EXERCISES

Ex. 3–1

1. Prepaid expense
2. Accrued revenue
3. Unearned revenue
4. Accrued expense
5. Unearned revenue
6. Prepaid expense
7. Accrued expense
8. Accrued expense

Ex. 3–2

<table>
<thead>
<tr>
<th>Account</th>
<th>Answer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts Receivable</td>
<td>Normally requires adjustment (AR).</td>
</tr>
<tr>
<td>Capital Stock</td>
<td>Does not normally require adjustment.</td>
</tr>
<tr>
<td>Cash</td>
<td>Does not normally require adjustment.</td>
</tr>
<tr>
<td>Interest Expense</td>
<td>Normally requires adjustment (AE).</td>
</tr>
<tr>
<td>Interest Receivable</td>
<td>Normally requires adjustment (AR).</td>
</tr>
<tr>
<td>Land</td>
<td>Does not normally require adjustment.</td>
</tr>
<tr>
<td>Office Equipment</td>
<td>Does not normally require adjustment.</td>
</tr>
<tr>
<td>Prepaid Rent</td>
<td>Normally requires adjustment (PE).</td>
</tr>
<tr>
<td>Supplies</td>
<td>Normally requires adjustment (PE).</td>
</tr>
<tr>
<td>Unearned Fees</td>
<td>Normally requires adjustment (UR).</td>
</tr>
<tr>
<td>Wages Expense</td>
<td>Normally requires adjustment (AE).</td>
</tr>
</tbody>
</table>

Ex. 3–3

Supplies Expense .......................................................... 2,165
Supplies ....................................................................   2,165
Supplies used ($3,915 – $1,750).

Ex. 3–4

$3,650 ($900 + $2,750)
Ex. 3–5

a. Insurance expense (or expenses) will be understated. Net income will be overstated.

b. Prepaid insurance (or assets) will be overstated. Stockholders’ equity (retained earnings) will be overstated.

Ex. 3–6

a. Insurance Expense ........................................................ 11,200
   Prepaid Insurance .................................................... 11,200
   Insurance expired.

b. Insurance Expense ........................................................ 11,200
   Prepaid Insurance .................................................... 11,200
   Insurance expired ($14,800 – $3,600).

Ex. 3–7

a. Insurance Expense ........................................................ 14,800
   Prepaid Insurance .................................................... 14,800
   Insurance expired ($4,800 + $15,000 – $5,000).

b. Insurance Expense ........................................................ 14,800
   Prepaid Insurance .................................................... 14,800
   Insurance expired.

Ex. 3–8

Unearned Fees ............................................................... 36,000
   Fees Earned .............................................................. 36,000
   Fees earned ($45,000 – $9,000).

Ex. 3–9

a. Rent revenue (or revenues) will be understated. Net income will be understated.

b. Unearned rent (liabilities) will be overstated. Stockholders’ equity (retained earnings) at the end of the period will be understated.
Ex. 3–10

a. Accounts Receivable..................................................... 12,300
   Fees Earned.............................................................. 12,300
   Accrued fees.

b. No. If the cash basis of accounting is used, revenues are recognized only when the cash is received. Therefore, earned but unbilled revenues would not be recognized in the accounts, and no adjusting entry would be necessary.

Ex. 3–11

a. Unearned Fees............................................................... 78,500
   Fees Earned.............................................................. 78,500
   Unearned fees earned during year.

b. Accounts Receivable..................................................... 23,600
   Fees Earned.............................................................. 23,600
   Accrued fees earned.

Ex. 3–12

a. Fees earned (or revenues) will be understated. Net income will be understated.

b. Accounts (fees) receivable (or assets) will be understated. Stockholders’ equity (retained earnings) will be understated.

Ex. 3–13

a. Salary Expense .............................................................. 3,750
   Salaries Payable.............................................................. 3,750
   Accrued salaries [($9,375/5 days) × 2 days].

b. Salary Expense .............................................................. 7,500
   Salaries Payable.............................................................. 7,500
   Accrued salaries [($9,375/5 days) × 4 days].

