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BIRZEIT UNIVERSITY
FACULTY OF BUSINESS AND ECONOMICS
ACCOUNTING DEPARTMENT

LECTURERS: Dr. ZEYAD MUNAWER
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FIRST SEM. 2013/2014
FIRST HOUR EXAM

ACCT335

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Section Time: Miss Samia
at 9:30 T

Answer Sheet
Multiple Choices

| | |
|----|--------------|
| 1 | d |
| 2 | a |
| 3 | d |
| 4 | a |
| 5 | c |
| 6 | b |
| 7 | c |
| 8 | d |
| 9 | b |
| 10 | a |

9

Question 1

| | |
|----|--------------|
| 1 | h |
| 2 | d |
| 3 | a |
| 4 | i |
| 5 | j |
| 6 | l |
| 7 | e |
| 8 | c |
| 9 | b |
| 10 | f |
| 11 | k |
| 12 | a |

12
9
13

11

PART 1

Question 1 (12 points)

In each case 1 through 12, select the assumption, principle, or constraint that has been violated.

Use the table on the first page to indicate the following letter code for your selections.

| | | |
|------------------------------------|-------------------------------|------------------------------|
| a. Expense recognition principle ✓ | e. Monetary unit assumption | k. Materiality |
| b. Revenue recognition principle ✓ | f. Going concern assumption ✓ | j. Cost-benefit relationship |
| c. Full disclosure principle ✓ | g. Periodicity assumption | k. Industry practice |
| d. Measurement principle | h. Economic entity assumption | l. Conservatism |

1. Helen Cho, a sole proprietor, pays for her daughter's preschool out-of-business funds. **h**

~~2.~~ To make the balance sheet look better, Alfredo co. added several thousand dollars to the Equipment account that she believed was undervalued. **d**

3. Computers costing less than \$1,000 are immediately expensed even though their useful life is three years. **a**

~~4.~~ The auditors of Dietrich Co. found an error of \$50 in its financial statements and decide to restate their financial statements; Dietrich has sales revenue of \$15 million. **i**

5. To appropriately account for the pension liability, Orange Co. installs an abnormally expensive system to track employees, their health, and their pension status. Orange argues that this system is necessary to comply with accounting guidelines. **j**

6. Inventory is reported at market value when cost is lower. **d, l**

~~7.~~ ~~Mayan Imports receives a shipment from Germany, the invoice is stated in Euros.~~ **e**

8. In preparation of its financial statements, Ettredge Inc. omitted information about its method of accounting for accounts receivable. **c Full disclosure**

9. To make its profits look better, Shanghai Automotive booked sales before its cars were shipped. **b Rev-**

10. Jose Martinez reports all of its assets and liabilities at liquidation value, even though the company does not expect to go out of business in the foreseeable future. **f**

11. Hawaii Tropical Inc. reports its agricultural crops of pineapples, mango & cactus at cost. **k**

~~12.~~ Blacksmith factory calculated depreciation on factory machines in the amount of \$200,000. Blacksmith argues that since net income is expected to be lower in the current fiscal year, it should just charge it as an expense next year. **a**

Question 2 (14 points)

The following information pertains to Pinar for Dairy Food Co., a calendar-year sole proprietorship, which maintains its books on the cash basis of accounting. Pinar's net cash receipts over cash disbursements was \$50,000 during the fiscal year ended December 31, 2012.

Pinar has developed plans to expand into the wholesale dairy food market and is in the process of negotiating a bank loan to finance the expansion. The bank is requesting from Pinar the financial statements for the year ended December 31, 2012 prepared on the accrual basis of accounting. During the course of a review engagement, Ramez, Pinar's accountant, obtained the following additional information.

- Unpaid invoices for milk purchases totaled \$3,850 and \$2,100 at December 31, 2012 and December 31, 2011, respectively.
- Accrued expenses at December 31, 2011 and 2012 were as follows:

| Accrued Expenses | Year 2011 | Year 2012 |
|------------------|----------------|----------------|
| Utilities | \$1,900 | \$1,200 |
| Income taxes | 1,400 | 2,000 |
| Rent | 1,000 | 3,000 |
| Total | \$4,300 | \$6,200 |

- An analysis of the prepaid fire Insurance expense revealed a decrease in the amount of \$1,500.
- An analysis of the unearned sales revenue revealed an increase in the amount of \$2,500.
- Amounts due from customers totaled \$4000 and \$6000, at December 31, 2012 and December 31, 2011, respectively.
- All long-lived assets are rented?
No Dep.?

