**ACC-405**

**Module Seven Project Practice Problems and Solutions**

**Problem 1.** Circus City issued an 8%, 10‐year $2,000,000 bond to build a monorail mass transit system. The city received $1,754,217 cash from the bond issuance on January 1, 2020. The bond yield is 10%. Interest is paid annually on December 31 of each year. Disclosure information about capital assets is reported below.



Depreciation expense charged to governmental activities as follows:

Public Safety $ 55,000

General Government 72,000

Highways and Streets 25,000

Sanitation    17,000

$169,000

Circus City's governmental funds financial statements are as follows:





**Required:**

Using the information above, prepare the statement of activities and the statement of net position on a government‐wide basis (using full accrual accounting). The beginning fund balance in the government‐wide Statement of Net Position is $2,686,283.

|  |  |
| --- | --- |
| **Answer**  Circus City |  |
| Statement of Activites -Government-Wide |  |
| For the Year Ended December 31, 2020 |  |
|  |  |  |  |  |  |  | Net (Expense) Revenue  |  |
|  |  |  |  |  |  |  | and Changes in Net Position |   |
|  |  |  | Program Revenues |  | Primary Government |   |
|  |  |  | Charges for |  | Grants and |  | Governmental |  |
| Functions/Programs | Expenses (a) |  | Services |  | Contributions |  | Activities |  |
| **Primary Government** |  |  |  |  |  |  |  |  |
| *Governmental Activities* |  |  |  |  |  |  |  |  |
| Public Safety |  $ 555,000  |  |  |  |  |  |  $ (555,000) |  |
| General Government |  372,000  |  |  $180,000  |  (b)  |  $1,000,000  |  |  808,000  |  |
| Highways and Streets |  155,000  |  |  100,000  |  (b)  |  250,000  |  |  195,000  |  |
| Sanitation |  87,000  |  |  |  |  |  |  (87,000) |  |
| Interest on long-term debt |  175,422  | (c) |  \_\_\_\_\_\_\_  |  |  \_\_\_\_\_\_\_  |  |  (175,422)  |  |
|  Total governmental activities |  1,344,422  |  |  280,000  |  |  1,250,000  |  |  185,578  |  |
|  |  |  |  |  |  |  |  |  |
|  **Total primary government** |  $ 1,344,422  |  |  $ 280,000  |  |  $ 1,250,000  |  |  $ 185,578  |  |
|  |  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |  |
|  | **General Revenues** |  |  |  |  |  |  |
|  | Property taxes |  |  |  |  |  |  $ 575,000  |  |
|  | Investment earnings |  |  |  |  |  75,000  |  |
|  | Special item - gain on sale of equipment |  |  |  30,000  |  |
|  |  Total general revenues, special items, |  |  |  |  |
|  |  and transfers |  |  |  |  |  |  $ 680,000  |  |
|  |  |  |  |  |  |  |  |  |
|  | Change in net position |  |  |  |  |  865,578  |  |
|  | Net position – beginning |  |  |  |  2,686,283  |  |
|  | Net position - ending  |  |  |  |  | $ 3,551,861 |  |
|  |  |  |  |  |  |  |  |  |
| (a) Depreciation expense has been added to each governmental activity. |  |  |  |  |
| (b) Licenses and permits are charged $100,000 to highways and streets and $50,000 to general government. |  |
| (c) The debt amortization schedule is as follows (next page): |  |

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  |  |  |  |  |  |  |  |
|  | Interest expense |  | Cash paid |  | Discount |  | Carrying Value |  |
| Beginning balance |  |  |  |  |  |  | $1,754,217 |  |
| 12/31/20 |  175,422  |  |  160,000  |  |  15,422  |  | $1,769,639 |  |
| 12/31/21 |  176,964  |  |  160,000  |  |  16,964  |  | $1,786,603 |  |
| 12/31/22 |  178,660  |  |  160,000  |  |  18,660  |  | $1,805,263 |  |
| 12/31/23 |  180,526  |  |  160,000  |  |  20,526  |  | $1,825,790 |  |
| 12/31/24 |  182,579  |  |  160,000  |  |  22,579  |  | $1,848,369 |  |
| 12/31/25 |  184,837  |  |  160,000  |  |  24,837  |  | $1,873,205 |  |
| 12/31/26 |  187,321  |  |  160,000  |  |  27,321  |  | $1,900,526 |  |
| 12/31/27 |  190,053  |  |  160,000  |  |  30,053  |  | $1,930,579 |  |
| 12/31/28 |  193,058  |  |  160,000  |  |  33,058  |  | $1,963,637 |  |
| 12/31/29 |  196,363  |  |  160,000  |  |  36,363  |  | $2,000,000 |  |

