounts at year end is \$2,880.
3. On July 31, 2002 the firm paid the annual insurance premium of \$19,200.
4. The building was purchased on July 1, 1999. It is estimated to have a 15 year useful life and depreciation is calculated using straight line. Salvage value was estimated at \$75,000.
5. AGM borrowed \$150,000 at 10% on May 1, 2002. Interest payments are due annually beginning April 30, 2003.
6. On 11/30/02 the rental agreement was renewed at an annual rental of \$7,800. Payments are due to the landlord at the *end* of each 3 month period of time (first due 3/1/03). The old rental contract was \$7,200 per year.
7. At December 31, 2002 the cost of supplies on hand was \$475.

**Required: Prepare all appropriate adjusting journal entries for the year ended 12/31/02.**

**III. Closing Entries (5 points)**

For the following accounts write in **column 1** Yes, if the account is closed at the end of the accounting period, otherwise write No [if you leave it blank, it will be counted wrong]; and in **column 2** write ABAL if the account will appear on the end of the period balance sheet, write AINC if it will appear on the period's income statement, write ASSE if it will appear on the period's statement of stockholders' equity, write ABOTH if it will appear on both the balance sheet and statement of stockholders' equity, or write ANONE if it does not appear on any of the financial statements.

<u>ACCOUNT NAME</u>	<u>column 1</u>	<u>column 2</u>
Example: Wage Expense	<u>yes</u>	<u>INC</u>
Accumulated Depreciation	_____	_____
Income Summary	_____	_____
Cost of Goods Sold	_____	_____
Dividends Declared	_____	_____
Gain due to change in depreciation methods	_____	_____

**IV. Discontinued Operations (6 points)**

On May 1, 2002 Koch Communications entered into a binding agreement to dispose of their newspaper subsidiary. The disposition will be completed on March 1, 2003.

**Information as of 12/31/02:**

Income (loss) from operations 1/1/02 - 4/30/02:	\$ (25,000)
Income (loss) from operations 5/1/02 - 12/31/02:	(60,000)
Carrying Value of Net Assets less disposal costs at 12/31/02:	940,000
Fair Value of Net Assets less disposal costs at 12/31/02:	936,000

**Information as of 12/31/03:**

Income (loss) from operations 1/1/03 - 3/1/03:	\$ (13,000)
Carrying Value of net assets at 3/1/03:	???
Sales Price less disposal costs at 3/1/03:	927,500

REQUIRED: Ignoring the income tax effect, what will be reported for the Results of Discontinued Operations for:

	<u>2002</u>	<u>2003</u>
Income (Loss) from Discontinued Operations	_____	_____
Gain (Loss) due to Impairment	_____	_____
Gain (Loss) from Sale of Discontinued Operation	_____	_____

## V. Essay (5 points)

For any credit, the answer must be READABLE

Cuban's Broadband Hardware, Inc. incurred \$15,000,000 of research and development costs (R&D) during 2002. The CFO tells you that there is a reasonable probability that this R&D will be successful. He gives you a report showing that if the R&D is successful the company will develop a new broadband delivery satellite that is estimated to increase net profits by \$500,000,000 over the next 15 years, beginning in 2003.

Using your professional judgment and knowledge of accounting theory, how would you account for the R&D costs incurred in both the 2002 and 2003 financial statements? What is the basis (rationale) for this accounting. (i.e., how will the R&D be recognized and classified and what is the basis for this type of recognition).

## VI. Income Statement and Retained Earnings [7 points]

For the year ended 12/31/02, DJ Computer Inc. had income from continuing operations before taxes of \$420,000 **before** considering the following transactions and events. All of the items below are before income taxes and are material.

1. During 2002 DJ had a \$3,000 gain due to an insurance claim from flood damages (excess insurance was received); the flood was unusual but not infrequent.
2. In January, 2002 DJ changed inventory methods, from weighted average to the FIFO method. The cumulative effect was to increase inventory by \$13,000.
3. In 2001 DJ omitted \$2,500 of accrued rent expense due to an error not discovered until 2002.
4. In 2002 DJ sold a copy machine for \$147,000; on the books it had a book value of \$140,000.
5. *Unadjusted* Beginning Retained Earnings at 1/1/02 was \$243,000.
6. The tax rate for DJ is 40%.

A.] Required: In **GOOD REPORT FORMAT**, prepare the Income Statement for the year 2002. Give all relevant line items, sub-totals and totals. Begin with income from continuing operations before taxes and ignore EPS disclosures.

**DJ=s**  
**INCOME STATEMENT**  
**for the year ending 12/31/02**

B.] How much is DJ's Adjusted Beginning Retained Earnings for 2002?

## EX I PART II

### I. Multiple Choice [10 points-- 2 each]

Instructions: Clearly print the letter of the best answer in the space provided next to each question.