Required

Use the following schedule to convert Pinar's net cash receipts over cash disbursements for the year ended December 31, 2012 to net income on an accrual basis.

Pinar Co.
Conversion of Income Statement Data
From Cash Basis to Accrual Basis
For the year ended December 31, 2012

| | Cash Basis | Adjustments | | Accrual Basis |
|-------------------------------------|------------|-------------|---------|---------------|
| | | Add | Deduct | |
| Net Cash (Receipts > Disbursements) | \$50,000 | | | |
| Increase in unearned Revenue | | | ✓ 2500 | |
| Beginning Accounts Receivable | | | + 6000 | |
| Ending Accounts Receivable | | (6000) | | |
| Beginning accrued expenses | | 6400 | | |
| Ending accrued expenses | | | ✓ 10050 | |
| Decrease in prepaid Insurance | | | ✓ 1500 | |
| Net Income | | | | 40350 |

$$- \left(\begin{array}{l} + \text{Beg A/P} \\ + \text{End A/P} \\ + \text{Beg prepaid Exp.} \\ + \text{End " "} \end{array} \right) \begin{array}{l} 2500 \\ 0 \end{array}$$

Cash receipts
- Cash payments
net cash flow 50,000
+ End A/R
- Beg A/R
+ Beg U-R
- End U-R

Prepaid Insurance
+ Beg. ↓
- End 0
+ 1500

+ Beg - End
↓ Prepaid Insurance
Beg. (1500)
End = 0

A/R
Beg = 6000 End = 4000 - Beg
End = 6000 Beg = 6000 + End

U-R
Beg = 0
- U-R End = 2500
+ U-R (2500)
- 2500

A/R
U-R

12
14

Packaging M.
Cash

Paid

Question 3 (11 points)

When the accounts of Golden Olive Co. were examined, the adjusting data listed below were uncovered on December 31, 2013 the end of an annual fiscal period.

1. Purchase of packaging materials for \$5000 during the year was recorded in the Packaging Material account. A physical count revealed that on December 31, packaging materials of \$2,900 are on hand. $5000 - 2100 = 2900$

2. Interest of \$1000 was earned on notes receivable.

Interest Exp. 1000
Interest Payable 1000

3. On August 1, Rental Revenue was credited for \$30,000, representing revenue from a sub-rental for a 12-month period beginning on that date. $\frac{30000}{12} \times 5 = 12500$

4. The prepaid insurance expense account shows a debit of \$45,000, representing the cost of a 3-year fire insurance policy dated April 1 of the current year. $\frac{45000}{3} = 15000$, $\frac{15000}{12} = 1250$

5. On March 1, Unearned Service Revenue was credited for \$30,000, representing services to be performed within 2-year period beginning on that date. An analysis reveals that \$12,500 of these services was earned during the current year. $\frac{30000}{2} = 15000$, $\frac{15000}{12} = 1250$

B.S. Approach

U.R. 12500

12500

Exp. Prepaid

Cash U.R. 30000

U.R. service Rev.

Aug
15 Sep
30 Oct
Nov
5 Dec

B.S. Approach

B.S. Approach

Required

Use the following table below to:

- Prepare the adjusting entry for each item.
- Prepare the reversing entry for each item where appropriate.

9

| Item | Adjusting Entry | Reversing Entry (if appropriate) |
|------|---|--|
| 1. | <p>Packaging material Expense 2100</p> <p> Packaging Material 2100</p> | No Reversing entry |
| 2. | <p>Interest Receivable 1000</p> <p> Interest Expense 1000</p> <p>Interest Revenue 1000</p> <p> Interest Receivable 1000</p> | <p>Interest Revenue 1000</p> <p> Interest Receivable 1000</p> |
| 3. | <p>Rent Revenue 17500</p> <p> Unearned Rent Revenue 17500</p> | <p>Unearned Rent Revenue 17500</p> <p> Rent Revenue 17500</p> |
| 4. | <p>Insurance Expense 11250</p> <p> Prepaid Insurance Expense 11250</p> | No Reversing entry |
| 5. | <p>Unearned Service Revenue 12500</p> <p> Service Revenue 12500</p> | No Reversing entry |

Question 4 (14 points)

Herbawi Co. is in the process of preparing its Financial Statements for December 31, 2013.