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  |  |  |  |  |  |  |
|  | Circus City |
|  | Statement of Net Position - Government-Wide Basis |
|  |  At December 31, 2020 |
|  |  |  |  |  |  | Statement  |
|  |  |  |  |  |  | of Net Position |
|  |  |  |  |  |  | Total |
|  |  | Governmental |  |  |  | Government |
|  |  | Funds |  | Adjustments |  | Activities |
|  | Assets |  |  |  |  |  |
|  | Cash | $ 364,000  |  |  |  | $ 364,000  |
|  | Interest Receivable |  16,000  |  |  |  |  16,000  |
|  | Investments |  1,450,500  |  |  |  |  1,450,500  |
|  | Receivables |  183,000  |  |  |  |  183,000  |
|  | Capital Assets (net) |  \_\_\_\_\_\_\_\_\_\_  |  |  3,431,000  |  |  3,431,000  |
|  |  Total Assets |  2,013,500  |  |  |  | $ 5,444,500  |
|  |  |  |  |  |  |  |
|  | Liabilities and Fund Balance |  |  |  |  |  |
|  | Payables | $ 123,000  |  |  |  | $ 123,000  |
|  | Long-term Liabilities |  \_\_\_\_\_\_\_\_\_\_  |  |  1,769,639  |  |  1,769,639  |
|  |  Total Liabilities |  $ 123,000  |  |  |  | $1,892,639  |
|  |  |  |  |  |  |  |
|  | Net Position |  |  |  |  |  |
|  | Invested in Capital Assets, net of related debt |  |  |  |  |  $ 1,661,361  |
|  |  Unrestricted |  $ 1,786,500  |  |  |  |  1,786,500  |
|  |  Restricted for  |  |  |  |  |  |
|  |  Debt Service |  104,000  |  |  |  |  104,000  |
|  |   |  |  |  |  |  |
|  |  Total Fund Balance |  1,890,500  |  |  |  |  3,551,861  |
|  |  Total  | $ 2,013,500  |  |  |  | $ 5,444,500  |

|  |  |  |  |
| --- | --- | --- | --- |
|  | Reconciling the Statement of Net Position with Governmental Fund Reporting |  |  |
|  |  |  |  |  |  |  |
|  | Fund balance for governmental activities |  |  |  |  |  **$ 1,890,500**  |
|  |  |  |  |  |  |  |
|  | Capital assets used in governmental activities are not financial resources |  |  |
|  |  and are not reported in the funds |  |  |  |  |  3,431,000 |
|  |   |  |  |  |  |  |
|  | Long-term liabilities are not due and payable  |  |  |  |  |  |
|  |  in the current period and therefore are not reported in the funds.  |  |  |  (1,769,639) |
|  |  |  |  |  |  |  |
|  | Net Position in governmental activities  |  |  |  |  |  **$ 3,551,861**  |

|  |  |
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|  |  |
| Circus City |
| Reconciliation of the Statement of Revenues, |
| Expenditures, and Changes in Fund Balances of Governmental |
| Funds to the Statement of Activities |
| For the Year Ended December 31, 2020 |
|  |  |  |  |
|  | Net change in fund balances - total governmental funds |  | $ 1,389,217 |
|  |  |  |  |
|  | Governmental funds report capital outlays as expenditures while |  |  |
|  | governmental activities report depreciation expense to allocate those  |  |  |
|  | expenditures over the life of the asset. This is the amount by which |  |  |
|  | capital outlays exceeded depreciation in the current period. |  |  1,331,000  |
|  |  |  |  |
|  | In the statement of activities, only the gain on the sale of equipment |  |  |
|  | is reported, while in the governmental funds, the proceeds from the sale |  |  |
|  | increase financial resources. Thus, the change in net position differs |  |  |
|  | from the change in fund balance by the book value of the asset sold. |  |  (85,000) |
|  |  |  |  |
|  | Bond proceeds provide current financial resources to governmental funds, |  |  |
|  | but issuing debt increases long-term liabilities in the statement of net |  |  |
|  | position.  |  |  (1,754,217) |
|  |  |  |  |
|  | Interest expense recognized on the accrual basis exceeds the amounts |  |  |
|  | paid by the amortization of the bond discount |  |  (15,422) |
|  |  |  |  |
|  | Change in Net Position of Governmental Activities |  | **$ 865,578**  |
|  |  |  |  |

