

CHAPTER 4

INCOME STATEMENT AND RELATED INFORMATION

1. The income statement is useful for helping to assess the risk or uncertainty of achieving future cash flows.
2. A strength of the income statement as compared to the statement of financial position is that items that cannot be measured reliably can be reported in the income statement.
3. Earnings management generally makes income statement information more useful for predicting future earnings and cash flows.
4. The transaction approach of income measurement focuses on the income-related activities that have occurred during the period.
5. Income from operations represents a company's results before any gain or loss on discontinued operations.
6. Both revenues and gains increase both net income and equity.
7. Companies frequently report income tax as the last item before net income on the income statement.
8. The income statement presents subtotals for gross profit, income before continuing operations, income before income tax, and net income.
9. The nature-of-expense method identifies the major cost drivers and helps users to assess whether these amounts are appropriate for the revenue generated.
10. Income before income taxes is computed by deducting interest expense from income from operations.
11. The IASB takes the position that both revenues and expenses and other income and expense should be reported as part of income from operations.
12. Companies report the results of operations of a component of a business that will be disposed of separately from continuing operations.
13. Discontinued operations and gains and losses are both reported net of tax in the income statement.
14. A company that reports a discontinued operation has the option of reporting per share amounts for this item.
15. Intraperiod tax allocation relates the income tax expense of the period to the specific items that give rise to the amount of the tax provision.
16. A company recognizes a change in estimate by making a retrospective adjustment to the financial statements.
17. Prior period adjustments can either be added or subtracted in the Retained Earnings Statement.
18. Companies only restrict retained earnings to comply with contractual requirements or current necessity.
19. Comprehensive income includes all changes in equity during a period except those resulting from distributions to owners.
20. Comprehensive income can be reported in a statement of changes in equity.

MULTIPLE CHOICE—Conceptual

21. The major elements of the income statement are
 - a. revenue, cost of goods sold, selling expenses, and general expense.
 - b. operating section, nonoperating section, discontinued operations and cumulative effect.
 - c. revenues, expenses, gains, and losses.
 - d. All of these.
22. Information in the income statement helps users to
 - a. evaluate the past performance of the enterprise.
 - b. provide a basis for predicting future performance.
 - c. help assess the risk or uncertainty of achieving future cash flows.
 - d. All of these.
23. Limitations of the income statement include all of the following *except*
 - a. items that cannot be measured reliably are not reported.
 - b. only actual amounts are reported in determining net income.
 - c. income measurement involves judgment.
 - d. income numbers are affected by the accounting methods employed.
- ^s24. Which of the following would represent the least likely use of an income statement prepared for a business enterprise?
 - a. Use by customers to determine a company's ability to provide needed goods and services.
 - b. Use by labor unions to examine earnings closely as a basis for salary discussions.
 - c. Use by government agencies to formulate tax and economic policy.
 - d. Use by investors interested in the financial position of the entity.
- ^s25. The income statement reveals
 - a. resources and equities of a firm at a point in time.
 - b. resources and equities of a firm for a period of time.
 - c. net earnings (net income) of a firm at a point in time.
 - d. net earnings (net income) of a firm for a period of time.
26. The income statement information would help in which of the following tasks?
 - a. Evaluate the liquidity of a company.
 - b. Evaluate the solvency of a company.
 - c. Estimate future cash flows.
 - d. Estimate future financial flexibility.
27. Which of the following is an example of managing earnings down?
 - a. Changing estimated bad debts from 3 percent to 2.5 percent of sales.
 - b. Revising the estimated life of equipment from 10 years to 8 years.
 - c. Not writing off obsolete inventory.
 - d. Reducing research and development expenditures.
28. Which of the following is an example of managing earnings up?
 - a. Decreasing estimated salvage value of equipment.
 - b. Writing off obsolete inventory.
 - c. Underestimating warranty claims.
 - d. Accruing a contingent liability for an ongoing lawsuit.
29. What might a manager do during the last quarter of a fiscal year if she wanted to improve current annual net income?
 - a. Increase research and development activities.
 - b. Relax credit policies for customers.
 - c. Delay shipments to customers until after the end of the fiscal year.
 - d. Delay purchases from suppliers until after the end of the fiscal year.
30. What might a manager do during the last quarter of a fiscal year if she wanted to decrease current annual net income?
 - a. Delay shipments to customers until after the end of the fiscal year.
 - b. Relax credit policies for customers.
 - c. Pay suppliers all amounts owed.
 - d. Delay purchases from suppliers until after the end of the fiscal year.

31. The income statement provides investors and creditors information that helps them predict
 - a. the amounts of future cash flows.
 - b. the timing of future cash flows.
 - c. the uncertainty of future cash flows.
 - d. All of the above.
32. Investors and creditors use income statement information for each of the following except to
 - a. evaluate the future performance of the company.
 - b. provide a basis for predicting future performance.
 - c. help assess the risk and uncertainty of achieving future cash flows.
 - d. All of the above.
33. The planned timing of revenues, expenses, gains, and losses to smooth out bumps in earnings is the definition of
 - a. quality of earnings.
 - b. earnings management.
 - c. smoothing of earnings.
 - d. earnings averaging.
34. Which of the following situations involving different accounting methods or accounting estimates results in comparison difficulties between companies?
 - a. Estimated useful lives for depreciable assets.
 - b. Inventory methods.
 - c. Estimates of bad debts.
 - d. All of the above.
35. Which method of income measurement is used in the preparation of the income statement?
 - a. Capital maintenance approach.
 - b. Transaction approach.
 - c. Cash-flow approach.
 - d. Income components approach.
36. Which of the following equations expresses the definition of "income"?
 - a. $\text{Income} = \text{Revenues} - \text{Expenses}$
 - b. $\text{Income} = (\text{Revenues} + \text{Gains}) - (\text{Expenses} + \text{Losses})$
 - c. $\text{Income} = \text{Revenues} + \text{Gains}$
 - d. $\text{Income} = \text{Gains} - \text{Losses}$
37. Which of the following is not required to be presented on the income statement under IFRS?
 - a. Revenue.
 - b. Other gains/losses.
 - c. Finance costs.
 - d. Tax expense.
38. The non-controlling interest section of the income statement is shown
 - a. below net income.
 - b. below income from operations.
 - c. above other income and expenses.
 - d. above income tax.
39. The definition of expenses includes
 - a. losses only.
 - b. expenses and losses.
 - c. expenses only.
 - d. expenses, losses and unrealized losses on available-for-sale securities.
40. IFRS requires that a single amount be disclosed within the income statement for
 - a. the post-tax profit/loss on discontinued operations and the pre-tax gain/loss on the disposal of discontinued operational assets.
 - b. the pre-tax profit/loss on discontinued operations and the post-tax gain/loss on the disposal of discontinued operational assets.
 - c. the pre-tax profit/loss on discontinued operations and the pre-tax gain/loss on the disposal of discontinued operational assets.
 - d. the post-tax profit/loss on discontinued operations and the post-tax gain/loss on the disposal of discontinued operational assets.
41. Which of the following is *not* a generally practiced method of presenting the income statement?
 - a. Including prior period adjustments in determining net income.
 - b. The condensed income statement.
 - c. The consolidated income statement.
 - d. Including gains and losses from discontinued operations of a component of a business in determining net income.
42. The occurrence which most likely would have no effect on 2011 net income (assuming that all amounts involved are material) is the
 - a. sale in 2011 of an office building contributed by a stockholder in 1983.
 - b. collection in 2011 of a receivable from a customer whose account was written off in 2010 by a charge to the allowance account.
 - c. settlement based on litigation in 2011 of previously unrecognized damages from a serious accident which occurred in 2009.
 - d. worthlessness determined in 2011 of stock purchased on a speculative basis in 2007.
- ^s43. The occurrence that most likely would have no effect on 2011 net income is the
 - a. sale in 2011 of an office building contributed by a stockholder in 1962.
 - b. collection in 2011 of a dividend from an investment.
 - c. correction of an error in the financial statements of a prior period discovered subsequent to their issuance.
 - d. stock purchased in 1997 deemed worthless in 2011.
- ^p44. Which of the following is *not* a selling expense?
 - a. Advertising expense.
 - b. Office salaries expense.
 - c. Freight-out.
 - d. Store supplies consumed.
- ^p45. The accountant for the Lintz Sales Company is preparing the income statement for 2011 and the statement of financial position at December 31, 2011. The January 1, 2011, merchandise inventory balance will appear
 - a. only as an asset on the statement of financial position.
 - b. only in the cost of goods sold section of the income statement.