The items listed below represent various transactions that occurred during 2013.

The following two responses are required for each item:

- Compute the amount of gain, loss, or adjustment to be reported in the year-end financial statements, assuming an interest rate of 30%.
- Select from the list below the financial statement category in which the gain, loss, or adjustment should be presented.

| Financial Statement Categories | |
|--------------------------------|--|
| A ¹ | Income from continuing operations |
| B ² | Extraordinary item |
| C ³ | Prior period adjustment to beginning retained earnings |
| D ⁴ | Other comprehensive income |
| E ⁵ | Change in accounting principles to beginning retained earnings |
| F ⁶ | Discontinued operations |
| G ⁷ | Change in estimate |

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14

| Item | Amount | Category |
|---|---|----------|
| <p>1. During the year, Herbawi received \$1,500,000 from its insurance company to cover losses suffered during a hurricane. This was the first hurricane ever to strike in area. The hurricane destroyed a warehouse with a carrying amount of \$640,000, containing equipment with a carrying amount of \$370,000 and inventory with a carrying amount of \$785,000 and a fair value of \$900,000. Compute the amount of gain or loss from the hurricane and select the proper category.</p> | <p>\$1,256,500</p> | <p>B</p> |
| <p>2. During the year Herbawi discontinued its manufacturing mattress segment, the segment had revenues of \$900,000 and expenses of \$800,000; the gain from the disposal of the manufacturing mattress segment was \$200,000 pre-tax. Compute the amount of gain or loss from the results of operations and disposal of the manufacturing mattress segment and select the proper category.</p> | <p>Gain on disposal 140,000 loss from operations 210,000 loss from discontinued operations = \$70,000</p> | <p>F</p> |

Ext

Cash received CV

loss
300
gain
200

| | Amount | Category | | | | | | | | | |
|---|---|------------|------------|----------------------|----------|----------|---------------------------------|----------------------------|---------|---------|---|
| 3. Herbawi had an unrealized holding gain on available-for-sale securities for 2013 of \$80,000 pre-tax. | ✓ 56000 | ✓ D | | | | | | | | | |
| 4. Herbawi decided to change from the Straight-line method of depreciation to the Double-declining-balance depreciation method in December 2013. Data related to this change is presented below. | Reg R-E ~ Add Change in acc. method 42000 | E | | | | | | | | | |
| <table border="1"> <thead> <tr> <th></th> <th>Old Method</th> <th>New Method</th> </tr> </thead> <tbody> <tr> <td>Depreciation in 2013</td> <td>\$40,000</td> <td>\$70,000</td> </tr> <tr> <td>Accumulated Dep. as of 1/1/2013</td> <td>130,000 130,000</td> <td>190,000</td> </tr> </tbody> </table> | | Old Method | New Method | Depreciation in 2013 | \$40,000 | \$70,000 | Accumulated Dep. as of 1/1/2013 | 130,000 130,000 | 190,000 | ✓ 42000 | ✓ |
| | Old Method | New Method | | | | | | | | | |
| Depreciation in 2013 | \$40,000 | \$70,000 | | | | | | | | | |
| Accumulated Dep. as of 1/1/2013 | 130,000 130,000 | 190,000 | | | | | | | | | |
| Compute the amount of the change and select the proper category. | | | | | | | | | | | |
| 5. In January 2013, Herbawi determined that the ^{12 + 3 = 15 Years} 12-year estimated useful life of a machine purchased for \$48,000 in January 2008 should be extended by 3 years. The machine is being depreciated using the straight-line method and has <u>no salvage value</u> . Compute the amount of depreciation expense that should be reported in the financial statements for the year ended December 31, 2013 and select the proper category. | ✓ 2800 | ✓ G | | | | | | | | | |
| 6. During 2013, Herbawi experienced a <u>material gain</u> in the amount of \$200,000 from the repurchase of a large bond issue that has been outstanding for 3 years. Herbawi regularly repurchases bonds of this nature. | ✓ 200000 | ✓ CA | | | | | | | | | |
| 7. During 2013, Herbawi sold the <u>only land</u> it owns for \$800,000. The land was acquired 10 years ago for the amount of \$100,000 for future expansion, but shortly thereafter; the company abandoned all plans for expansion and decided to hold the land for future sale. Compute the gain or loss on the sale of land and select the proper category. | ✓ 490000 | ✓ B | | | | | | | | | |

sold land for 800 000
 Cost 100 000
 Gain 700 000

PART 2

Multiple Choice Questions (10 points)

