1. During the year, Urban Theory Company's retained earnings increased from $38,000 to $50,000. The company earned net income of $18,000. How much in dividends did it declare during the year?

a. 0 (no dividends were paid)

b. $12,000

c. $6,000

d. $7,000

Answer: C  
Explanation: Apply the equation “Beginning balance of retained earnings + Net Income (minus Loss) – Dividends = Ending balance of retained earnings”.   
Net Income ($18,000) – Dividends ($X) = Increase in equity of $12,000  
Dividends = $18,000 - $12,000 = $6,000

2. *Javier’s* Company had total assets of $340,000 and total shareholders' equity of $130,000 at the beginning of the year. During the year assets increased by $70,000 and liabilities increased by $25,000. Shareholders' equity at the end of the year is:

a. $95,000

b. $175,000

c. $200,000

d. $155,000

Answer: B  
Explanation: Accounting equation of “Assets = Liabilities + Equity”  
$70,000 = $25,000 + Equity  
Equity = $70,000 - $25,000 = $45,000 (Increase in equity)  
Beginning shareholders’ equity ($130,000) + Increase in equity ($45,000) = $175,000

3. Office supplies having original cost $4,320 were unused till the end of the period. Office supplies having original cost of $22,800 are shown on unadjusted trial balance. What is the adjusting entry that should be done?

a. DR Supplies Expense $18,480, CR Office Supplies $18,480

b. DR Office Supplies $22,800, CR Supplies Expense $22,800

c. DR Supplies Expense $22,800, CR Office Supplies $22,800

d. DR Supplies Expense $4,320, CR Office Supplies $4,320

Answer: A

Explanation: $22,800 - $4,320 (Ending unused supplies) = $18,480 (USED supplies)

4. One month of ABC Company’s insurance expired in January. The original payment of $1,000 covers January through April. What’s the adjusting journal entry for this transaction?

a. DR Insurance Expense $1000, CR Prepaid Insurance $1000

b. DR Prepaid Insurance $1000, CR Insurance Expense $1000

c. DR Insurance Expense $250, CR Prepaid Insurance $250

d. DR Insurance Expense $750, CR Prepaid Insurance $750

Answer: C  
Explanation: Payment of $1,000 is for 4 months (Jan-Apr). Increase in Insurance expense of $250 ($1000/4) reflects the expiration of insurance in Jan. Credit Prepaid Insurance reflects a decrease in prepaid insurance because now the business has only pre-paid in advance of 3 months compared to the original 4 months. The pre-adjusted entry is DR Prepaid Insurance $1000 and CR Cash $1000.

5. APAC Company’s employees earned $800 during June and are paid in July. What journal entries should be recorded to reflect this information.

a. DR Wages Expense $800  
 CR Wages Payable $800  
 DR Wages Payable $800  
 CR Cash $800

b. DR Wages Expense $800  
 CR Wages Payable $800

c. DR Wages Payable $800  
 CR Cash $800

d. DR Wages Payable $800  
 CR Wages Expense $800

DR Cash $800  
 CR Wages Payable $800

Answer: A  
Explanation: Incur wages expense of $800 in June but yet to pay until July, hence credit Wages Payable (liability). In July, wages were paid, therefore credit cash to reflect a decrease in cash level and debit Wages Payable to reflect a decrease in liability.

6. $3,000 worth of service has been provided to the customer who paid an advance amount of $4,000. The adjusting entry is DR Unearned Revenue $4,000 and CR Service Revenue $4,000.

True/False?

Answer: False. It is DR Unearned Revenue $3,000 and CR Service Revenue $3,000.   
Explanation: $4,000 is the amount that customer has paid in advance. The journal entry for this is DR Cash $4,000 and CR Unearned Revenue $4,000. Now that $3,000 worth of service has been provided, we DR Unearned Revenue $3,000 to reflect a decrease in liability and CR Service Revenue $3,000 as the money is considered ‘earned’ now.

7. The equipment costing $80,000 has useful life of 5 years and its estimated salvage value is $14,000. Depreciation is provided using the straight line depreciation method. The adjusting entry for this transaction for 1 month of depreciation is to DR Depreciation Expense $13,200 and CR Accumulated Depreciation $13,200.

True/False?

Answer: False. It is DR Depreciation Expense $1,100 and CR Accumulated Depreciation $1,100.  
Explanation: ($80,000 - $14,000)/(5 x 12) = $1,100 depreciation expense per month\*

8. Issuance of share capital and net income result in an increase in equity, while a net loss and providing dividends result in a decrease in equity.

True/False?

Answer: True  
Explanation: Equity includes share capital and retained earnings. The share capital account shows the owners’ investment in the company. The retained earnings account shows the cumulative net income earned by the company over its lifetime, minus its cumulative net losses and dividends.