- c. as a deduction in the cost of goods sold section of the income statement and as a current asset on the statement of financial position.
 - d. as an addition in the cost of goods sold section of the income statement and as a current asset on the statement of financial position.
46. In which section of the income statement is interest expense reported?
- a. Gross profit.
 - b. Income from operations.
 - c. Income before income taxes.
 - d. Non-controlling interest.
47. If a company prepares a consolidated income statement, IFRS requires that net income be reported for
- a. the majority interest only.
 - b. the minority interest only.
 - c. both the majority interest and the minority interest.
 - d. as a single amount only.
48. Earnings per share relate to
- a. preference shares only.
 - b. ordinary shares only.
 - c. both preference and ordinary shares.
 - d. neither preference nor ordinary shares.
49. Undeclared dividends are deducted from net income in the earnings per share computation for which type of preference shares?
- a. Non-cumulative only.
 - b. Cumulative only.
 - c. Neither non-cumulative nor cumulative.
 - d. Both non-cumulative and cumulative.
50. The earnings per share computation is **not** required for
- a. Net income.
 - b. Gain on disposal of discontinued operation, net of tax.
 - c. Income from continuing operations.
 - d. Income from operations.
51. Given the following income statement line items:
- Income from operations
 - Income before income taxes
 - Income from continuing operations
 - Income from discontinued operations
 - Net income
- How many earnings per share amounts are required to be disclosed?
- a. 5
 - b. 5
 - c. 3
 - d. 2
52. Which of the following earnings per share figures must be disclosed on the face of the income statement?
- a. EPS for income before taxes.
 - b. The effect on EPS from unusual items.
 - c. EPS for gross profit.
 - d. EPS for income from continuing operations.
53. Earnings per share should always be shown separately for
- a. net income and gross profit.
 - b. net income and pretax income.
 - c. income from continuing operations.
 - d. discontinued operations and prior period adjustments.
54. Which of the following is a required disclosure in the income statement when reporting the disposal of a component of the business?
- a. The gain or loss on disposal should be reported as an other income item.
 - b. Results of operations of a discontinued component should be disclosed immediately below income from operations.
 - c. Earnings per share from both continuing operations and net income should be disclosed on the face of the income statement.
 - d. The gain or loss on disposal should not be segregated, but should be reported together with the results of continuing operations.
55. When a company discontinues an operation and disposes of the discontinued operation (component), the transaction should be included in the income statement as a gain or loss on disposal reported as
- a. a prior period adjustment.
 - b. an other income and expense item.
 - c. an amount after continuing operations and before net income.
 - d. a bulk sale of plant assets included in income from continuing operations.
56. Gains or losses on the disposal of investments should be shown in the income statement
- | | <u>Net of Tax</u> | <u>Disclosed Separately</u> |
|----|-------------------|-----------------------------|
| a. | No | No |
| b. | Yes | Yes |
| c. | No | Yes |
| d. | Yes | No |
57. Income taxes are allocated to
- a. continuing operations.
 - b. discontinued operations.
 - c. prior period adjustments.
 - d. All of these.
58. Which of the following is true about intraperiod tax allocation?
- a. It arises because certain revenue and expense items appear in the income statement either before or after they are included in the tax return.
 - b. It is required for the cumulative effect of accounting changes but not for prior period adjustments.
 - c. Its purpose is to allocate income tax expense evenly over a number of accounting periods.
 - d. Its purpose is to relate the income tax expense to the items which affect the amount of tax.

59. Companies use intraperiod tax allocation for all of the following items except
- discontinued operations.
 - prior period adjustments.
 - changes in accounting estimates.
 - income from continuing operations.
60. A change in accounting principle requires what kind of adjustment to the financial statements?
- Current period adjustment.
 - Prospective adjustment.
 - Retrospective adjustment.
 - Current and prospective adjustment.
61. A change in accounting principle requires that the cumulative effect of the change for prior periods be shown as an adjustment to
- beginning retained earnings for the earliest period presented.
 - net income for the period in which the change occurred.
 - comprehensive income for the earliest period presented.
 - stockholders' equity for the period in which the change occurred.
62. Changes in estimates affect reported amounts
- retrospectively only.
 - prospectively only.
 - currently and prospectively.
 - currently and retrospectively.
63. Prior years income statements are not restated for
- changes in accounting principle.
 - changes in estimates.
 - corrections of errors.
 - Any of the above.
64. In 2011, Milford Corporation determined that it overstated salaries payable and salaries expense by \$20,000 in 2010. In 2011, which of the following accounts will have to be credited to correct this error?
- Salaries Payable.
 - Salaries Expense.
 - Retained Earnings.
 - Income Summary.
65. Which of the following **does not** appear on a statement of retained earnings?
- Net loss.
 - Prior period adjustments.
 - Preference share dividends.
 - Other comprehensive income.
66. Which of the following would appear first in a statement of retained earnings?
- Net income.
 - Prior period adjustment.
 - Cash dividends.
 - Share dividends.
67. A correction of an error in prior periods' income will be reported
- | | <u>In the income statement</u> | <u>Net of tax</u> |
|----|--------------------------------|-------------------|
| a. | Yes | Yes |
| b. | No | No |
| c. | Yes | No |
| d. | No | Yes |
68. Which of the following items will *not* appear in the retained earnings statement?
- Net loss.
 - Prior period adjustment.
 - Discontinued operations.
 - Dividends.
69. Watts Corporation made a very large arithmetical error in the preparation of its year-end financial statements by improper placement of a decimal point in the calculation of depreciation. The error caused the net income to be reported at almost double the proper amount. Correction of the error when discovered in the next year should be treated as
- an increase in depreciation expense for the year in which the error is discovered.
 - a component of income for the year in which the error is discovered, but separately listed on the income statement and fully explained in a note to the financial statements.
 - an other expense item for the year in which the error was made.
 - a prior period adjustment.
70. Which of the following is included in comprehensive income?
- Investments by owners.
 - Unrealized gains on available-for-sale securities.
 - Distributions to owners.
 - Changes in accounting principles.
71. Which of the following is not an acceptable way of displaying the components of other comprehensive income?
- Combined statement of retained earnings.
 - Second income statement.
 - Combined statement of comprehensive income.
 - All of the above are acceptable.
72. Comprehensive income includes all of the following *except*
- dividend revenue.
 - losses on disposal of assets.
 - investments by owners.
 - unrealized holding gains.
73. Comprehensive income includes all of the following, except
- revenues and gains.
 - expenses and losses.
 - preference share dividends.
 - unrealized gains and losses on available-for-sale securities.

74. Under IFRS other comprehensive income must be displayed (reported) in
- the equity section of the statement of financial position.
 - a second income statement.
 - the income statement.
 - retained earnings the statement.

MULTIPLE CHOICE—Computational

75. Ortiz Co. had the following account balances:
- | | |
|----------------------|------------|
| Sales | \$ 120,000 |
| Cost of goods sold | 60,000 |
| Salary expense | 10,000 |
| Depreciation expense | 20,000 |
| Dividend revenue | 4,000 |
| Utilities expense | 8,000 |
| Rental revenue | 20,000 |
| Interest expense | 12,000 |
| Sales returns | 11,000 |
| Advertising expense | 13,000 |

What amount would Ortiz report as other income and expense in its income statement?

- \$24,000
 - \$12,000
 - \$49,000
 - \$10,000
76. Ortiz Co. had the following account balances:
- | | |
|----------------------|------------|
| Sales | \$ 120,000 |
| Cost of goods sold | 60,000 |
| Salary expense | 10,000 |
| Depreciation expense | 20,000 |
| Dividend revenue | 4,000 |
| Utilities expense | 8,000 |
| Rental revenue | 20,000 |
| Interest expense | 12,000 |
| Sales returns | 11,000 |
| Advertising expense | 13,000 |

What amount would Ortiz report as income from operations in its income statement?

