Midterm 2021 – Financial Accounting and Reporting (BPOLO2090D)

Home assignment (UC)

BSc in International Business and Politics

Copenhagen Business School

23 April 2021

Student Number:

Examiner: Sumair Hussain

Pages: 5

Q1

A:
FALSE
FASB stands for Financial Accounting Standards Board and is the authority, who sets accounting standards in the US. The IASB on the other hand is the International Accounting Standards Board and is responsible for the worldwide standard (located in London).

B:
FALSE
GAAP is short for "Generally Accepted Accounting Principles".

C:
TRUE

D:
TRUE

E:
'Accumulated depreciation account - Building' is a contra account to the asset account 'Buildings'.
'Allowance for Doubtful Accounts' is a contra asset account to 'Accounts Receivable'.

F:
No, accumulated depreciation appears in the balance sheet (shown as a contra account below the account it is contra to).

G:
The direct write-off method is undesirable, because it does not consider possible bad debt, which will thus overstate the net income. It also violates the matching principle, saying that revenues in a period must be associated with all cost necessary to generate that revenue, thus bad debt must be taken into account.

H:
The two methods for estimating the allowance for doubtful accounts are called 'the balance sheet approach' and the 'income statement approach'.
The balance sheet approach takes a percentage of Accounts Receivable and makes a journal entry by debiting a 'Bad Debts Expense' and crediting 'Allowance for Doubtful Accounts' with the amount of the percentage of the Accounts Receivable taking into account the existing balance in the Allowance for Doubtful Accounts account.
The Income statement approach takes the relevant percentage of the estimated Uncollectible amount of Net Credit Sales (found in the income statement) and makes a journal entry of debiting Bad Debts Expense and crediting Allowance for Doubtful Accounts - not taking the existing balance in the Allowance for Doubtful Accounts account into consideration.

Q2
A:

In ¥	Ending Inventory	Cost of Goods Sold	Gross Profit
Weighted average	(53250/1860) × 650 = 18,294.35	(53250/1860) × 1210 = 34,055.65	54,450 – 34,055.65 =20,394.35
FIFO	(650 × 25) = 16,250	(275× 20) + (325 × 30) + (560 × 35) +(50 × 25) = 36,100	54,450 – 36,100 = 18,350
LIFO	(275 × 20) + (325 × 30) + (50 × 35) = 17,000	(700 × 25) + (510 × 35) = 35,350	54,450 – 35,350 = 19,100

B:
The Perpetual system is a system in which the inventory account is "corrected" (increased and decreased) at the time of each purchase and sale. Thus, my answer in A would be different is Sakura Corporation had used a perpetual inventory system, as we would have known exactly what amounts of each type of inventory would have been sold.

Q3
A:
The Annual depreciation expense with the straight-line depreciation method is:

$$\text{Ann.} Depreciation = \frac{Acq.cost - Residual\ value}{Life\ in\ years} = \frac{700{,}000 + 100{,}000 - 200{,}000}{4} = \$150{,}000$$

B:

DATE	ACCOUNT - DEBIT	ACCOUNT - CREDIT	AMOUNT - DEBIT	AMOUNT CREDIT
DEC 31 2017*	Depreciation Expense		150,000	
		Accumulated Depreciation		150,000
	(Depreciation of equipment for 2017)			

*Assuming the end of the fiscal year is December 31.

C:

Year	Annual depreciation	Accumulated Depreciation	Book value (End of fiscal year)
1	$150,000	$150,000	$650,000
2	$150,000	$300,000	$500,000
3	$150,000	$450,000	$350,000
4	$150,000	$600,000	$200,000

Book value is found by:

$$Book\ value = Acquisition\ cost - Accumulated\ Depreciation$$

D:
The pre-tax income for 2017 would have been higher if the expected useful life had been 5 years instead of 4 years, because the annual depreciation, which is an Expense Account, would have been lower and thus net income ($Revenues - Expenses$), would have been higher.
(The annual depreciation would have been $120,000 instead of $150,000)

<u>Q4</u>
A:

DATE /TRANSACTION	ACCOUNT - DEBIT	ACCOUNT - CREDIT	AMOUNT - DEBIT	AMOUNT CREDIT
1	Cash		600,000	
		Capital stock		600,000
	(Issuing shares)			
2	Building		200,000	
		Cash		80,000
		Notes payable		120,000
	(Purchase of building)			
3	Equipment		300,000	
		Accounts payable		300,000
	(Purchase of equipment from Charlene Inc)			
4	Notes payable		30,000	
		Cash		30,000
	(Payment on note)			
5	Cash		10.000	
		Product delivery/ Product liability/ Deferred revenue		10.000
	(Received cash for product delivered later)			

B:
Trial balance for Beta Inc.

Account	Debit balance	Credit balance
Cash	500,000	
Building	200,000	
Equipment	300,000	
Accounts Payable		300,000
Deferred revenue		10,000
Notes payable		90,000
Capital stock		600,000
Totals	1,000,000	1,000,000

Q5
The mistake made in the balance sheet for Agarwal Saris is that unearned revenue is recorded under Current Assets, while it is a current liability, as Unearned revenue is when a company has received cash for a product or service but is yet to provide the product/service, and it is thus a liability of the company.
Likewise, 'Prepaid Rent' is a Current Asset and not a liability, and these two mistakes with equal amounts in their balances are thus the reason why the balance sheet balances, which makes the mistake difficult to realize.

Q6
A:

Partial Balance sheet Dec 31 - Liabilities	
Current Liabilities:	
Accounts payable	550
Bank loan – Due March 2021	750
Income taxes payable	350
Accrued rent	700
Non-current liabilities:	
Notes payable – Due June 2023	1300
Total Liabilities	=3,650

Partial Balance sheet Dec 31 - Equity	
Equity: Capital Retained earnings Total Equity:	 3500 1,250 = 4,750

Total Liabilities and equity is: 8,400.

B:
The amount of current assets is:

$$Current\ Assets = 450 + 800 + 150 + 650 + 500 = 2550$$

(Stock investments are not counted in current assets in this case, as I assume that the stock investments are long-term).

Q7
A:

$$Current\ ratio\ 2019 = \frac{Current\ assets}{Current\ liabilities} = \frac{536,671}{115,845} = 4.633\ to\ 1$$

B:

$$Profit\ Margin\ 2019 = \frac{Net\ income}{Sales\ or\ Revenues} = \frac{Revenues\ - expenses}{Sales\ or\ Revenues} = \frac{(210,935)}{3,781} = -55.79$$

C:

$$Gross\ profit\ ratio\ 2019 = \frac{Gross\ profit}{Net\ sales} = \frac{1,777}{3,781} = 0.47 = 47\%$$

D:

$$Inventory\ turnover\ ratio = \frac{Cost\ of\ goods\ sold}{Average\ inventory} = \frac{\overset{2,004}{\cancel{23,288 + 26,817}}}{2} = 0.08$$

E:

$$Accounts\ Receivable\ Turnover\ ratio = \frac{Net\ credit\ sales}{Average\ Accounts\ Receivable} = \frac{3,781}{\frac{1,279 + 461}{2}} = 4.35$$

F:

$$Asset\ turnover\ ratio = \frac{Net\ sales}{Average\ total\ assets} = \frac{3,781}{\frac{156,039 + 605,546}{2}} = 0.01$$

What makes this company's performance challenging to analyze is the very short income statement - A more comprehensive income statement would also have made it easier to analyze why the company's net loss is that significant.