2007-2008

ACY1111 Suggested Solution

Problem 1

(a) ABC Engineering Co.

Bank Reconciliation Statement at October 31, 2006

Cash Balance per Bank Statement	$21,762.7
Add: Deposit-in-transit	2,727.3
	24,490
Less: Outstanding Checks	
#1780	(1,425.9)
#1786	(353.1)
#1789	(639.5)
Adjusted Cash Balance per Bank	$22,071.5
Cash Balance per Book	$15,177.3
Add: Collection of Note Receivable	7,300
Collection of Interest	100
	22,577.3
Less: Error in recording Utilities Expense	(10)
NSF Check	(431.8)
Note Collection Fee	(50)
Bank Service Charge	(14)
Adjusted Cash Balance per Book	$22,071.5

(b)

Date	Details	Dr. ($)	Cr. ($)
2006			
Oct 31	Utilities Expense	10	
	Cash		10
	Accounts Receivables	431.8	
	Cash		431.8
	Cash	7,350	
	Collection Fee	50	
	Note Receivable		7,300

	Interest Income		100
Bank Service Charge		14	
	Cash		14

Problem 2

(a)

Date	Details	Dr. ($)	Cr. ($)
2006			
Jul 10	Allowance for Doubtful Accounts	2,000	
	Accounts Receivable		2,000
Sept 20	Allowance for Doubtful Accounts	9,000	
	Accounts Receivable		9,000
Nov 10	Accounts Receivable	2,000	
	Allowance for Doubtful Accounts		2,000
	Cash	900	
	Accounts Receivable		900
Nov 15	Cash	1,100	
	Accounts Receivable		1,100

(b)

Date	Details	Dr. ($)	Cr. ($)
2006			
Dec 31	Bad Debt Expense	22,000	
	Allowance for Doubtful Debts		22,000

Allowance for Doubtful Accounts

	$2,000		$10,000
	9,000		2,000
			22,000
		Bal.	$23,000

(c)

Date	Details	Dr. ($)	Cr. ($)
2006			
Dec 31	Bad Debt Expense	18,900	
	Allowance for Doubtful Accounts		18,900

Allowance for Doubtful Accounts

	$2,000		$10,000
	9,000		2,000
			18,900
		Bal.	$19,900

Problem 3

Part A

Date	Details	Dr. ($)	Cr. ($)
2004			
Jan 1	Computer	12,800	
	Cash		12,800
Dec 31	Depreciation Expense-Computer	2,700	
	Accumulated Depreciation-Computer		2,700
2005			
Dec 31	Depreciation Expense-Computer	2,700	
	Accumulated Depreciation-Computer		2,700
2006			
Jan 1	Computer	2,760	
	Cash		2,760
Jul 1	Depreciation Expense-Computer	2,040	
	Accumulated Depreciation-Computer		2,040
	Accumulated Depreciation-Computer	7,440	
	Computer	6,000	
	Loss on Disposal	2,120	
	Computer		15,560
	Computer	12,000	
	Cash		12,000
Dec 31	Depreciation Expense-Computer	1,875	
	Accumulated Depreciation-Computer		1,875

Part B

Date	Details	Dr. ($)	Cr. ($)
2004			
Feb 1	Truck	81,000	

	Cash		81,000
Dec 31	Depreciation Expense-Truck	29,700	
	Accumulated Depreciation-Truck		29,700
	81,000 x40% x$\frac{11}{12}$		
2005			
Nov 1	Depreciation Expense-Truck	17,280	
	Accumulated Depreciation-Truck		17,280
	81,000 x40% x$\frac{1}{12}$ + (81,000-32,400) x40% x$\frac{9}{12}$		
	Accumulated Depreciation-Truck	46,980	
	Cash	35,000	
	Truck		81,000
	Gain on Disposal		980