- \$49,000
 - \$30,000
 - \$22,000
 - \$10,000
77. For Mortenson Company, the following information is available:
- | | |
|--------------------|-----------|
| Cost of goods sold | \$ 60,000 |
| Sales discounts | 2,000 |
| Income tax expense | 6,000 |
| Operating expenses | 23,000 |
| Sales | 100,000 |

In Mortenson's income statement, gross profit

- should not be reported.
 - should be reported at \$9,000.
 - should be reported at \$38,000.
 - should be reported at \$40,000.
78. For Rondelli Company, the following information is available:
- | | |
|------------------------------|-----------|
| Cost of goods sold | \$ 90,000 |
| Sales returns and allowances | 4,000 |
| Income tax expense | 9,000 |
| Operating expenses | 35,000 |
| Sales | 150,000 |
- In Rondelli's income statement, gross profit
- should not be reported.
 - should be reported at \$12,000.
 - should be reported at \$56,000.
 - should be reported at \$60,000.
79. Gross billings for merchandise sold by Lang Company to its customers last year amounted to \$15,720,000; sales returns and allowances were \$370,000, sales discounts were \$175,000, and freight-out was \$140,000. Net sales last year for Lang Company were
- \$15,720,000.
 - \$15,350,000.
 - \$15,175,000.
 - \$15,035,000.
80. Use the following information (in thousands):
- | | |
|-----------------------------------|------------|
| Revenues | ¥1,200,000 |
| Income from continuing operations | 150,000 |
| Net Income | 135,000 |
| Income from operations | 330,000 |
| Selling & administrative expenses | 750,000 |
| Income before income tax | 300,000 |
- Determine the amount of other income and expense.
- | | |
|-------------|-------------|
| a. ¥30,000 | c. ¥150,000 |
| b. ¥120,000 | d. ¥15,000 |

81. Use the following information (in thousands):

Revenues	¥1,200,000
Income from continuing operations	150,000
Net Income	135,000
Income from operations	330,000
Selling & administrative expenses	750,000
Income before income tax	300,000

Determine the amount of financing costs.

a. ¥30,000

b. ¥15,000

c. ¥150,000

d. ¥120,000
82. Use the following information (in thousands):

Revenues	¥1,200,000
Income from continuing operations	150,000
Net Income	135,000
Income from operations	330,000
Selling & administrative expenses	750,000
Income before income tax	300,000

Determine the amount of income tax.

a. ¥30,000

b. ¥15,000

c. ¥150,000

d. ¥120,000
83. Use the following information (in thousands):

Revenues	¥1,200,000
Income from continuing operations	150,000
Net Income	135,000
Income from operations	330,000
Selling & administrative expenses	750,000
Income before income tax	300,000

Determine the amount of discontinued operations.

a. ¥(30,000)

b. ¥120,000

c. ¥150,000

d. ¥(15,000)
84. Use the following information (in thousands):

Sales revenue	¥150,000
Gain on sale of equipment	45,000
Cost of goods sold	82,000
Interest expense	8,000
Selling & administrative expenses	15,000
Income tax rate	30%

Determine the amount of income from operations.

a. ¥38,000

b. ¥98,000

c. ¥30,000

d. ¥90,000
85. Use the following information (in thousands):

Sales revenue	¥150,000
Gain on sale of equipment	45,000
Cost of goods sold	82,000
Interest expense	8,000
Selling & administrative expenses	15,000
Income tax rate	30%

Determine the amount of income before taxes.

a. ¥38,000

b. ¥98,000

c. ¥30,000

d. ¥90,000
86. Use the following information (in thousands):

Sales revenue	¥150,000
Gain on sale of equipment	45,000
Cost of goods sold	82,000
Interest expense	8,000
Selling & administrative expenses	15,000
Income tax rate	30%

Determine the amount of income taxes.

a. ¥4,000

b. ¥9,000

c. ¥13,500

d. ¥27,000
87. Use the following information (in thousands):

Sales revenue	¥150,000
Gain on sale of equipment	45,000
Cost of goods sold	82,000
Interest expense	8,000
Selling & administrative expenses	15,000
Income tax rate	30%

Determine the amount of net income.

- a. ¥63,000
b. ¥10,500
c. ¥21,000
d. ¥31,500
88. Majors Corporation had income from continuing operations of \$1,600,000 in 2011. During 2011 it disposed of its repair division at a pre-tax gain of \$27,000. Prior to disposal, the division operated at a pre-tax loss of \$45,000. The tax rate was 30%. What is the question here?
a. \$1,582,000
b. \$1,528,000
c. \$1,549,600
d. \$1,587,400
89. Manning Company has the following items: write-down of inventories, \$120,000; loss on disposal of part of Sports Division, \$185,000; and loss on restructurings, \$113,000. Ignoring income taxes, what total amount should Manning Company report as other income and expense?
a. \$418,000
b. \$185,000
c. \$233,000
d. \$298,000
90. Garwood Company has the following items: write-down of inventories, \$240,000; loss on disposal of part of Sports Division, \$370,000; and loss due to an asset impairment, \$226,000. Ignoring income taxes, what total amount should Garwood Company report as other income and expense?
a. \$836,000
b. \$370,000
c. \$466,000
d. \$596,000
91. At Ruth Company, events and transactions during 2011 included the following. The tax rate for all items is 30%.
(1) Depreciation for 2009 was found to be understated by \$30,000.
(2) A litigation settlement resulted in a loss of \$25,000.
(3) The inventory at December 31, 2009 was overstated by \$40,000.
(4) The company disposed of its recreational division at a loss of \$500,000.
The effect of these events and transactions on 2011 income from continuing operations net of tax would be
a. \$17,500.
b. \$38,500.
c. \$66,500.
d. \$416,500.
92. At Ruth Company, events and transactions during 2011 included the following. The tax rate for all items is 30%.
(1) Depreciation for 2009 was found to be understated by \$30,000.
(2) A litigation settlement resulted in a loss of \$25,000.
(3) The inventory at December 31, 2009 was overstated by \$40,000.
(4) The company disposed of its recreational division at a loss of \$500,000.
The effect of these events and transactions on 2011 net income net of tax would be
a. \$17,500.
b. \$367,500.
c. \$388,500.
d. \$416,500.
93. During 2011, Lopez Corporation disposed of Pine Division, a major component of its business. Lopez realized a gain of \$1,200,000, net of taxes, on the sale of Pine's assets. Pine's operating losses, net of taxes, were \$1,400,000 in 2011. How should these facts be reported in Lopez's income statement for 2011?
- | Total Amount to be Included in | |
|--------------------------------------|---------------------------------------|
| Income from
Continuing Operations | Results of
Discontinued Operations |
| a. \$1,400,000 loss | \$1,200,000 gain |
| b. 200,000 loss | 0 |
| c. 0 | 200,000 loss |
| d. 1,200,000 gain | 1,400,000 loss |
94. In 2011, Esther Corporation reported net income of \$1,000,000. It declared and paid preference dividends of \$250,000 and ordinary share dividends of \$100,000. During 2011, Esther had a weighted average of 200,000 ordinary shares outstanding. Compute Esther's 2011 earnings per share.
a. \$3.25
b. \$3.75
c. \$5.00
d. \$6.25
95. In 2011, Linz Corporation reported a discontinued operations loss of \$1,000,000, net of tax. It declared and paid preference dividends of \$100,000 and ordinary share dividends of \$300,000. During 2011, Linz had a weighted average of 200,000 ordinary shares outstanding. Compute the effect of the discontinued operations loss, net of tax, on earnings per share.
a. \$3.00
b. \$3.50
c. \$4.50
d. \$5.00
96. In 2011, Benfer Corporation reported net income of \$350,000. It declared and paid ordinary share dividends of \$40,000 and had a weighted average of 70,000 ordinary shares outstanding. Compute the earnings per share to the nearest cent.
a. \$4.43
b. \$3.50
c. \$4.50
d. \$5.00
97. Benedict Corporation reports the following information:
- | | |
|--|-----------|
| Net income | \$500,000 |
| Dividends on ordinary shares | 140,000 |
| Dividends on preference shares | 60,000 |
| Weighted average ordinary shares outstanding | 100,000 |

Benedict should report earnings per share of

- a. \$3.00.
- b. \$3.60.
- c. \$4.40.
- d. \$5.00.

98. Norling Corporation reports the following information:

Net income	\$500,000
Dividends on ordinary shares	140,000
Dividends on preference shares	60,000
Weighted average ordinary shares outstanding	200,000

Norling should report earnings per share of

- a. \$1.50.
- b. \$1.80.
- c. \$2.20.
- d. \$2.50.

99. In 2011, Timmons Company reported net income of £2,000,000. It declared and paid preference share dividends of £200,000 and ordinary share dividends of £250,000. During 2011, Timmons had a weighted average of 150,000 ordinary shares outstanding. The 2011 earning per share for Timmons Company is:.

- a. £13.33
- b. £12.00
- c. £11.67
- d. £10.33

100. Given the following:

Net income	\$600,000
EPS	4.25
Dividend/ordinary shares	2.00
Weighted average ordinary shares outstanding	120,000

Determine the amount of the preference share dividend.

- a. \$360,000
- b. \$240,000
- c. \$120,000
- d. \$90,000

101. Use the following information:

Gross profit	£7,800,000
Loss on sale of investments	20,000
Interest expense	15,000
Gain on sale of discontinued operations	60,000
Income tax rate	20%

Compute the amount of income tax applicable to continuing operations.

- a. £1,553,000
- b. £1,640,000
- c. £1,569,000
- d. £1,568,000

102. Use the following information:

Gross profit	£7,800,000
Loss on sale of investments	20,000
Interest expense	15,000
Gain on sale of discontinued operations	60,000
Income tax rate	20%

Compute the amount of discontinued operations to be combined with income from continuing operations on the income statement.