1. \_\_\_\_\_ In a Statement of Cash Flows, issuance of common stock to retire long term debt would be classified as:
- a. Non cash investing and financing activities
  - b. Investing activities
  - c. Financing activities
  - d. Operating activities
2. \_\_\_\_\_ Comprehensive income includes:
- a. Investments by owners.
  - b. Dividend declared
  - c. Unrealized Holding Losses
  - d. All of the above are excluded in Comprehensive Income.
  - e. Two of the above are included in Comprehensive Income.
3. \_\_\_\_\_ Which of the following is a false statement:
- a. A potential material loss on a lawsuit, the outcome of which is uncertain as of the end of the current accounting period is a contingent event.
  - b. Related party transactions must be disclosed in notes to the financial statements.
  - c. Liabilities are eventually paid back with cash or provision of other assets or the provision of services.
  - d. Assets must be owned by the company.
4. \_\_\_\_\_ Josi Inc. produces expensive equipment for sale by contracts. For a few of the contracts there is substantial doubt about eventual collectibility and the revenue recognition method used is based on the gross profit ratio. The revenue recognition method used is:
- a. the Completed Contract Method
  - b. to recognize at time of delivery
  - c. the Percentage of Completion Method
  - d. The Installment Method
  - e. The Cost Recovery Method.
5. \_\_\_\_\_ Hill Co. began operations in 2001 and appropriately uses the installment method of accounting. At 12/31/01 they provide you the following:
- |  |           |
|--|-----------|
| Installment Receivables                    | \$400,000 |
| Installment Sales                          | 900,000   |
| Cost of Goods Sold, as percentage of Sales | 60%       |
- How much gross profit will be deferred in 2001?
- a. \$ 160,000
  - b. \$ 200,000
  - c. \$ 240,000
  - d. \$ 360,000

**II. Long Term Construction Contracts---Financial Statement Interpretation [6 points]**

Spear Corporation account for their long term construction contracts using the percentage of completion method. Below are the partial Income Statements and Balance Sheets for 2000-2001. All projects began in 2000 and were fully completed in 2002. The total contract price for these projects was \$10,000,000.

**PARTIAL INCOME STATEMENTS**

	<u>2000</u>	<u>2001</u>
Construction Revenue.....	\$3,750,000	\$4,000,000
Construction Expenses.....	<u>(2,250,000)</u>	<u>(3,105,000)</u>
Income (gross profit) from construction projects.....	\$1,500,000	\$ 895,000

**PARTIAL BALANCE SHEETS**

Current Assets:		
Accounts Receivable	\$ 305,000	\$ 430,000
Construction in Progress	\$3,750,000	
Less: Billings	<u>(3,000,000)</u>	
	750,000	
Current Liabilities:		
Billings .....		\$7,771,000
Less: Construction in Progress.....		<u>(7,750,000)</u>
		21,000

- a. How much cash did Spear collect from their customers in **2001**?
  
- b. How much were customers billed in **2000**?
  
- c. How much constructions revenue was recognized in **2001**?
  
- d. What was the estimated percentage completed for the project *through 2000*?

**III. Revenue Recognition--Long term Construction (21 pts)**

Denton Construction entered into a construction contract with KDNT on July 1, 1999 to construct a new television tower. The fixed fee contracted price for construction of the tower was \$6,000,000. The tower was completed on Feb 1, 2002. You are given the following:

	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>
Total Costs incurred <b>TO</b> date...	\$ 800,000	\$2,852,500	\$3,895,000	\$4,200,000
Year end <u>estimate</u> of <u>remaining</u> costs to complete project.....	3,200,000	1,222,500	205,000	-0-
Amounts billed to KDNT <b>during</b> year.....	1,750,000	2,700,000	1,550,000	-0-
Amounts collected during year.....	1,341,000	2,900,000	1,700,000	59,000

**REQUIRED:**

A] 1. ASSUME Denton Construction uses the **completed contract method**, prepare the relevant portion of the 2001 Balance Sheet, excluding the cash account. I will include the potential Balance Sheet Classifications and you are required to show the appropriate accounts, account balances and sub-totals.[as done in class notes, excluding the cash]

**2001**

CURRENT ASSETS:

CURRENT LIABILITIES:

2. How much Construction **Gross Profit (Loss)** will be recognized in:

**2001** \_\_\_\_\_

**2002** \_\_\_\_\_

3. What will be the balance in the CIP Account at 12/31:

**1999** \_\_\_\_\_

**2000** \_\_\_\_\_

**III. (continued)**

B] ASSUME Denton Construction uses the **Percentage of Completion method**:

i.) What will be the balance in the CIP Account at 12/31:

**2000** \_\_\_\_\_

**2001** \_\_\_\_\_

ii.) How much Construction **Gross Profit (Loss)** will be recognized in:

**2000** \_\_\_\_\_

**2001** \_\_\_\_\_

**2002** \_\_\_\_\_

**IV. Cash Flow/Cash-Accrual [10 points]**

You are provided with the following operating account balances for the year 2002

	Beginning Balance	Ending Balance
Accounts Receivable, net.....	\$ 75,000	\$ 65,400
Inventory.....	18,700	21,000
Prepaid Rent.....	1,800	1,450
Accounts Payable.....	15,600	14,000
Wages Payable.....	<u>2,100</u>	<u>2,260</u>

Additional Information:

- A. \$175,000 cash was collected from customers during the year (assume all sales are on credit)
- B. \$62,000 was paid to suppliers of inventory (assume all purchases of inventory are on credit and accounts payable is only used for inventory suppliers).
- C. \$17,000 was paid for rent during the year.
- D. \$88,000 was paid to employees during the year.

**Requirements----MUST SHOW YOUR WORK FOR ANY PARTIAL CREDIT**the above represents all the necessary information needed to construct an income statement. You need to convert the cashflow information in A through D above to accrual information using the above accounts. On the next page prepare a basic income statement that will show the revenues, each individual expense account implied by the above, and net income.

INCOME STATEMENT

REVENUES (list all relevant accounts implied)

EXPENSES (list each individual account implied)

NET INCOME (LOSS)