

FINANCIAL ACCOUNTING EXAM 2.1 SOLUTION

Check your work carefully, no partial credit.

Question 1

(1/2 point each, for a total of 2 points)

Part 1(a)

Record a journal entry for the following:

On December 1, 2012, the company recognized \$250 of depreciation expense related to the office computer it used in the marketing department.

	Debit	Credit
<u>Selling, general, and administrative expense</u>	<u>\$250</u>	
<u>PP&E accumulated depreciation</u>		<u>\$250</u>

Part 1(b)

Record a journal entry for the following:

On December 31, 2012, the company received \$40 thousand cash when it sold some auto-repair equipment it had used in its service department. The equipment had \$100 thousand of historical cost and \$50 thousand of accumulated depreciation. Consistent with U.S. GAAP, the company does not recognize unrealized gains associated with PP&E

	Debit	Credit
<u>Cash</u>	<u>\$40</u>	
<u>PP&E accumulated depreciation</u>	<u>\$50</u>	
<u>Loss on sale of PP&E</u>	<u>\$10</u>	
<u>PP&E historical cost</u>		<u>\$100</u>

Part 1(c)

Record a journal entry for the following:

Based on the company's Schedule II, record the journal entry to recognize the write-offs of accounts receivables for the year ended December 31, 2012.

	Debit	Credit
<u>Allowance for bad debt (contra asset)</u>	<u>\$4,500</u>	
<u>Accounts receivable, gross</u>		<u>\$4,500</u>

Part 1(d)

Record a journal entry for the following:

Based on the company's Schedule II, record the journal entry to recognize its bad debts expense for accounts receivables for the year ended December 31, 2012.

	Debit	Credit
<u>Bad debts expense</u>	<u>\$4,400</u>	
<u>Allowance for bad debt (contra asset)</u>		<u>\$4,400</u>

Question 2

(1/2 point for each statement, for a total of 1 point)

Part 2(a)

Fan's High Tech Products and Services	
2012 Direct Cash Flow Statement	
<i>In Dollars, for year ended December 31, 2012</i>	
Operating activities	
Customer collections	\$2,300
Resource provider payments	(\$825)
Tax payments	(\$10)
Net cash from operations	\$1,465
Investing activities	
Purchase property, plant, and equipment	(\$2,300)
Net cash from investing activities	(\$2,300)
Financing activities	
Issue common stock	\$2,000
Net cash from financing activities	\$2,000
Net change in cash during year	\$1,165
Beginning cash balance	\$650
Ending cash balance	\$1,815

Part 2(b)

Fan's High Tech Products and Services	
2012 Indirect Cash Flow Statement	
<i>In Dollars, for year ended December 31, 2012</i>	
Operating activities	
Net income	\$240
Depreciation	\$25
Accounts receivable	\$100
Inventory	\$200
Prepaid expenses	(\$50)
Accounts payable	\$750
Accrued taxes	\$0
Other accrued liabilities	(\$410)
Deferred revenues	\$610
Net cash from operations	\$1,465
Investing activities	
Purchase property, plant, and equipment	(\$2,300)
Net cash from investing activities	(\$2,300)
Financing activities	
Issue common stock	\$2,000
Net cash from financing activities	\$2,000
Net change in cash during year	\$1,165
Beginning cash balance	\$650
Ending cash balance	\$1,815

Question 3

You MUST CIRCLE the letter associated with the best response to receive credit.

(1/2 point each for a total of 1 point)

Question 3(i)

CIRCLE the letter associated with the best response.