- a. £60,000
- b. £48,000
- c. £12,000
- d. None of the above.

103. Use the following information:

Gross profit	£7,800,000
Loss on sale of investments	20,000
Interest expense	15,000
Gain on sale of discontinued operations	60,000
Income tax rate	20%

Compute the total amount of income tax expense experienced by the company.

- a. £1,530,000
- b. £1,600,000
- c. £1,565,000
- d. £2,010,000

104. Sandstrom Corporation has a discontinued operations loss of \$50,000, an unusual gain of \$35,000, and a tax rate of 40%. At what amount should Sandstrom report each item?

	<u>Discontinued loss</u>	<u>Unusual gain</u>
a.	\$(50,000)	\$35,000
b.	(50,000)	21,000
c.	(30,000)	35,000
d.	(30,000)	21,000

105. Prophet Corporation has a discontinued operations loss of \$200,000, an unusual gain of \$140,000, and a tax rate of 40%. At what amount should Prophet report each item?

	<u>Discontinued loss</u>	<u>Unusual gain</u>
a.	\$(200,000)	\$140,000
b.	(200,000)	84,000
c.	(120,000)	140,000
d.	(120,000)	84,000

106. Arreaga Corp. has a tax rate of 40 percent and income before non-operating items of \$232,000. It also has the following items (gross amounts).

Unusual loss	\$ 37,000
Discontinued operations loss	101,000
Gain on disposal of equipment	8,000
Change in accounting principle increasing prior year's income	53,000

What is the amount of income tax expense Arreaga would report on its income statement?

- a. \$92,800
- b. \$81,200
- c. \$99,200
- d. \$62,000

107. Palomo Corp has a tax rate of 30 percent and income before non-operating items should this be income from operations of \$357,000. It also has the following items (gross amounts).

Unusual gain	\$ 23,000
Loss from discontinued operations	183,000
Dividend revenue	6,000
Income increasing prior period adjustment	74,000

What is the amount of income tax expense Palomo would report on its income statement?

- a. \$115,800
- b. \$ 60,900
- c. \$ 83,100
- d. \$108,900

108. Lantos Company had a 40 percent tax rate. Given the following pre-tax amounts, what would be the income tax expense reported on the face of the income statement?

Sales	\$ 100,000
Cost of goods sold	60,000
Salary expense	8,000
Depreciation expense	11,000
Dividend revenue	9,000
Utilities expense	1,000
Loss from discontinued operations	10,000
Interest expense	2,000

- a. \$10,800
- b. \$ 6,800
- c. \$ 7,200
- d. \$ 3,200

109. Moorman Corporation reports the following information:

Correction of understatement of depreciation expense in prior years, net of tax	\$ 430,000
Dividends declared	320,000
Net income	1,000,000
Retained earnings, 1/1/11, as reported	2,000,000

Moorman should report retained earnings, January 1, 2011, as adjusted at

- a. \$1,570,000.
- b. \$2,000,000.
- c. \$2,430,000.
- d. \$3,110,000.

110. Moorman Corporation reports the following information:

Correction of understatement of depreciation expense in prior years, net of tax	\$ 430,000
Dividends declared	320,000
Net income	1,000,000
Retained earnings, 1/1/11, as reported	2,000,000

Moorman should report retained earnings, December 31, 2011, of

- a. \$1,570,000.
- b. \$2,250,000.
- c. \$2,680,000.
- d. \$3,110,000.

111. Leonard Corporation reports the following information:

Correction of overstatement of depreciation expense in prior years, net of tax	\$ 215,000
Dividends declared	160,000
Net income	500,000
Retained earnings, 1/1/11, as reported	1,000,000

Leonard should report retained earnings, January 1, 2011, as adjusted at

- a. \$785,000.
- b. \$1,000,000.
- c. \$1,215,000.
- d. \$1,555,000.

112. Leonard Corporation reports the following information:
- | | |
|---|------------|
| Correction of overstatement of depreciation expense
in prior years, net of tax | \$ 215,000 |
| Dividends declared | 160,000 |
| Net income | 500,000 |
| Retained earnings, 1/1/11, as reported | 1,000,000 |
- Leonard should report retained earnings, December 31, 2011, at
- \$785,000.
 - \$1,125,000.
 - \$1,340,000.
 - \$1,555,000.
113. The following information was extracted from the accounts of Essex Corporation at December 31, 2011:
- | | |
|---|---------------|
| | <u>CR(DR)</u> |
| Total reported income since incorporation | \$1,700,000 |
| Total cash dividends paid | (800,000) |
| Unrealized holding loss | (120,000) |
| Total share dividends distributed | (200,000) |
| Prior period adjustment, recorded January 1, 2011 | 75,000 |
- What should be the balance of retained earnings at December 31, 2011?
- \$655,000
 - \$700,000
 - \$580,000
 - \$775,000
114. Pullman Corporation had retained earnings of \$700,000 at January 1, 2011. During the year the company experienced a net loss of \$300,000 and declared cash dividends of \$80,000. Determine the retained earnings balance at December 31, 2011.
- \$920,000
 - \$400,000
 - \$1,000,000
 - \$320,000
115. Pullman Corporation had retained earnings of \$700,000 at January 1, 2011. During the year the company experienced a net loss of \$300,000 and declared cash dividends of \$80,000. It was discovered in 2011 that \$50,000 of repair expense was debited to the land account in 2010. The income tax rate is 20%. Determine the retained earnings balance at December 31, 2011.
- \$270,000
 - \$360,000
 - \$350,000
 - \$280,000
116. Rodriguez Corporation had retained earnings of \$750,000 at January 1, 2011. During the year the company generated a net income of \$150,000 and declared share dividends of \$50,000. It was discovered during 2011 that \$40,000 of closing costs on a 2010 purchase of land was debited to maintenance expense. The income tax rate is 30%. Determine the retained earnings balance at December 31, 2011.
- \$878,000
 - \$860,000
 - \$810,000
 - \$838,000
117. On January 1, 2011, Zhang Inc. had cash and share capital of ¥5,000,000. At that date, the company had no other asset, liability, or equity balances. On January 5, 2011, it purchased for cash ¥3,000,000 of equity securities that it classified as available-for-sale. It received cash dividends of ¥400,000 during the year on these securities. In addition, it has an unrealized loss on these securities of ¥300,000. The tax rate is 20%.
- Compute the amount of net income/(loss).
- ¥400,000
 - ¥320,000
 - ¥(100,000)
 - ¥80,000
118. On January 1, 2011, Zhang Inc. had cash and share capital of ¥5,000,000. At that date, the company had no other asset, liability, or equity balances. On January 5, 2011, it purchased for cash ¥3,000,000 of equity securities that it classified as available-for-sale. It received cash dividends of ¥400,000 during the year on these securities. In addition, it has an unrealized loss on these securities of ¥300,000. The tax rate is 20%.
- Compute the amount of comprehensive income.
- ¥100,000
 - ¥80,000
 - ¥320,000
 - ¥300,000
119. On January 1, 2011, Zhang Inc. had cash and share capital of ¥5,000,000. At that date, the company had no other asset, liability, or equity balances. On January 5, 2011, it purchased for cash ¥3,000,000 of equity securities that it classified as available-for-sale. It received cash dividends of ¥400,000 during the year on these securities. In addition, it has an unrealized loss on these securities of ¥300,000. The tax rate is 20%.
- Compute the amount of other comprehensive income/(loss).
- ¥240,000
 - ¥(300,000)
 - ¥100,000
 - ¥80,000
120. On January 1, 2011, Zhang Inc. had cash and share capital of ¥5,000,000. At that date, the company had no other asset, liability, or equity balances. On January 5, 2011, it purchased for cash ¥3,000,000 of equity securities that it classified as available-for-sale. It received cash dividends of ¥400,000 during the year on these securities. In addition, it has an unrealized loss on these securities of ¥300,000. The tax rate is 20%.

Compute the amount of accumulated other comprehensive income/(loss).

- a. ¥(300,000)
- b. ¥100,000
- c. ¥80,000
- d. ¥240,000

121. Madsen Company reported the following information for 2011:

Sales revenue	\$510,000
Cost of goods sold	350,000
Operating expenses	55,000
Unrealized holding gain on available-for-sale securities	40,000
Cash dividends received on the securities	2,000

For 2011, Madsen would report other comprehensive income of

- a. \$137,000.
- b. \$135,000.
- c. \$42,000.
- d. \$40,000.

122. Korte Company reported the following information for 2011:

Sales revenue	\$500,000
Cost of goods sold	350,000
Operating expenses	55,000
Unrealized holding gain on available-for-sale securities	20,000
Cash dividends received on the securities	2,000

For 2011, Korte would report comprehensive income of

- a. \$117,000.
- b. \$115,000.
- c. \$97,000.
- d. \$20,000.