Part C

Date	Details	Dr. ($)	Cr. ($)
2005			
Jan 2	Machinery	86,000	
	Cash		86,000
Dec 31	Depreciation Expense-Machinery	19,000	
	Accumulated Depreciation-Machinery		19,000
2006			
Jan 2	Machinery	5,000	
	Cash		5,000
Dec 31	Depreciation Expense-Machinery	16,500	
	Accumulated Depreciation-Machinery		16,500
	$\frac{86,000 - 19,000 + 5,000 - 6,000}{4}$		
	Accumulated Depreciation-Machinery	35,500	
	Machinery	60,000	
	Machinery		86,000
	Gain on Disposal		9,500
	Machinery	100,000	
	Cash		100,000

Problem 4

(a)

Date	Details	Dr. ($)	Cr. ($)
2006			
Jan 25	Cash	2,400,000	
	Common Stock		600,000
	Paid-in Capital in excess of Stated Value		1,800,000
Feb 18	Retained Earnings	600,000	
	Dividends Payable-Preferred		360,000
	3,000,000 x6% x2		
	Dividends Payable-Common		240,000
Mar 15	Dividends Payable-Preferred	360,000	
	Dividends Payable-Common	240,000	
	Cash		600,000
May 20	Retained Earnings	1,840,000	
	Common Stock Dividends Distributable		460,000
	Paid-in Capital in excess of Stated Value		1,380,000
Jun 15	Common Stock Dividends Distributable	460,000	
	Common Stock		460,000
Oct 7	Treasury Stock	1,900,000	
	Cash		1,900,000
Dec 31	Income Summary	1,000,000	
	Retained Earnings		1,000,000

(b)

Items	Computations	Value ($)
Common Stock	4,000,000 +600,000+ 460,000	5,060,000
Paid-in Capital in excess of Stated Value-Common	12,000,000 +1,800,000 +1,380,000	15,180,000
Retained Earnings	4,100,000 -600,000 -1,840,000 +1,000,000	2,660,000
Treasury Stock-Common		1,900,000

Problem 5

(a)

Items	Computations	Value
Debt to Total Assets	$\frac{850,000}{1,415,660}$	0.6
Profit Margin	$\frac{82,642}{2,800,300}$	0.03
Average Collection Period	$\frac{(250,000+296,500)\div 2}{2,800,300}$ x365	35.62 days
Times Interest Earned	$\frac{208,060}{90,000}$	2.31
Current Ratio	$\frac{1,415,660\ -803,500\ -85,760}{560,000}$	0.94:1
Return on Assets	$\frac{82,642}{(1,189,870+1,415,660)\div 2}$	0.06

(b)

1. Liquidity

Great Value Discount Store Inc. has a shorter average collection period of 20.73 days when compared to Crystal Department Store Inc.'s 35.62 days. Great Value has a higher efficiency in collecting debts. It has a higher liquidity on receivables.

At the same time, Great Value has a better current ratio (2.22:1) than Crystal (0.94:1). It has a higher short-term debt-paying ability and thus a lower risk of getting bankrupt. Based on these two ratios, we can conclude that Great Value Discount Store Inc. has a better liquidity.

2. Profitability

Crystal has a higher profit margin (0.03) while that of Great Value is only 0.017. More net income is generated by Crystal for each dollar of sales.

Meanwhile, the return on assets of Crystal is 0.06 but that of Great Value is only 0.03. This shows that assets of Crystal are used more efficiently. Crystal has a higher general profitability of assets. Therefore, Crystal Department Store Inc. has a better profitability.

3. Solvency

Great Value has a lower debt to assets ratio (0.39) while Crystal has a ratio of 0.6. Great Value has a smaller percentage of assets supplied by creditors. Hence, it has a higher ability in meeting its liabilities. Great Value has a higher times interest earned

ratio (3.95) while that of Crystal is 2.31. Great Value's lenders have a lower risk that the company can't pay them the required interest payments when profits fall. In accordance with these two ratios, we can conclude that Great Value has a better solvency.

(c) As a part of the bank, my main concern is the liquidity of the company which shows the degree of risks the bank has to bear after granting the short-term loans. After reviewing the financial performance of these two companies, I would prefer to lend money to Great Value Discount Store Inc. as it has a better liquidity and better solvency. It has a higher ability in repaying its debts.