**Problem 2.**

Preston Library, a nonprofit organization, presented the following statement of financial position and statement of activities for its fiscal year ended February 28, 2019.

|  |
| --- |
| **Preston Library** |
| **Statement of Financial Position** |
| **February 28, 2019** |
|  |  |  |
| **Assets** | **Unrestricted** | **Temporarily Restricted** |
| Current Assets |  |  |
|  Cash |  $285,000  |  $80,000  |
|  Grants Receivable |  80,000  |  |
|  Prepaid Expense |  65,000  |  |
|  Total |  430,000  |  |
| Investments (at market) |  1,020,000  |  |
| Land, Building, and Equipment (less Acc Dep of $50,000) |  530,000  |  |
|  Total Assets |  $1,980,000  | 80,000  |
| **Liabilities and Fund Balances** |  |  |
| Current Liabilities |  |  |
|  Accounts Payable and Accrued Expenses |  $150,000  |  |
|  Total |  150,000  |  |
| Long-Term Debt |  200,000  |  |
| Fund Balances |  1,630,000  |  80,000  |
|  Total Liabilities and Fund Balances |  $1,980,000  |  $80,000  |

|  |
| --- |
| **Preston Library** |
| **Statement of Activities** |
| **for Year Ended February 28, 2019** |
| **Support and Revenue** | **Unrestricted** | **Temporarily Restricted** |
| Support and Revenue |  |  |
|  Grants |  $ 70,000  |  $ -  |
|  Gifts |  300,000  |  80,000  |
|  Total |  370,000  |  80,000  |
| Revenue |  |  |
|  Service Fees |  22,000  |  |
|  Book Rentals and Fines |  107,000  |  |
|  Investment Income |  71,000  |  -  |
|  Total |  200,000  |  |
|  Total Support and Revenue |  $ 570,000  |  $ 80,000  |
| **Expenses** |  |  |
| Program Services |  |  |
|  Circulating Library |  $ 212,000  |  |
|  Research Library |  86,000  |  |
|  Exhibits |  20,000  |  |
|  Community Services |  10,000  |  |
|  Total |  328,000  | 0 |
| Supporting Services |  |  |
|  General and Administrative |  175,000  |  |
|  Fund Raising |  111,000  |  |
|  Total |  286,000  | 0 |
|  Total Expenses |  614,000  | 0 |
| Increase (decrease) in Net Assets |  (44,000) |  80,000  |
| Fund Balances - Beginning of Year |  1,674,000  |  -  |
| Fund Balances - End of Year |  $ 1,630,000  |  $ 80,000  |
|  |  |  |

The following transactions occurred during the fiscal year ended February 28, 2020.

1. Fees were billed as follows:

Service fees $30,000

Book rentals  43,000

Book fines  78,000

1. $40,000 of the Grant Receivable was received. Another grant in the amount of $20,000 was promised.
2. Contributions in the amounts summarized below were received:

Unrestricted $215,000

Restricted  108,000

1. Investment income totaled $75,000 for the year.
2. Vouchers for the year were approved as follows:

Circulating library $189,000

Research library   74,000

Exhibits   15,000

Community services  12,000

General and administrative 166,000

Fund raising   103,000

Total $559,000

1. During the year, $500,000 worth of vouchers were paid.

Adjustment Data

1. Accounts Payable and Accrued Expenses at February 28, 2020, should be $217,000. The difference should be allocated to the following expenses:

Research library $5,000

General and administrative  3,000

1. Additions to the research library in the amount of $68,000 that were approved in (5) above were made in accordance with the terms of a contribution that had been received earlier and that was restricted for that purpose.
2. The current market value of the investments is $1,035,000 (no investment transactions occurred).
3. Depreciation amounted to $9,000 for the year. It should be allocated as follows:

Circulating library $3,500

Research library   2,900

General and administrative  2,600

1. Prepaid Expenses should be $60,000. The difference should be allocated to:

Exhibits $3,700

General and administrative  1,300

**Required:**

1. Prepare journal entries to record the transactions
2. Prepare the statement of financial position and the statement of activities for the year ended February 28, 2020.