123. For the year ended December 31, 2011, Transformers Inc. reported the following:

Net income	\$ 60,000
Preference dividends declared	10,000
Ordinary share dividends declared	2,000
Unrealized holding loss, net of tax	1,000
Retained earnings	80,000
Share capital – Ordinary	40,000
Accumulated Other Comprehensive Income, Beginning Balance	5,000

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

- a. \$6,000
- b. \$5,000
- c. \$4,000
- d. \$1,000

124. For the year ended December 31, 2011, Transformers Inc. reported the following:

Net income	\$ 60,000
Preference dividends declared	10,000
Ordinary share dividends declared	2,000
Unrealized holding loss, net of tax	1,000
Retained earnings, beginning balance	80,000
Share capital – Ordinary	40,000
Accumulated Other Comprehensive Income, Beginning Balance	5,000

What would Transformers report as the ending balance of Retained Earnings?

- a. \$139,000
- b. \$133,000
- c. \$128,000
- d. \$127,000

125. For the year ended December 31, 2011, Transformers Inc. reported the following:

Net income	\$ 60,000
Preference dividends declared	10,000
Ordinary share dividends declared	2,000
Unrealized holding loss, net of tax	1,000
Retained earnings, beginning balance	80,000
Share capital – Ordinary	40,000
Accumulated Other Comprehensive Income, Beginning Balance	5,000

What would Transformers report as total stockholders' equity?

- a. \$172,000
- b. \$168,000
- c. \$128,000
- d. \$120,000

MULTIPLE CHOICE—CPA Adapted

126. Perry Corp. reports operating expenses in two categories: (1) selling and (2) general and administrative. The adjusted trial balance at December 31, 2011, included the following expense accounts:

Accounting and legal fees	\$140,000
Advertising	120,000
Freight-out	75,000
Interest	60,000
Loss on sale of long-term investments	30,000
Officers' salaries	180,000
Rent for office space	180,000
Sales salaries and commissions	110,000

One-half of the rented premises is occupied by the sales department.

How much of the expenses listed above should be included in Perry's selling expenses for 2011?

- a. \$230,000
- b. \$305,000
- c. \$320,000
- d. \$395,000

127. Perry Corp. reports operating expenses in two categories: (1) selling and (2) general and administrative. The adjusted trial balance at December 31, 2011, included the following expense accounts:

Accounting and legal fees	\$140,000
Advertising	120,000
Freight-out	75,000
Interest	60,000
Loss on sale of long-term investments	30,000
Officers' salaries	180,000
Rent for office space	180,000
Sales salaries and commissions	110,000

One-half of the rented premises is occupied by the sales department.

How much of the expenses listed above should be included in Perry's general and administrative expenses for 2011?

- a. \$410,000
- b. \$440,000
- c. \$470,000
- d. \$500,000

128. Didde Corp. reports operating expenses in two categories: (1) selling and (2) general and administrative. The adjusted trial balance at December 31, 2011 included the following expense and loss accounts:

Accounting and legal fees	\$140,000
Advertising	180,000
Freight-out	80,000
Interest	70,000
Loss on sale of long-term investment	30,000
Officers' salaries	225,000
Rent for office space	220,000
Sales salaries and commissions	170,000

One-half of the rented premises is occupied by the sales department. Didde's total selling expenses for 2011 are

- a. \$540,000.
- b. \$460,000.
- c. \$430,000.
- d. \$370,000.

129. The following items were among those that were reported on Dye Co.'s income statement for the year ended December 31, 2011:

Legal and audit fees	\$130,000
Rent for office space	180,000
Interest on inventory floor plan	210,000
Loss on abandoned equipment used in operations	35,000

The office space is used equally by Dye's sales and accounting departments. What amount of the above-listed items should be classified as general and administrative expenses in Dye's income statement?

- a. \$220,000
- b. \$255,000
- c. \$310,000
- d. \$430,000

130. Logan Corp.'s trial balance of income statement accounts for the year ended December 31, 2011 included the following:

	Debit	Credit
Sales		\$140,000
Cost of sales	\$ 50,000	
Administrative expenses	25,000	
Loss on sale of equipment	9,000	
Commissions to salespersons	8,000	
Interest revenue		5,000
Freight-out	3,000	
Loss on disposition of wholesale division	12,000	
Bad debt expense	3,000	
Totals	<u>\$110,000</u>	<u>\$145,000</u>

Other information:

Logan's income tax rate is 30%. Finished goods inventory:

January 1, 2011	\$80,000
December 31, 2011	70,000

On Logan's income statement for 2011, cost of goods manufactured is

- a. \$63,000.
- b. \$60,000.
- c. \$43,000.
- d. \$40,000.

131. Logan Corp.'s trial balance of income statement accounts for the year ended December 31, 2011 included the following:

	<u>Debit</u>	<u>Credit</u>
Sales		\$140,000
Cost of sales	\$ 50,000	
Administrative expenses	25,000	
Loss on sale of equipment	9,000	
Commissions to salespersons	8,000	
Interest revenue		5,000
Freight-out	3,000	
Loss on disposition of wholesale division	12,000	
Bad debt expense	3,000	
Totals	<u>\$110,000</u>	<u>\$145,000</u>

Other information:

Logan's income tax rate is 30%. Finished goods inventory:

January 1, 2011	\$80,000
December 31, 2011	70,000

On Logan's income statement for 2011, income from continuing operations is

- a. \$64,000.
- b. \$35,000.
- c. \$47,000.
- d. \$24,500.

132. Logan Corp.'s trial balance of income statement accounts for the year ended December 31, 2011 included the following:

	<u>Debit</u>	<u>Credit</u>
Sales		\$140,000
Cost of sales	\$ 50,000	
Administrative expenses	25,000	
Loss on sale of equipment	9,000	
Commissions to salespersons	8,000	
Interest revenue		5,000
Freight-out	3,000	
Loss on disposition of wholesale division	12,000	
Bad debt expense	3,000	
Totals	<u>\$110,000</u>	<u>\$145,000</u>

Other information:

Logan's income tax rate is 30%. Finished goods inventory:

January 1, 2011	\$80,000
December 31, 2011	70,000

On Logan's income statement for 2011, discontinued operations loss is

- a. \$8,400.
- b. \$12,000.
- c. \$14,700.
- d. \$21,000.

133. Chase Corp. had the following infrequent transactions during 2010:

- A \$150,000 gain from selling its automotive division.
- A \$210,000 gain on the sale of investments.
- A \$70,000 loss on the write-down of inventories.

In its 2010 income statement, what amount should Chase report as other income and expense?

- a. \$80,000
- b. \$140,000
- c. \$290,000
- d. \$360,000

134. James, Inc. incurred the following infrequent losses during 2010:

- A \$70,000 impairment loss on intangible assets.
- A \$40,000 litigation settlement.
- A \$60,000 write-off of obsolete inventory.

In its 2010 income statement, what amount should James report as other income and expense?

- a. \$170,000
- b. \$130,000
- c. \$110,000
- d. \$100,000

135. Which of the following should be reported as a prior period adjustment?

	<u>Change in Estimated Lives of Depreciable Assets</u>	<u>Change from Unaccepted Principle to Accepted Principle</u>
a.	Yes	Yes
b.	No	Yes
c.	Yes	No
d.	No	No

Ex. 4-137—Terminology.

In the space provided, write the word or phrase that is defined or indicated.

1. Net income minus preference dividends
divided by the weighted average of ordinary
shares outstanding.

1. _____

- | | |
|---|----------|
| 2. All changes in equity during a period except those resulting from investments by owners and distributions to owners. | 2. _____ |
| 3. A correction of an error is reported as a | 3. _____ |
| 4. A change from one generally accepted principle to another. | 4. _____ |
| 5. The income statement category for a disposal of a component of a business. | 5. _____ |
| 6. Relating tax expense to specific items on the income statement. | 6. _____ |

Solution 4-137

- Earnings per share.
- Comprehensive income.
- Prior period adjustment.
- Changes in accounting principle.
- Discontinued operations.
- Intraperiod tax allocation.

Ex. 4-138—Calculation of net income from the change in equity.

Presented below is certain information pertaining to Edson Company.

Assets, January 1	\$240,000
Assets, December 31	230,000
Liabilities, January 1	150,000
Share capital, December 31	80,000
Retained earnings, December 31	31,000
Ordinary shares sold during the year	10,000
Dividends declared during the year	13,000

Compute the net income for the year.

Solution 4-138

	January 1	December 31
Assets	\$240,000	
Liabilities	<u>150,000</u>	
Equity	<u>\$ 90,000</u>	<u>\$111,000*</u>
Computation of net income:		
Equity December 31	\$111,000	
Equity January 1	<u>90,000</u>	
Increase	21,000	
Add: Dividend declared	13,000	
Less: Ordinary shares sold	<u>(10,000)</u>	
Net income	<u>\$ 24,000</u>	

*\$80,000 + \$31,000

Ex. 4-139—Calculation of net income from the change in equity.

