

# 13

## Financial Statements, Closing Entries, and Reversing Entries

### DEMONSTRATION PROBLEM

Christy's Apparel has a fiscal year extending from January 1 through December 31. Its account balances after adjustments are presented below in random order. The beginning merchandise inventory amounts to \$35,870. With regard to the outstanding mortgage, \$2,000 is due within the next twelve months.

Notes Receivable	\$ 7,000	Freight In	\$ 7,040
Interest Income	5,362	Office Salary Expense	11,119
Building	45,400	Accounts Receivable	46,627
Accounts Payable	25,245	Store Supplies	1,094
Prepaid Insurance	1,090	Interest Expense	2,100
Insurance Expense	2,505	Cash	3,305
Accumulated Depreciation, Building	15,133	Depreciation Expense, Building	1,297
Notes Payable	10,250	Purchases Discounts	1,335
Sales	267,111	Accumulated Depreciation, Store Equipment	10,750
Sales Salary Expense	60,377	Salaries Payable	3,420
Rent Income	2,400	C.P. Bennett, Drawing	60,000
Store Equipment	21,500	Office Equipment	8,875
Mortgage Payable (current portion is \$2,000)	31,000	Taxes Expense	4,006
Land	10,000	Accumulated Depreciation, Office Equipment	4,438
Sales Commission Expense	6,400	Miscellaneous General Expense	1,750
Sales Discounts	2,671	Store Supplies Expense	1,918
Merchandise Inventory, Dec. 31, 20—	41,998	C.P. Bennett, Capital, Jan. 1, 20—	110,980
Purchases	133,556	Depreciation Expense, Office Equipment	1,775
Advertising Expense	5,342	Depreciation Expense, Store Equipment	4,300
Sales Returns and Allowances	3,149		
Purchases Returns and Allowances	2,642		

### Instructions

1. Prepare a classified income statement and subdivide operating expenses.
2. Prepare a statement of owner's equity.
3. Prepare balance sheet.
4. Determine the amount of working capital and the current ratio.

## SOLUTION

1.

### Christy's Apparel

#### Income Statement

For Year Ended December 31, 20—

<i>Revenue from Sales:</i>			
<i>Sales</i>		\$267,111.00	
<i>Less: Sales Returns and Allowances</i>	\$ 3,149.00		
<i>Sales Discounts</i>	2,671.00	5,820.00	
<i>Net Sales</i>			\$261,291.00
<i>Cost of Goods Sold:</i>			
<i>Merchandise Inventory, January 1, 20—</i>		\$ 35,870.00	
<i>Purchases</i>	\$133,556.00		
<i>Less: Purchases Returns and Allowances</i>	\$2,642.00		
<i>Purchases Discounts</i>	1,335.00	3,977.00	
<i>Net Purchases</i>	\$129,579.00		
<i>Add Freight In</i>	7,040.00		
<i>Delivered Cost of Purchases</i>		136,619.00	
<i>Cost of Goods Available for Sale</i>		\$172,489.00	
<i>Less Merchandise Inventory, December 31, 20—</i>		41,998.00	
<i>Cost of Goods Sold</i>			130,491.00
<i>Gross Profit</i>			\$130,800.00
<i>Operating Expenses:</i>			
<i>Selling Expenses:</i>			
<i>Sales Salary Expense</i>	\$ 60,377.00		
<i>Sales Commission Expense</i>	6,400.00		
<i>Advertising Expense</i>	5,342.00		
<i>Store Supplies Expense</i>	1,918.00		
<i>Depreciation Expense, Store Equipment</i>	4,300.00		
<i>Total Selling Expenses</i>		\$ 78,337.00	
<i>General Expenses:</i>			
<i>Insurance Expense</i>	\$ 2,505.00		
<i>Office Salary Expense</i>	11,119.00		
<i>Depreciation Expense, Building</i>	1,297.00		
<i>Taxes Expense</i>	4,006.00		
<i>Miscellaneous General Expense</i>	1,750.00		
<i>Depreciation Expense, Office Equipment</i>	1,775.00		
<i>Total General Expenses</i>		22,452.00	
<i>Total Operating Expenses</i>			100,789.00
<i>Income from Operations</i>			\$ 30,011.00
<i>Other Income:</i>			
<i>Interest Income</i>		5,362.00	
<i>Rent Income</i>		\$ 2,400.00	
<i>Total Other Income</i>		\$ 7,762.00	
<i>Other Expenses:</i>			
<i>Interest Expense</i>		2,100.00	5,662.00
<i>Net Income</i>			\$ 35,673.00

**SOLUTION** (continued)

2.

*Christy's Apparel*

*Statement of Owner's Equity*

*For Year Ended December 31, 20 —*

<i>C. P. Bennett, Capital, January 1, 20 —</i>			<i>\$110,980.00</i>
<i>Net Income for the Year</i>		<i>\$ 35,673.00</i>	
<i>Less Withdrawals for the Year</i>		<i>60,000.00</i>	
<i>Decrease in Capital</i>			<i>24,327.00</i>
<i>C. P. Bennett, Capital, December 31, 20 —</i>			<i>\$ 86,653.00</i>

3.

*Christy's Apparel**Balance Sheet**December 31, 20 —*

<i>Assets</i>			
<i>Current Assets:</i>			
<i>Cash</i>		<i>\$ 3,305.00</i>	
<i>Notes Receivable</i>		<i>7,000.00</i>	
<i>Accounts Receivable</i>		<i>46,627.00</i>	
<i>Merchandise Inventory</i>		<i>41,998.00</i>	
<i>Store Supplies</i>		<i>1,094.00</i>	
<i>Prepaid Insurance</i>		<i>1,090.00</i>	
<i>Total Current Assets</i>			<i>\$101,114.00</i>
<i>Plant and Equipment:</i>			
<i>Land</i>		<i>\$10,000.00</i>	
<i>Building</i>	<i>\$45,400.00</i>		
<i>Less Accumulated Depreciation</i>	<i>15,133.00</i>	<i>30,267.00</i>	
<i>Office Equipment</i>	<i>\$ 8,875.00</i>		
<i>Less Accumulated Depreciation</i>	<i>4,438.00</i>	<i>4,437.00</i>	
<i>Store Equipment</i>	<i>\$21,500.00</i>		
<i>Less Accumulated Depreciation</i>	<i>10,750.00</i>	<i>10,750.00</i>	
<i>Total Plant and Equipment</i>			<i>55,454.00</i>
<i>Total Assets</i>			<i>\$156,568.00</i>
<i>Liabilities</i>			
<i>Current Liabilities:</i>			
<i>Notes Payable</i>		<i>\$10,250.00</i>	
<i>Mortgage Payable (current portion)</i>		<i>2,000.00</i>	
<i>Accounts Payable</i>		<i>25,245.00</i>	
<i>Salaries Payable</i>		<i>3,420.00</i>	
<i>Total Current Liabilities</i>			<i>\$ 40,915.00</i>
<i>Long-Term Liabilities:</i>			
<i>Mortgage Payable</i>			<i>29,000.00</i>
<i>Total Liabilities</i>			<i>\$ 69,915.00</i>
<i>Owner's Equity</i>			
<i>C. P. Bennett, Capital</i>			<i>86,653.00</i>
<i>Total Liabilities and Owner's Equity</i>			<i>\$156,568.00</i>

4. Working capital = Current assets – Current liabilities  
= \$101,114 – \$40,915 = \$60,199

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}} = \frac{\$101,114}{\$40,915} = \underline{\underline{2.47}}$$