**Answer**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Part A** | 1. | Cash Revenue - Service Fees Revenue - Book Rentals & Fines  | 151,000 | 30,000121,000 |
|  | 2. | Cash Grant Receivable Grant ReceivableSupport – Grants | 40,00020,000 | 40,00020,000 |
|  | 3. | Cash (Unrestricted)Cash – Temporarily RestrictedContributions – GiftsContributions – Restricted Support | 215,000108,000 | 215,000108,000 |
|  | 4. | Cash Investment Income  | 75,000 | 75,000 |
|  | 5. | Expenses - Circulating Library Expenses - Research Library Expenses - ExhibitsExpenses - Community Services Expenses - General & Administrative Expenses - Fund RaisingAccounts Payable  | 189,00074,00015,00012,000166,000103,000 | 559,000 |
|  | 6. | Accounts Payable Cash | 500,000 | 500,000 |
|  | 7. | Expenses - Research Library Expenses - General & Administrative Accrued Expenses  | 5,0003,000 | 8,000 |
|  | 8. | Net Assets Released from Restrictions Cash – Temporarily RestrictedCash – Unrestricted Net Assets Released from Restrictions | 68,00068,000 | 68,00068,000 |
|  | 9. | Investments Investment Income | 15,000 | 15,000 |
|  | 10. | Expenses - Circulating Library Expenses - Research Library Expenses - General & Administrative Accumulated Depreciation  | 3,5002,9002,600 | 9,000 |
|  | 11. | Expenses - Exhibits Expenses - General & Administrative Prepaid Expenses | 3,7001,300 | 5,000 |

**Part B**

**PRESTON LIBRARY**

**Statement of Financial Position, February 28, 2020**

|  |  |  |
| --- | --- | --- |
| Assets Current Assets Cash Grants Receivable Prepaid Expenses Total Investments (at market) Land, Buildings, and Equipment Less accumulated depreciation of $59,000 Total Assets Liabilities and Fund Balances Current Liabilities Accounts Payable & Accrued ExpensesTotal Long-term Debt Fund Balances Total Liabilities and Fund Balances  | Unrestricted$334,00060,000 60,000454,0001,035,000 521,000$2,010,000$ 217,000217,000200,000 1,593,000$2,010,000 | TemporarilyRestricted$120,000\_\_\_\_\_\_\_\_$120,000120,000$ 120,000 |

**PRESTON LIBRARY**

**Statement of Activities**

**For Year Ended February 28, 2020**

|  |  |  |
| --- | --- | --- |
| Support & Revenue Support GrantsGiftsTotal RevenueService FeesBook Rental & FinesInvestment Income 20-20Total Net Assets Released from RestrictionsTotal Revenue, Gains and Other SupportExpenses Program ServicesCirculating LibraryResearch LibraryExhibitsCommunity ServicesTotal Support ServicesGeneral & Administrative Fund Raising Total TotalIncrease (decrease) in Net AssetsFund Balances – Beginning of YearFund Balances – End of Year | WithoutDonorRestrictions$20,000 215,000 235,00030,000121,000 90,000 241,000 68,000 $544,000$192,500 81,900  18,700 12,000  305,100 172,900 103,000  275,900 $ 581,000($37,000) 1,630,000$1,593,000 | With donorRestrictions108,000108,000(68,000) 40,000 40,000 80,000$ 120,000 |

**Problem 3.** The partnership of Cain, Gallo, and Hamm engaged you to adjust its accounting records and convert them uniformly to the accrual basis in anticipation of admitting Kerns as a new partner. Some accounts are on the accrual basis and some are on the cash basis. The partnership's books were closed at December 31, 2019, by the bookkeeper, who prepared the general ledger trial balance that appears as follows:

****

Your inquiries disclose the following:

1. The partnership was organized on January 1, 2018. No provision was made in the partnership agreement for the allocation of partnership profits and losses. During 2018, profits were allocated equally among the partners. The partnership agreement was amended, effective January 1, 2019, to provide for the following profit and loss ratio: Cain, 40%; Gallo, 40%; and Hamm, 20%. The amended partnership agreement also stated that the accounting records were to be maintained on the accrual basis and that any adjustments necessary for 2018 should be allocated according to the 2019 profit allocation agreement.
2. The following amounts were not recorded as prepayments or accruals.

December 31 2019 2018

Prepaid insurance $700 $ 800

Advances from customers  900 1,500

Accrued interest expense —   450

The advances from customers were recorded as sales in the year the cash was received.