Presented below are changes (in thousands) in the account balances of Wenn Company during the year, except for retained earnings.

	Increase (Decrease)		Increase (Decrease)
Cash	¥29,000	Accounts payable	¥34,000
Accounts receivable (net)	(13,000)	Bonds payable	(20,000)
Inventory	52,000	Share capital	72,000
Plant Assets (net)	37,000	Share premium	16,000

The only entries in Retained Earnings were for net income and a dividend declaration of \$12,000.

Compute the net income for the current year.

Solution 4-139

Computation of net income		
Change in assets (¥118,000 – ¥13,000)	¥105,000	Increase
Change in liabilities (¥34,000 – ¥20,000)	<u>14,000</u>	Increase
Change in equity	91,000	Increase
Add: Dividend declared	12,000	
Less: Investment by shareholders	<u>(88,000)</u>	
Net income	<u>¥ 15,000</u>	

Ex. 4-140—Income measures.

Presented below is information related to Watt Company in its first year of operation. The following information is provided at December 31, 2011, the end of its first year.

Sales revenue	€450,000
Cost of good sold	210,000
Selling and administrative expenses	75,000
Gain on sale of plant assets	45,000
Unrealized gain on available-for-sale financial assets	15,000
Financial costs	10,000
Loss on discontinued operations	20,000
Allocation to non-controlling interest	60,000
Dividends declared and paid	8,000

Compute the following (a) income from operations, (b) net income, (c) net income attributable to Watt Company shareholders, (d) comprehensive income, and (e) retained earnings balance at December 31, 2011.

Solution 4-140

Sales revenue.....	€450,000
Cost of goods sold.....	<u>210,000</u>
Gross profit.....	240,000
Selling and administrative expenses.....	<u>75,000</u>
Other income and expenses	
Gain on sale of plant assets.....	<u>45,000</u>
Income from operations.....	210,000(a)
Financing costs.....	<u>10,000</u>
Income from continued operations.....	200,000
Loss on discontinued operations.....	<u>20,000</u>
Net income.....	180,000(b)
Allocation to non-controlling interest.....	<u>60,000</u>
Net income attributable to shareholders.....	€120,000(c)
Net income.....	€180,000
Unrealized gain on available for sale financial assets.....	<u>15,000</u>
Comprehensive income.....	€195,000(d)
Net income.....	€180,000
Dividends declared and paid.....	<u>8,000</u>
Retained earning December 31, 2011.....	<u>€172,000(e)</u>

Ex. 4-141—Income Computations.

Presented below is financial information related to Finney Company

Revenue	€950,000
Income from continuing operations	120,000
Comprehensive income	140,000
Net income	105,000
Income from operations	260,000
Selling and administrative expenses	600,000
Income before income tax	240,000

Compute the following (a) other income and expense, (b) financing costs, (c) income tax, (d) discontinued operations, and (e) other comprehensive income.

Solution 4-141

- a. Other income and expense = €950,000 – €600,000 – €260,000 = €90,000.
- b. Financing costs = €260,000 – €240,000 = €20,000.
- c. Income tax = €240,000 – €105,000 = €135,000.
- d. Discontinued operations = €120,000 – €105,000 = (€15,000).
- e. Other Comprehensive income = €140,000 – €105,000 = €35,000.

Ex. 4-142—Income statement classifications.

Indicate the major section or subsection of an income statement in which each of the following items would usually appear:

- a. Advertising
- b. Depletion
- c. Dividend revenue
- d. Freight-in
- e. Loss on disposal of a component of the business, net of tax
- f. Income taxes on income
- g. Interest income
- h. Purchase discounts
- i. Sales discounts
- j. Officers' salaries
- k. Freight-out

Solution 4-142

- a. Selling expense.
- b. Cost of goods sold.
- c. Other income and expense.
- d. Cost of goods sold as an addition to purchases.
- e. Discontinued operations.
- f. Income taxes; subtracted from income before income taxes in arriving at net income.
- g. Other income and expense.
- h. Cost of goods sold as a subtraction from purchases.
- i. Subtracted from gross revenues.
- j. Administrative or general expenses.
- k. Selling expense.

Ex. 4-143—Income statement relationships.

Fill in the appropriate blanks for each of the independent situations below.

	Company A	Company B	Company C
Sales	(a) ¥	¥343,400	¥540,000
Beginning inventory	52,600	(d)	90,000
Net purchases	175,300	255,600	(g)
Ending inventory	52,200	108,000	63,000
Cost of goods sold	(b)	(e)	407,000
Gross profit	85,300	98,000	(h)
Operating expenses	(c)	50,000	48,000
Income before taxes	6,000	(f)	(i)

Solution 4-143

- (a) ¥261,000

(b) ¥175,700

(c) ¥79,300
- (d) ¥97,800

(e) ¥245,400

(f) ¥48,000
- (g) ¥380,000

(h) ¥133,000

(i) ¥85,000

Ex. 4-144— Income statement.

Listed below in scrambled order are 11 income statement categories. Use the numerals 1 through 11 to indicate the order in which these categories should appear on an income statement.

- ()

Discontinued operations.
- ()

Cost of goods sold.
- ()

Other income and expense.
- ()

Net income.
- ()

Income taxes.
- ()

Sales.
- ()

Gross profit.
- ()

Income from operations.
- ()

Income before income taxes.
- ()

Selling and administrative expenses.
- ()

Income from continuing operations.

Solution 4-144

10, 2, 5, 11, 8, 1, 3, 6, 7, 4, 9

Ex. 4-145—Classification of income statement and retained earnings statement items.

For each of the items listed below, indicate how it should be treated in the financial statements. Use the following letter code for your selections:

- a.

Other income and expense item on the income statement
- b.

Discontinued operations
- c.

Prior period adjustment

- _____

1.

The company incurred a loss from impairment of plant assets.
- _____

2.

Obsolete inventory was written off. This was the first loss of this type in the company's history.
- _____

3.

Loss on the disposal of a component of the business.
- _____

4.

Recognition of income earned last year which was inadvertently omitted from last year's income statement.
- _____

5.

The company sold one of its warehouses at a loss.
- _____

6.

Settlement of litigation with federal government related to income taxes of three years ago. The company is continually involved in various adjustments with the federal government related to its taxes.
- _____

7.

Loss on sale of investments. The company last sold some of its investments two years ago.
- _____

8.

The company neglected to record its depreciation in the previous year.
- _____

9.

Discontinuance of all production in the United States. The manufacturing operations were relocated in Mexico.

Solution 4-145

1.

a
2.

a
3.

b
4.

c
5.

a
6.

a
7.

a
8.

c
9.

a

Pr. 4-146—Income statement.

Presented below is information (in thousands) related to Chen Company.

Retained earnings, December 31, 2010	¥ 650,000
Sales	1,400,000
Selling and administrative expenses	240,000
Loss on disposal of component (pre-tax)	290,000
Cash dividends declared on common stock	33,600
Cost of goods sold	780,000
Gain resulting from computation error on depreciation charge in 2009 (pre-tax)	520,000
Rent revenue	120,000
Impairment loss	90,000
Interest expense	10,000

Instructions

Prepare in good form an income statement for the year 2011. Assume a 30% tax rate and that there were 80,000 ordinary shares outstanding during the year.

Solution 4-146

Chen Company
INCOME STATEMENT
For the Year Ended December 31, 2011

Sales	¥1,400,000
Cost of goods sold	<u>780,000</u>
Gross profit	620,000
Selling and administrative expenses	240,000
Other income and expense	120,000
Impairment loss	<u>90,000</u>
Income from operations	410,000
Interest expense	<u>10,000</u>
Income before taxes	400,000
Income taxes	<u>(120,000)</u>
Income from continuing operations	280,000
Discontinued operations, net of applicable income taxes of ¥87,000	<u>(203,000)</u>
Net income	<u>¥ 77,000</u>

Per share—

Income from continuing operating	¥ 3.50
Discontinued operations net of tax	<u>(2.54)</u>
Net income	<u>¥ 0.96</u>

Pr. 4-147—Income statement form.

Wilcox Corporation had income from continuing operations of \$800,000 (after taxes) in 2011. In addition, the following information has not been considered.

1. A machine was sold for \$140,000 cash during the year at a time when its book value was \$110,000. (Depreciation has been properly recorded.) The company often sells machinery of this type.
2. Wilcox decided to discontinue its stereo division in 2011. During the current year, the loss on the disposal of this component of the business was \$150,000 less applicable taxes.