Ex. 3–14

$37,500 ($41,250 − $3,750)
Ex. 3–15

a. Salary expense (or expenses) will be understated. Net income will be overstated.

b. Salaries payable (or liabilities) will be understated. Stockholders’ equity (retained earnings) will be overstated.

Ex. 3–16

a. Salary expense (or expenses) will be overstated. Net income will be understated.

b. The balance sheet will be correct. This is because salaries payable has been satisfied, and the net income errors have offset each other. Thus, stockholders’ equity (retained earnings) is correct.

Ex. 3–17

a. Taxes Expense .............................................................. 6,750
   Prepaid Taxes ........................................................... 6,750
   Prepaid taxes expired [($9,000/12) × 9 months].
   Taxes Expense .............................................................. 34,500
   Taxes Payable .......................................................... 34,500
   Accrued taxes.

b. $41,250 ($6,750 + $34,500)

Ex. 3–18

Depreciation Expense ................................................... 2,900
   Accumulated Depreciation—Equipment ................ 2,900
   Depreciation on equipment.

Ex. 3–19

a. $325,000 ($750,000 – $425,000)

b. No. Depreciation is an allocation of the cost of the equipment to the periods benefiting from its use. It does not necessarily relate to value or loss of value.
Ex. 3–20

a. $7,535 million ($15,082 – $7,547)

b. No. Depreciation is an allocation method, not a valuation method. That is, de-
preciation allocates the cost of a fixed asset over its useful life. Depreciation
does not attempt to measure market values, which may vary significantly
from year to year.

Ex. 3–21

Income: $3,434 million ($1,714 + $1,720)

Ex. 3–22

a. $579 million

b. 53.7% ($579 + $1,079)

Ex. 3–23

<table>
<thead>
<tr>
<th>Error (a)</th>
<th>Over-stated</th>
<th>Under-stated</th>
<th>Error (b)</th>
<th>Over-stated</th>
<th>Under-stated</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Revenue for the year would be ..................</td>
<td>$ 0</td>
<td>$18,000</td>
<td>$ 0</td>
<td>$ 0</td>
<td>$ 0</td>
</tr>
<tr>
<td>2. Expenses for the year would be ..................</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>3. Net income for the year would be ..............</td>
<td>0</td>
<td>18,000</td>
<td>3,000</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>4. Assets at May 31 would be .......................</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>5. Liabilities at May 31 would be....................</td>
<td>18,000</td>
<td>0</td>
<td>0</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>6. Stockholders’ equity at May 31 would be ..........</td>
<td>0</td>
<td>18,000</td>
<td>3,000</td>
<td>0</td>
<td></td>
</tr>
</tbody>
</table>

Ex. 3–24

$255,000 ($240,000 + $18,000 – $3,000)
Ex. 3–25

a. Depreciation Expense ................................................... 14,500
   Accumulated Depreciation—Equipment ................   14,500
   Depreciation on equipment.

b. (1) Depreciation expense would be understated. Net income would be over-
   stated.
   (2) Accumulated depreciation would be understated, and total assets would 
   be overstated. Stockholders’ equity (retained earnings) would be over-
   stated.

Ex. 3–26

1. Accounts Receivable..................................................... 2
   Fees Earned.............................................................. 2
   Accrued fees earned.

2. Supplies Expense.......................................................... 1
   Supplies .................................................................... 1
   Supplies used.

3. Insurance Expense........................................................ 4
   Prepaid Insurance .................................................... 4
   Insurance expired.

4. Depreciation Expense ................................................... 1
   Accumulated Depreciation—Equipment ................   1
   Equipment depreciation.

5. Wages Expense ............................................................. 1
   Wages Payable ......................................................... 1
   Accrued wages.
1. The accountant debited Accounts Receivable for $3,750 but did not credit Laundry Revenue. This adjusting entry represents accrued laundry revenue.

2. The accountant debited rather than credited Laundry Supplies for $1,750.

3. The accountant credited the prepaid insurance account for $3,800 but debited the insurance expense account for only $800.