1. In 2019, the partnership recorded a provision of $8,000 for anticipated declines in inventory prices. You convinced the partners that the provision was unnecessary and should be removed from the books.
2. The partnership charged equipment purchased for $4,400 on January 1, 2019, to expense. This equipment has an estimated life of 10 years and an estimated salvage value of $400. The partnership depreciates its capitalized equipment using the declining balance method at twice the straight‐line depreciation rate.
3. The partners agreed to establish an allowance for doubtful accounts at 2% of current accounts receivable and 5% of past‐due accounts. At December 31, 2018, the partnership had $54,000 of accounts receivable, of which only $4,000 was past due. At December 31, 2019, 20% of accounts receivable was past due, of which $4,000 represented sales made in 2018 and was considered collectible. The partnership had written off uncollectible accounts in the year the accounts became worthless as follows:

Accounts Written Off In 2019 2018

2019 accounts $ 800   —

2018 accounts 1,000   $250

1. Goodwill was recorded on the books in 2019 and credited to the partners' capital accounts in the profit and loss ratio in recognition of an increase in the value of the business resulting from improved sales volume. The partners agreed to write off the goodwill before admitting the new partner.

**Required:**

Prepare a worksheet showing the adjustments and the adjusted trial balance for the partnership on the accrual basis at December 31, 2019. All adjustments affecting income should be made directly to partners' capital accounts. Supporting computations should be in good form. (Do not prepare formal financial statements or formal journal entries.)

**Answer**

 Adjustments to Adjustments To

 2018 Income 2019 Income

2. Prepaid insurance expensed in 2018 $800 $(800)a

 Prepaid insurance expensed in 2019 --- 700

 Advances from customers in 2018 (1,500) 1,500b

 Advances from customers in 2019 --- (900)

 Accrued interest expense (450) 450c

3. Add back provision for inventory decline 8,000

4. Add back purchase price of equipment expensed

 less depreciation expense of $880 3,520d

5. Deduct (add) adjustment to allowance account (1,200) 160e

6. Deduct goodwill recognized               (5,000)

 Total adjustment to capital accounts $(2,350) $7,630

aThis assumes that the prepaid insurance expires in the next year.

bThis assumes that the advances are earned in the next year.

cThis assumes that the interest expense was deducted in 2019.

dDepreciation expense = $4,400 × 0.20 = $880

 **2018 2019**

e2% of current receivables (0.02 × $50,000) $1,000 (0.02 × $32,000) $640

 5% of past due receivables (0.05 × $4,000) 200 (0.05 × $8,000) 400

 Allowance account balance at 12/31 $1,200 $1,040

|  |
| --- |
| Allowance for Bad Debts |
| Write-off-2019 1,800 | 1/1 1,200 |
|   | Adjustment 1,640 |
|  | 12/31 Bal. 1,040 |
|  |  |

During 2019, $1,800 was written off and debited to expense

Adjustment to income is $160 or ($1,800 - $1,640)

Analysis of Change in Capital Accounts

 2018 Adjustment 2019 Adjustment Total

Cain 1/3 $(783) 0.40 $3,052 $2,269

Gallo 1/3 (783) 0.40 3,052 2,269

Hamm 1/3 (784) 0.20 1,526 742

 $(2,350)\* $7,630 $5,280

\*Number is rounded: 

 Cain, Gallo, and Hamm Partnership

 Adjusted Trial Balance

 December 31, 2019

 Unadjusted Adjusted

          Balance      Adjustment Balance 12/31/2019

 Dr. Cr.       Dr        Cr      Dr. Cr.

Cash $15,000 $15,000

Accounts Receivable 40,000 40,000

Inventory 30,000 30,000

Land 9,000 9,000

Buildings 50,000 50,000

Allowance for Depreciation of Buildings 6,000 6,000

Equipment 56,000 4,400 60,400

Allowance for Depreciation of Equipment 6,000 880 6,880

Goodwill 5,000 5,000

Accounts Payable 56,000 56,000

Allowance for Future Inventory Losses 8,000 8,000

Cain, Capital 37,000 2,269 39,269

Gallo, Capital 60,000 2,269 62,269

Hamm, Capital 32,000 742 32,742

Prepaid Insurance 700 700

Advances from Customers 900 900

Allowance for Doubtful Accounts \_\_\_\_\_\_\_ \_\_\_\_\_\_\_ \_\_\_\_\_\_ 1,040 \_\_\_\_\_\_\_ 1,040

 $205,000 $205,000 $13,100 $13,100 $205,100 $205,100