Based on the available information in Tim Hortons' financial statements in the exam supplement, it is reasonable to conclude:

- (a) Tim Hortons' \$115,869 thousand depreciation and amortization adjustment on the cash flow statement for the period ending January 1, 2012 represents depreciation and amortization that increased net cash from operations.
- (b) Tim Hortons' (\$32,057) thousand inventories and other adjustment on the statement of cash flows represents a \$32,057 thousand net decrease in inventories and other due to operating activities during the period ending January 1, 2012.
- (c) Tim Hortons' \$2,099 thousand accounts receivable adjustment on the statement of cash flows for the period ending January 1, 2012 differs from \$8,338 thousand change in accounts receivable, net on the balance sheet (from 2011 to 2012) because the cash flow adjustment does not include the net effects of an allowance for doubtful accounts.
- (d) (a) and (b)
- (e) none of the above

Question 3(ii)

CIRCLE the letter associated with the best response.

Based on the available information in Tim Hortons' financial statements in the exam supplement, it is reasonable to conclude:

- (a) When Tim Hortons replenished its allowance for doubtful accounts during the period ending January 1, 2012, the accounts receivable adjustment on the statement of cash flows increased.
- (b) When Tim Hortons replenished its allowance for doubtful accounts during the period ending January 1, 2012, the accounts receivable adjustment on the statement of cash flows decreased.
- (c) When Tim Hortons used its allowance for doubtful accounts during the period ending January 1, 2012, net income on the statement of cash flows decreased.
- (d) (a) and (b)
- (e) (b) and (c)

Question 4

Part 4(a)

Record a single journal entry that summarizes the entries Tim Hortons recorded during fiscal 2011 (the period ending January 1, 2012) to replenish the inventory allowance for obsolescence.

(1 point)

	Debit	Credit
<u>Cost of sales</u>	<u>\$689</u>	
<u> Allowance for inventory obsolescence (contra asset)</u>		<u>\$689</u>

Source: Schedule II footnote

Part 4(b)

Determine the direct effect(s) on the following Tim Hortons metrics for fiscal 2011, everything else equal, if Tim Hortons had recorded the journal entry in Part 4(a) to replenish the inventory allowance for obsolescence during fiscal 2011 (the period ending January 1, 2012).

Ignore taxes.

(1/4 point per ratio, for a total of 1 point.)

	Increases	Decreases	No Effect
<u>Working capital</u> (current assets - current liabilities)	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
<u>Financial leverage</u> (liabilities / assets)	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<u>Inventory turnover</u> (cost of sales / average inventories)	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<u>Return on equity (ROE)</u> (net profit / average owners' equity)	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>

Question 5

For the purpose of this question, assume 90% of Whirlpool's total cost to meet customers' warranty and recall claims is related to inventoried replacement parts or products and 10% to wages for labor to be paid at a future date. Round amounts to one decimal place.

Part 5(a)

Record a single journal entry that summarizes the entries Whirlpool recorded during fiscal 2012 to meet customers' warranty and recall claims. That is, to repair or replace products under warranty and recall programs.

(1 point)

	Debit	Credit
<u>Accrued warranty allowance (current and noncurrent)</u>	<u>\$313.0</u>	
<u> Parts inventories</u>		<u>\$281.7</u>
<u> Accrued liabilities</u>		<u>\$31.3</u>

Source: Warranties footnote and given assumptions

Part 5(b)

Record a single journal entry that summarizes the entries Whirlpool recorded during fiscal 2012 to replenish the warranty allowance.

(1 point)

	Debit	Credit
Cost of sales	\$303.0	
Accrued warranty allowance (current and noncurrent)		\$303.0

Source: Warranties footnote and given assumptions

Part 5(c)

Identify the Whirlpool financial statement line items that would have been directly affected (and the direction of the effects) if Whirlpool had recorded the journal entry in question 5(b) to replenish the warranty allowance during during fiscal 2012. **HOWEVER, UNLIKE THE ENTRY IN 5(b), CONSIDER THE EFFECTS OF CURRENT AND NON-CURRENT SEPARATELY** and assume both effects occur. The amounts are not disclosed, but you can determine the line items directly affected and the direction of the effects.

(1/2 point per statement, for a total of 2 points.)