Instructions

Present in good form the income statement of Wilcox Corporation for 2011 starting with "income from continuing operations." Assume that Wilcox's tax rate is 30% and 200,000 ordinary shares were outstanding during the year.

Solution 4-147

Wilcox Corporation
Partial Income Statement
For the Year Ended December 31, 2011

Income from continuing operations	\$821,000*
Discontinued operations	
Loss on disposal of a component of a business, \$150,000, less applicable income taxes, \$45,000	<u>(105,000)</u>
Net income	<u>\$716,000</u>
Per share—Income from cont. operations	\$4.11
Discontinued operations, net of tax	<u>(0.53)</u>
Net income	<u>\$3.58</u>
*Income from cont. operations (unadjusted)	\$800,000
Gain on sale of machinery (after tax)	<u>21,000</u>
Income from cont. operations (adjusted)	<u>\$821,000</u>

Pr. 4-148—Income statement.

Shown below is an income statement for 2011 that was prepared by a poorly trained bookkeeper of Howell Corporation.

Howell Corporation	
INCOME STATEMENT	
December 31, 2011	
Sales revenue	\$945,000
Investment revenue	19,500
Cost of merchandise sold	(408,500)
Selling expenses	(145,000)
Administrative expense	(215,000)
Interest expense	<u>(13,000)</u>
Income before special item	183,000
Special item	
Loss on disposal of a component of the business	(30,000)
Net income tax liability	<u>(45,900)</u>
Net income	<u>\$107,100</u>

Instructions

Prepare a multiple-step income statement for 2011 for Howell Corporation that is presented in accordance with IFRS (including format and terminology). Howell Corporation has 50,000 ordinary shares outstanding and has a 30% income tax rate on all tax related items. Round all earnings per share figures to the nearest cent.

Solution 4-148

Howell Corporation	
INCOME STATEMENT	
For the Year Ended December 31, 2011	
Sales	\$945,000
Cost of goods sold	<u>408,500</u>
Gross profit	536,500
Selling expenses	\$145,000
Administrative expenses	<u>215,000</u>
Other income: Investment revenue	19,500
Income from operations	196,000
Interest expense	<u>13,000</u>
Income before income taxes	183,000
Income taxes	<u>54,900</u>
Income from continuing operations	128,100
Loss from discontinued operations, net of applicable income tax of \$9,000	<u>21,000</u>
Net income	<u>\$107,100</u>
Per share of share—	
Income from continuing operations	\$2.56
Discontinued operations loss net of tax	<u>(0.42)</u>
Net income	<u>\$2.14</u>

Pr. 4-149—Income statement.

Presented below is an income statement for Kinder Company for the year ended December 31, 2011.

Kinder Company	
Income Statement	
For the Year Ended December 31, 2011	
Net sales	\$800,000
Costs and expenses:	
Cost of goods sold	640,000
Selling, general, and administrative expenses	70,000
Other, net	<u>20,000</u>
Income before income taxes	70,000
Income taxes	<u>21,000</u>
Net income	<u>\$ 49,000</u>

Additional information:

- "Selling, general, and administrative expenses" included a charge of \$7,000 for impairment of intangibles.
- "Other, net" consisted of interest expense, \$10,000, and a discontinued operations loss of \$10,000 before taxes. If the loss had not occurred, income taxes for 2011 would have been \$24,000 instead of \$21,000.
- Kinder had 20,000 ordinary shares outstanding during 2011.

Instructions

Prepare a corrected income statement, including the appropriate per share disclosures.

Solution 4-149

Kinder Company
Income Statement
For the Year Ended December 31, 2011

Net sales		\$800,000
Cost of goods sold		<u>640,000</u>
Gross profit		\$160,000
Selling, general, and administrative expenses		63,000
Other income and expense		
Loss on impairment		<u>7,000</u>
Income from operations		90,000
Interest expense		<u>10,000</u>
Income before taxes		80,000
Income taxes		<u>24,000</u>
Income from continuing operations		56,000
Discontinued operations		
Loss on disposal of component	10,000	
Less applicable taxes	<u>3,000</u>	<u>7,000</u>
Net income		<u>\$ 49,000</u>
Per share—		
Income from continuing operations	\$2.80	
Discontinued operations, net of tax	<u>(0.35)</u>	
Net income	<u>\$2.45</u>	

Pr. 4-150—Income statement and retained earnings statement.

Wang Corporation's capital structure consists of 50,000 ordinary shares. At December 31, 2011 an analysis of the accounts and discussions with company officials revealed the following information:

Sales	¥1,100,000
Purchase discounts	18,000
Purchases	642,000
Loss on discontinued operations (net of tax)	42,000
Selling expenses	128,000
Cash	60,000
Accounts receivable	90,000
Share capital	200,000
Accumulated depreciation	180,000
Dividend revenue	8,000
Inventory, January 1, 2011	152,000
Inventory, December 31, 2011	125,000
Unearned service revenue	4,400
Accrued interest payable	1,000
Land	370,000
Patents	100,000
Retained earnings, January 1, 2011	290,000
Interest expense	17,000
General and administrative expenses	150,000
Dividends declared	29,000
Allowance for doubtful accounts	5,000
Notes payable (maturity 7/1/14)	200,000
Machinery and equipment	450,000
Materials and supplies	40,000
Accounts payable	60,000

The amount of income taxes applicable to ordinary income was ¥48,600, excluding the tax effect of the discontinued operations loss which amounted to ¥18,000.

Instructions

- (a) Prepare an income statement.
- (b) Prepare a retained earnings statement.

Solution 4-150

Wang Corporation
INCOME STATEMENT
For the Year Ended December 31, 2011

Sales		¥1,100,000
Cost of goods sold:		
Merchandise inventory, Jan. 1	¥152,000	
Purchases	¥642,000	
Less purchase discounts	<u>18,000</u>	
Net purchases		<u>624,000</u>
Merchandise available for sale		776,000
Less merchandise inv., Dec. 31		<u>125,000</u>
Cost of goods sold		<u>651,000</u>
Gross profit		449,000
Selling expenses	128,000	
General and administrative expenses	<u>150,000</u>	278,000

Other income and expense:	
Dividend revenue	8,000
Income from operations	179,000
Interest expense	17,000
Income before income taxes	162,000
Income taxes	48,600
Income from continuing operations	113,400
Discontinued operations	
Loss on disposal, less applicable taxes of \$18,000	42,000
Net income	¥ 71,400
Per share of share capital—	
Income from continuing operations	¥2.27
Discontinued operations,	(0.84)
Net income	¥1.43

Wang Corporation
 RETAINED EARNINGS STATEMENT
 For the Year Ended December 31, 2011

Retained earnings, January 1, 2011		¥290,000
Add: Net income	¥71,400	
Deduct: Dividends declared	29,000	42,400
Retained earnings, December 31, 2011		¥332,400

Pr. 4-151—Irregular items and financial statements.

The accountant preparing the income statement for Bakersfield, Inc. had some doubts about the appropriate accounting treatment of the six items listed below during the fiscal year ending December 31, 2011. Assume a tax rate of 40 percent.

- The corporation disposed of its sporting goods division during 2011. This disposal meets the criteria for discontinued operations. The division correctly calculated income from operating this division of \$100,000 before taxes and a loss of \$12,000 before taxes on the disposal of the division. All of these events occurred in 2011 and have not been recorded.
- The company recorded advances of \$10,000 to employees made December 31, 2011 as Salary Expense.
- Dividends of \$10,000 during 2011 were recorded as an operating expense.
- In 2011, Bakersfield changed its method of accounting for inventory from the first-in-first-out method to the average cost method. Inventory in 2011 was correctly recorded using the average cost method. The new inventory method would have resulted in an additional \$125,000 of cost of goods sold (before taxes) being reported on prior years' income statement.
- Office equipment purchased January 1, 2011 for \$45,000 was incorrectly charged to Office Supplies Expense at the time of purchase. The office equipment has an estimated three-year service life with no expected salvage value. Bakersfield uses the straight-line method to depreciate office equipment for financial reporting purposes. This error has not been corrected.
- On January 1, 2007, Bakersfield bought a building that cost \$85,000, had an estimated useful life of ten years, and had a salvage value of \$5,000. Bakersfield uses the straight-line depreciation method to depreciate the building. In 2011, it was estimated that the remaining useful life was eight years and the salvage value was zero. Depreciation expense reported on the 2011 income statement was correctly calculated based on the new estimates. No adjustment for prior years' depreciation estimates was made.

Part A. For each item, record corrections to income from continuing operations before taxes, if any. Denote any negative numbers by using brackets < >.