- Which of the following is an implication of the going concern assumption?
 - The historical cost principle is credible. ✓
 - Depreciation and amortization policies are justifiable and appropriate. ✓
 - The current-noncurrent classification of assets and liabilities is justifiable and significant.
 - All of these.

- How should Pinar Co. report its decision to change from a cash-basis of accounting to accrual-basis of accounting?
 - As a change in accounting principle, requiring the cumulative effect of the change (net of tax) to be reported in the income statement.
 - Prospectively, with no amounts restated and no cumulative adjustment. ✓
 - As an extraordinary item (net of tax). ✗
 - As a prior-period adjustment (net of tax), by adjusting the beginning balance of retained earnings. ✗

Use the following information for questions 3 - 9.

At December 31, 2013, Sinokrot Corporation had the following stock

$1000 \times 100 = 100,000$

- | | |
|--|-----------|
| 1. 5% cumulative preferred stock, \$100 par, 1000 shares outstanding | \$100,000 |
| 2. Common stock, \$10 par, 100,000 shares outstanding | 1,000,000 |

During 2013, Sinokrot did not issue any additional common stock. The following also occurred during 2013.

| | | after-tax |
|---|-------------------|-------------------|
| • Income from continuing operations (pre taxes) | \$130,000 | 78,000 |
| • Loss on operations of discontinued soft drink component (pre taxes) | 70,000 | 42,000 |
| • loss on disposal of soft drink component (pre taxes) | 20,000 | 12,000 |
| • Extraordinary gain on an expropriation of property (pre taxes) | 50,000 | 30,000 |
| • Preferred dividends declared | 5,000 | 3,000 |
| • Common dividends declared | 20,000 | 12,000 |
| • Effective tax rate | 40% | |

3. Compute Sinokrot's 2013 earnings per share from income from continuing operations.

- \$1.30
- \$1.25
- \$0.78
- \$0.73

$$\frac{72,000 - 5,000}{100,000}$$

$$\begin{array}{r} 52,000 \\ - 28,000 \\ - 8,000 \\ + 2,000 \end{array}$$

4. Compute Sinokrot's 2013 per share loss from operations of discontinued soft drink component.

- a. \$(0.42)
- b. \$(0.37)
- c. \$(0.70)
- d. \$(0.65)

(2000)

5. Compute Sinokrot's 2013 per share loss from disposal of discontinued soft drink component.

- a. \$(0.20)
- b. \$(0.15)
- c. \$(0.12)
- d. \$(0.07)

6. Compute Sinokrot's 2013 earnings per share from income before extraordinary items.

- a. \$0.24
- b. \$0.19
- c. \$0.30
- d. \$0.40

7. Compute Sinokrot's 2013 earnings per share from gain of extraordinary item.

- a. \$0.45
- b. \$0.50
- c. \$0.30
- d. \$0.25

8. Compute Sinokrot's 2013 earnings per share from net income.

- a. \$0.59
- b. \$0.34
- c. \$0.54
- d. \$0.49

9. What is the total amount of income tax expense for the year 2013?

- a. \$52,000.
- b. \$36,000.
- c. \$44,000.
- d. \$68,000.

10. For the year ended December 31, 2013, Rayhan Inc. reported the following:

| | | |
|--|------------|------|
| Net income | \$ 100,000 | => |
| Preferred dividends declared | 5,000 | |
| Common dividends declared | 20,000 | |
| Unrealized holding loss on available-for-sale securities | 3,000 | => |
| Retained earnings | 88,000 | |
| Common stock | 60,000 | |
| Accumulated other comprehensive income, beginning balance | 15,000 | 2100 |
| Income tax rate | 30% | |

What would Rayhan report as its ending balance of Accumulated Other Comprehensive Income?

- a. \$12,900
- b. \$12,000
- c. \$17,100
- d. \$18,000

Acc. 2100

loss ~~3000~~ 2100