Whirlpool Financial Statements, fiscal 2012					
Balance Sheet			Statement of Stockholders' Equity		
Line Items	Increases	Decreases	Line Items	Increases	Decreases
Other current liabilities	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Net earnings	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Other noncurrent liabilities	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Retained earnings	<input type="checkbox"/>	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Income Statement			Statement of Cash Flows		
Line Items	Increases	Decreases	Line Items	Increases	Decreases
Cost of products sold	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Net earnings	<input type="checkbox"/>	<input checked="" type="checkbox"/>
	<input type="checkbox"/>	<input type="checkbox"/>	Other (operating cashflow adjustment)	<input checked="" type="checkbox"/>	<input type="checkbox"/>

Question 6

YOU MUST WRITE CLEARLY WITHIN THE GIVEN EXAM SPACE TO RECEIVE CREDIT.

If, in our sole judgment, we can not read your response you will not receive full credit.

(total of 10 points)

While there aren't correct responses to this portion of the exam, some are definitely better than others.

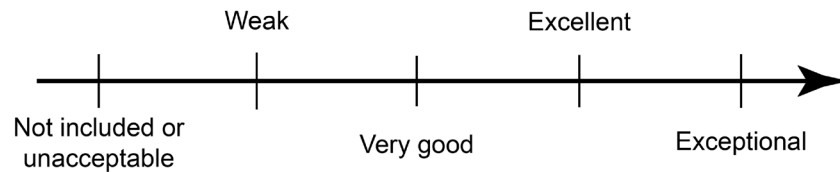
Below is a feedback form students received, along with their score out of 10 points.

Feedback Form

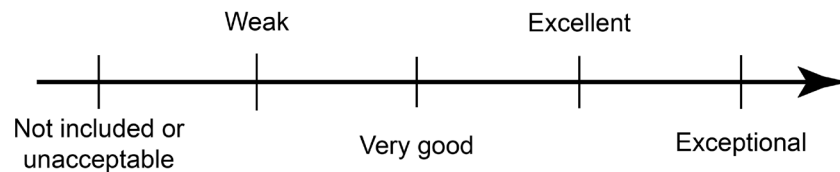
Question 6 asked: Which company appears to have the better future prospects at the most recent balance sheet dates, taking into consideration expected future ROEs, growth rates, and risks. Based on the information in the case and concepts covered thus far, there are excellent arguments on both sides. Hence, your responses were scored based on their overall merit and on the ratings below. You scored higher to the extent your analyses integrated business issues with patterns in the tabular data and your topic sentences were concise arguments (versus facts) substantiated with evidence, facts and/or logic.

The "X" on the scales below indicates how we rated this aspect of your response.

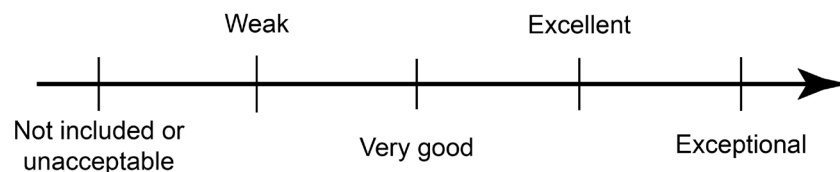
- **Expected future ROEs:**



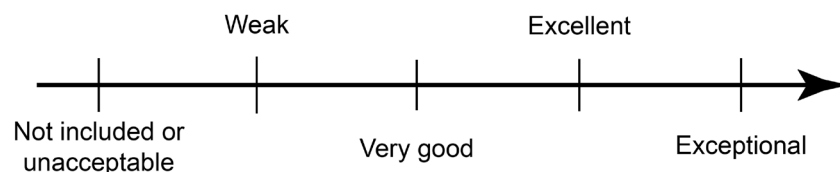
- **Expected future growth:**



- **Expected future risk:**



- **Other factors:** You rated higher on the scale below to the extent you raised other points that bolstered your position and we found them compelling.



- **Writing:** You rated higher on the scale below to the extent your response was well organized and written clearly, concisely, and persuasively.