Solution 4-151

Number Item	Description	Increase <Decrease> to Income from Continuing Operations
1.	Discontinued Items reported after ICO	No Effect
2.	Correct with Dr: Prepaid Salary Cr: Salary Expense	\$10,000
3.	Dividends are not reported on the Income Statement; should be on Statement of R/E.	\$10,000
4.	Change in inventory method: Current year reported correctly on income statement, need to adjust beginning R/E.	No Effect
5.	To correct, need to put back all \$45,000 of equipment into Equipment account and take out of Supplies Expense account. Also take depreciation of \$15,000 for the year. Net effect is to increase income by \$30,000.	\$30,000
6.	Current year is correct. Change in estimate does not need retroactive action.	No Effect

True False Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
1.	T	6.	T	11.	T	16.	F
2.	F	7.	T	12.	T	17.	T
3.	F	8.	F	13.	F	18.	F
4.	T	9.	F	14.	F	19.	F
5.	F	10.	T	15.	T	20.	T

Multiple Choice Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
21.	c	29.	b	37.	B	45.	b	53.	c	61.	a	69.	d
22.	d	30.	a	38.	A	46.	c	54.	c	62.	c	70.	b
23.	b	31.	d	39.	B	47.	c	55.	c	63.	b	71.	a
24.	d	32.	a	40.	D	48.	b	56.	c	64.	c	72.	c
25.	d	33.	b	41.	A	49.	b	57.	d	65.	d	73.	c
26.	c	34.	d	42.	B	50.	d	58.	d	66.	b	74.	b
27.	b	35.	b	43.	C	51.	c	59.	c	67.	d		
28.	c	36.	c	44.	B	52.	d	60.	c	68.	c		

Multiple Choice Answers—Computational

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
75.	a	84.	b	93.	c	102.	b	111.	c	120.	d
76.	c	85.	d	94.	b	103.	c	112.	d	121.	d
77.	c	86.	d	95.	d	104.	c	113.	d	122.	a
78.	c	87.	a	96.	d	105.	c	114.	d	123.	c
79.	c	88.	d	97.	c	106.	b	115.	d	124.	c
80.	b	89.	a	98.	c	107.	a	116.	a	125.	a
81.	a	90.	a	99.	b	108.	a	117.	b		
82.	c	91.	a	100.	d	109.	a	118.	b		
83.	d	92.	b	101.	a	110.	b	119.	a		

Multiple Choice Answers—CPA Adapted

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
126.	d	128.	a	130.	d	132.	a	134.	a
127.	a	129.	a	131.	c	133.	b	135.	b

DERIVATIONS — Computational

No.	Answer	Derivation
75.	a	$\$20,000 + \$4,000 = \$24,000.$
76.	c	$\$34,000 - \$8,000 + \$20,000 - \$11,000 - \$13,000 = \$22,000.$
77.	c	$\$100,000 - \$2,000 - \$60,000 = \$38,000.$
78.	c	$\$150,000 - \$4,000 - \$90,000 = \$56,000.$
79.	c	$\$15,720,000 - \$370,000 - \$175,000 = \$15,175,000.$
80.	b	$¥1,200,000 - ¥750,000 - 330,000 = ¥120,000.$
81.	a	$¥330,000 - ¥300,000 = ¥30,000.$
82.	c	$¥300,000 - ¥150,000 = ¥150,000.$
83.	d	$¥150,000 - ¥135,000 = ¥(15,000)$
84.	b	$¥150,000 - ¥82,000 - ¥15,000 + ¥45,000 = ¥98,000.$
85.	d	$¥150,000 - ¥82,000 - ¥15,000 + ¥45,000 - ¥8,000 = ¥90,000.$
86.	d	$¥150,000 - ¥82,000 - ¥15,000 + ¥45,000 - ¥8,000 = ¥90,000;$ $¥90,000 \times 0.30 = ¥27,000.$
87.	a	$¥150,000 - ¥82,000 - ¥15,000 + ¥45,000 - ¥8,000 = ¥90,000;$ $¥90,000 - ¥27,000 = ¥63,000$
88.	d	$\$1,600,000 - [(\$45,000 - \$27,000) - ((\$45,000 - \$27,000) \times 0.30)]$ $= \$1,587,400.$
89.	a	
90.	a	
91.	a	$\$25,000 - \$7,500 = \$17,500.$
92.	b	$\$17,500 + (\$500,000 \times 0.70) = \$367,500.$
93.	c	$\$1,400,000 - \$1,200,000 = \$200,000.$
94.	b	$(\$1,000,000 - \$250,000) \div 200,000 \text{ sh.} = \$3.75.$
95.	d	$\$1,000,000 \div 200,000 \text{ sh.} = \$5.00.$
96.	d	$\$350,000 \div 70,000 \text{ sh.} = \$5.00.$
97.	c	$(\$500,000 - \$60,000) \div 100,000 = \$4.40.$
98.	c	$(\$500,000 - \$60,000) \div 200,000 = \$2.20.$
99.	b	$(£2,000,000 - £200,000) \div 150,000 = £12.00.$

100.	d	$(\$600,000 - X) \div 120,000 = \$4.25.$ $\$600,000 - X = \$510,000 = \$90,000.$
101.	a	$(\pounds 7,800,000 - \pounds 20,000 - \pounds 15,000) \times 0.20 = \pounds 1,553,000.$
102.	b	$\pounds 60,000 - (\pounds 60,000 \times 0.20) = \pounds 48,000.$
103.	c	$[(\pounds 7,800,000 - \pounds 20,000 - \pounds 15,000) \times 0.20] + (\pounds 60,000 \times 0.20) = \pounds 1,565,000.$

No.	Answer Derivation	
104.	c	$\$50,000 \times 0.60 = \$30,000.$
105.	c	$\$200,000 \times 0.60 = \$120,000.$
106.	b	$(\$232,000 - \$37,000 + \$8,000) \times 0.40 = \$81,200.$
107.	a	$(\$357,000 + \$23,000 + \$6,000) \times 0.30 = \$115,800.$
108.	a	$(\$100,000 - \$60,000 - \$8,000 - \$11,000 + \$9,000 - \$1,000 - \$2,000) \times 0.40 = \$10,800.$
109.	a	$\$2,000,000 - \$430,000 = \$1,570,000.$
110.	b	$\$2,000,000 - \$430,000 + \$1,000,000 - \$320,000 = \$2,250,000.$
111.	c	$\$1,000,000 + \$215,000 = \$1,215,000.$
112.	d	$\$1,000,000 + \$215,000 + \$500,000 - \$160,000 = \$1,555,000.$
113.	d	$\$1,700,000 - \$800,000 - \$200,000 + \$75,000 = \$775,000.$
114.	d	$\$700,000 - \$300,000 - \$80,000 = \$320,000.$
115.	d	$\$700,000 - \$300,000 - \$80,000 - (\$50,000 \times 0.80) = \$280,000.$
116.	a	$\$750,000 + \$150,000 - \$50,000 - (\$40,000 \times 0.70) = \$878,000.$
117.	b	$\pounds 400,000 - (\pounds 400,000 \times 0.20) = \pounds 320,000.$
118.	b	$(\pounds 400,000 - \pounds 300,000) = \pounds 100,000 \times 0.80 = \pounds 80,000.$
119.	a	$\pounds 300,000 - (\pounds 300,000 \times 0.20) = \pounds 240,000$
120.	d	$\pounds 300,000 - (\pounds 300,000 \times 0.20) = \pounds 240,000$
121.	d	Other comprehensive income = \$40,000.
122.	a	$\$500,000 - \$350,000 - \$55,000 + \$20,000 + \$2,000 = \$117,000.$
123.	c	$\$5,000 - \$1,000 = \$4,000.$
124.	c	$\$80,000 + \$60,000 - \$10,000 - \$2,000 = \$128,000.$
125.	a	$(\$80,000 + \$60,000 - \$10,000 - \$2,000) + \$40,000 + (\$5,000 - \$1,000) = \$172,000.$

DERIVATIONS — CPA Adapted

No.	Answer Derivation	
126.	d	$\$120,000 + \$75,000 + \$110,000 + \$90,000 = \$395,000.$
127.	a	$\$140,000 + \$180,000 + \$90,000 = \$410,000.$
128.	a	$\$180,000 + \$80,000 + \$110,000 + \$170,000 = \$540,000.$
129.	a	$\$130,000 + \$90,000 = \$220,000.$
130.	d	$\$50,000 + \$70,000 - \$80,000 = \$40,000.$
131.	c	$\$140,000 - \$50,000 - \$25,000 - \$9,000 - \$8,000 + \$5,000 - \$3,000 - \$3,000 = \$47,000.$
132.	a	$\$12,000 \times 0.70 = \$8,400.$
133.	b	$\$210,000 - \$70,000 = \$140,000.$
134.	a	$\$70,000 + \$40,000 + \$60,000 = \$170,000.$
135.	b	Conceptual.