

## HOMEWORK PROBLEMS 3-1 AND 3-2

### Problem 3-1

Springfield Medical Center operates a nearby parking garage. Anyone is permitted to park in the parking garage. Parking charges are \$2.00 for the first two hours or part, \$1.00 for each additional hour or part to a maximum charge of \$5.00 for each 24 hour time period. For patients and visitors, the hospital will “validate” their parking tickets, permitting them to park for free. All a patient or visitor need do is bring the parking ticket to the information desk and have it stamped (with the name of the medical center). Fred has been the parking lot attendant for 7 years. He has been having some financial difficulties lately, so he decided to make a little extra money -- illegally. He had a rubber stamp produced with the name of the medical center -- virtually identical to the stamp used by the medical center to validate the parking tickets. When some of the paying customers would leave the parking deck, Fred would pocket the cash they paid and then he would stamp the ticket with the name of the medical center. Thus when the parking tickets were examined later, these tickets would be validated, and Fred would not be expected to have any money for them.

Requirements:

1. Explain how Fred might be caught
2. Indicate reasonable, cost-effective procedures that could be established to prevent such theft

### Problem 3-2

The balance sheet for the Petsmart, Inc as shown in it's January 29, 2006 10-K report reveals the following information about the current assets:

<b>Assets</b>	(add 000)	
	January 29 2006	January 30 2005
<b>Assets:</b>		
Cash and cash equivalents	\$110,415	\$ 87,032
Short-term investments	219,900	313,575
Receivables, net	36,902	27,123
Merchandise inventories	399,413	337,281
Deferred income taxes	26,254	19,881
Prepaid expenses and other current assets	<u>47,612</u>	<u>43,958</u>
<b>Total Current Assets</b>	<u>840,496</u>	<u>828,850</u>

The following footnote also appeared in the 10-K Report:

**Cash and Cash Equivalents** . . . As of January 29, 2006 and January 30, 2005, bank overdrafts of approximately \$40,257,000 and \$42,955,000, respectively, were included in accounts payable and bank overdraft in the Consolidated Balance Sheets. . . .

Required:

- a. Describe cash equivalents.
- b. How was the company able to overdraw its bank accounts by \$40,257,000 at January 29, 2006 without encountering difficulties with its banks?

### HOMEWORK PROBLEM 3-3

Use the internet to access the December 31, 2005 10-K for MGM Mirage. After reviewing the financial statements, including the footnotes and supporting schedules, answer the following questions:

- a. There are basically two methods of recognizing bad debt expense: (1) the direct write-off method, and (2) the allowance method. What are the deficiencies of the direct write-off method?
- b. If, during 2006, \$30,000 of MGM Mirage's accounts receivable were to be written off, what would be the effect on
  - Net income in the year of writeoff (ignore income tax effect)  
\_\_\_\_\_ (increase, decrease, no effect)
  - Total assets \_\_\_\_\_ (increase, decrease, no effect)
  - Total current assets \_\_\_\_\_ (increase, decrease, no effect)
- c. Based solely on the information presented in the MGM Mirage 10-K, show the journal entries, including amounts, that were most likely recorded during 2005, that affected the Allowance for Doubtful Accounts account for accounts receivable. You may assume that no accounts previously written off were subsequently collected.

## HOMEWORK PROBLEM 3-4

- (a) Use the internet to access the December 31, 2005 10-K report for Hershey Company. After reviewing the financial statements, including the footnotes, answer the following questions:
1. What is a LIFO reserve? How much was the LIFO reserve as of December 31, 2005?
  2. How much higher would pre-tax income in 2005 have been had the inventory been valued at current cost rather than LIFO?
  3. If replacement cost, rather than LIFO, was used to value the inventory, what would the inventory value be for Hershey Foods. on December 31, 2005?
  4. A primary ingredient for Hershey's chocolate is cocoa beans. Given that Hershey uses the LIFO inventory method, how old are the cocoa beans in their ending inventory?
- (b) Use the internet to access the December 31, 2005 10-K report for Keystone Consolidated Industries. After reviewing the financial statements, including the footnotes, answer the following questions:
1. What is the amount of the LIFO reserve as of December 31, 2005?
  2. What are "liquidation of LIFO inventory quantities"?
  3. What was the effect on net income due to the liquidation of LIFO inventory in **2003**? Why would this effect occur?
  4. Did the company deliberately liquidate inventories in **2003**?