4. The accountant credited Laundry Equipment for the depreciation expense of $6,000, instead of crediting the accumulated depreciation account.

5. The accountant did not debit Wages Expense for $1,200.

The corrected adjusted trial balance is shown below.

E-Z Laundry
Adjusted Trial Balance
July 31, 2012

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Credit Balances</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>7,500</td>
</tr>
<tr>
<td>Accounts Receivable</td>
<td>22,000</td>
</tr>
<tr>
<td>Laundry Supplies</td>
<td>2,000</td>
</tr>
<tr>
<td>Prepaid Insurance</td>
<td>1,400</td>
</tr>
<tr>
<td>Laundry Equipment</td>
<td>190,000</td>
</tr>
<tr>
<td>Accumulated Depreciation—Laundry Equipment</td>
<td>54,000</td>
</tr>
<tr>
<td>Accounts Payable</td>
<td>9,600</td>
</tr>
<tr>
<td>Wages Payable</td>
<td>1,200</td>
</tr>
<tr>
<td>Capital Stock</td>
<td>40,000</td>
</tr>
<tr>
<td>Retained Earnings</td>
<td>70,300</td>
</tr>
<tr>
<td>Dividends</td>
<td>28,775</td>
</tr>
<tr>
<td>Laundry Revenue</td>
<td>185,850</td>
</tr>
<tr>
<td>Wages Expense</td>
<td>50,400</td>
</tr>
<tr>
<td>Rent Expense</td>
<td>25,575</td>
</tr>
<tr>
<td>Utilities Expense</td>
<td>18,500</td>
</tr>
<tr>
<td>Depreciation Expense</td>
<td>6,000</td>
</tr>
<tr>
<td>Insurance Expense</td>
<td>3,800</td>
</tr>
<tr>
<td>Laundry Supplies Expense</td>
<td>1,750</td>
</tr>
<tr>
<td>Miscellaneous Expense</td>
<td>3,250</td>
</tr>
<tr>
<td><strong>360,950</strong></td>
<td><strong>360,950</strong></td>
</tr>
</tbody>
</table>
Ex. 3–28

a. $396 million decrease ($1,487 – $1,883)
   21.0% ($396 ÷ $1,883) decrease

b. 2009: 7.8% ($1,487 ÷ $19,176)
   2008: 10.1% ($1,883 ÷ $18,627)

c. The net income decreased during 2009 by $396 million, or 21.0%, from 2008, an unfavorable trend. The percent of net income to net sales also decreased.

Ex. 3–29

a. Dell Inc.

<table>
<thead>
<tr>
<th>Amount</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net sales..........................................</td>
<td>$61,101</td>
</tr>
<tr>
<td>Cost of goods sold..............................</td>
<td>(50,144)</td>
</tr>
<tr>
<td>Operating expenses.............................</td>
<td>(7,767)</td>
</tr>
<tr>
<td>Operating income (loss).......................</td>
<td>$ 3,190</td>
</tr>
</tbody>
</table>

b. Hewlett-Packard Company (HP)

<table>
<thead>
<tr>
<th>Amount</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net sales..........................................</td>
<td>$118,364</td>
</tr>
<tr>
<td>Cost of goods sold..............................</td>
<td>(89,592)</td>
</tr>
<tr>
<td>Operating expenses.............................</td>
<td>(17,970)</td>
</tr>
<tr>
<td>Operating income (loss).......................</td>
<td>$ 10,802</td>
</tr>
</tbody>
</table>

c. Hewlett-Packard (HP) is more profitable than Dell. Specifically, HP’s cost of goods sold of 75.7% is significantly less (6.4%) than Dell’s cost of goods sold of 82.1%. This is partially offset by HP’s higher operating expenses of 15.2% as compared to Dell’s operating expenses of 12.7%. The net result is that HP generates an operating income of 9.1% of sales, while Dell generates operating income of 5.2% of sales. Dell must improve its operations if it is to remain competitive with HP.