

## SELF STUDY PROBLEM 8-1

An examination of the books of the Kalmire Company reveals the following information pertaining to the company's operations during 20x5:

Sales .....	\$150,000
Cost of Goods Sold .....	40,000
Additional Federal Income Tax	
Assessment for Prior Years .....	10,000
Cumulative Effect on Prior Years	
of Change in Depreciation	
Method (a loss) .....	10,000
Operating Expenses .....	20,000
Extraordinary Loss Due to an	
Earthquake* .....	30,000
Dividends Declared During 20x5 .....	25,000
Retained Earnings, December 31, 20x4 ....	400,000

\*This item was deemed to be an extraordinary item in accordance with the criteria specified by the Accounting Principles Board.

Assume the income tax rate to be a straight 40%. Furthermore assume that all revenues, expenses, and losses, except the additional tax assessment, affected this years income tax return.

Prepare, in good form, a multiple step income statement and a retained earnings statement for the Kalmire Company for the year 20x5. You may ignore earnings per share calculations and presentation.

## SELF STUDY PROBLEM 8-2

An examination of the books of the Whopper Company reveals the following information pertaining to the company's operations during 20x5:

Sales .....	\$650,000
Loss Resulting From an Unsuccessful Defense in a Lawsuit Arising From a Breach of Contract in a Prior Period	10,000
Operating Expenses .....	100,000
Dividends Declared During 20x5 .....	50,000
Extraordinary Loss Due to an Earthquake* .....	80,000
Cost of Goods Sold .....	300,000
Retained Earnings, December 31, 20x4 ....	900,000
Loss Due to Reduction of Inventory to Market .....	50,000

\*This item was deemed to be an extraordinary item in accordance with the criteria specified by the Accounting Principles Board.

Assume the income tax rate to be a straight 40%. Furthermore assume that all revenues, expenses, and losses affected this years income tax return.

Prepare, in good form, a single step income statement and a retained earnings statement for the Whopper Company for the year 20x5. You may ignore earnings per share calculations and presentation.

### SELF STUDY PROBLEM 8-3

Data pertaining to the operations of the Soderholm Company for the year 20x5 is shown below:

1. Net sales for the year, \$600,000
2. Selling expense for the year, \$100,000
3. The company suffered \$80,000 of damage to their office building as a result of an earthquake that occurred during the year. This was the first major earthquake recorded in this geographical area in modern times.
4. The company had 5,000 shares of common stock outstanding at the beginning of the year. On April 1, 20x5 the company sold 2,500 additional shares. On August 1, 20x5 the company issued a 2-for-1 stock split on the outstanding shares of common stock. On November 1, 20x5 the company retired 1,500 shares of its common stock.
5. Assume that the tax rate is a straight 40%.
6. General and administrative expense for the year, \$100,000
7. Cost of goods sold for the year, \$250,000.

Required:

Indicate the earnings per share data that would be reported at the bottom of the income statement for the Soderholm Company for the year ended December 31, 20x5.

SELF STUDY PROBLEM 8-4

Collins, Inc. presented the following data for the year ended December 31, 20x3:

Income before extraordinary item .....	\$6,400,000
Extraordinary loss, net of applicable income tax	
benefit of \$947,000 (See Note 1) .....	<u>1,420,000</u>
Net income .....	\$4,980,000

Note 1: On September 14, 20x3 the Company suffered substantial damage to their office building as a result of a hurricane. Hurricanes do not occur frequently in the Company's geographical area and therefore, the loss is shown as an extraordinary item.

Common Stock	Shares Outstanding
Balance, 1/1/x3	10,000,000
Issued for cash, 5/1/x3	3,000,000
2-for-1 stock split, 10/1/x3	

Required:

Indicate the earnings per share data that would be reported at the bottom of the income statement for Collins, Inc. for the year ended December 31, 20x3.

## SELF STUDY PROBLEMS 8-5 AND 8-6

### Problem 8-5

The Hagen Company presented the following data for the year ended June 30, 20x4:

Income before extraordinary item .....	\$9,752,000
Extraordinary loss, net of applicable income tax benefit (See Note 1) .....	<u>1,687,000</u>
Net income .....	\$8,065,000

Note 1: During the year, the Hagen Company suffered a major casualty loss of \$1,687,000 after applicable income tax reduction of \$1,755,000.

At the end of the current year, the Hagen Company has outstanding 7,000,000 shares of \$10 par common stock. On April 1, 20x4 the Hagen Company issued 1,000,000 shares of common stock for \$16 per share to help finance the casualty.

Required:

Indicate the earnings per share data that would be reported at the bottom of the income statement for the Hagen Company for the year ended June 30, 20x4.

### Problem 8-6

The Houston Co. presented the following data for the fiscal years ended December 31, 20x6 and 20x5:

Income before extraordinary item .....	\$ 700,000	\$ 660,000
Extraordinary loss, net of applicable income tax benefit of \$40,000 in 20x6 .....	<u>60,000</u>	<u>---</u>
Net income .....	\$ 640,000	\$ 660,000

At the beginning of 20x5 the Houston Co. had 100,000 shares of common stock outstanding. On March 1, 20x5 the company issued a 10% stock dividend. Another 10% stock dividend was also issued on March 1, 20x6. As of December 31, 20x6 the company has 121,000 shares of common stock outstanding.

Required:

Indicate the earnings per share data that would be reported at the bottom of the income statement for Houston Co. for the years ended December 31, 20x6 and 20x5.

SELF STUDY PROBLEM 8-7

As the accountant for the Lambert Company, you have been asked by the president of the company to prepare a single step income statement and a retained earnings statement for the year 20x4. Your assistant has prepared the following drafts of the statements:

Lambert Company		
Income Statement		
<u>December 31, 20x4</u>		
Net Sales .....		\$ 500,000
Cost of Goods Sold .....		<u>280,000</u>
Gross Margin .....		\$ 220,000
Operating Expenses		
Salaries and Wages Expense .....	\$ 80,000	
Depreciation Expense .....	30,000	
Miscellaneous Expense .....	<u>20,000</u>	
Total Operating Expenses .....		<u>130,000</u>
Net Income Before Extraordinary items and Income Taxes .....		\$ 90,000
Extraordinary Items		
Shutdown Expenses Incurred by the Company during a Major Strike by its Operating Employees in 20x4 .....	\$ 30,000	
Loss Due to Destruction of One of the Company's Storage Facilities Resulting from a Tornado .....	<u>20,000</u>	
Total Extraordinary Items .....		<u>50,000</u>
Net Income Before Income Taxes .....		\$ 40,000
Income Taxes .....		<u>16,000</u>
Net Income .....		\$ 24,000

Lambert Company		
Retained Earnings Statement		
<u>December 31, 20x4</u>		
Retained Earnings, January 1, 20x4 .....		\$ 450,000
Add: Net Income .....		<u>24,000</u>
		\$ 474,000
Deduct: Dividends Declared .....	\$ 10,000	
Adjustment for Understatement of Prior Year's Uncollectible Accounts Expense .....	<u>20,000</u>	<u>30,000</u>
Retained Earnings, December 31, 20x4 .....		\$ 444,000

Using the information contained in the above statements, prepare a corrected income statement and a corrected retained earnings statement. You may assume that all revenues are taxable and all costs and expenses are tax deductible. You may also assume that the tax rate is a straight 40%, the company uses the allowance method for accounts receivable, and that ten thousand shares of common stock were outstanding during the entire year.

SELF STUDY PROBLEM 8-8

As the accountant for the XYZ Company, you have been asked by the president of the company to prepare a single step income statement and a retained earnings statement for the year 20x4. Your assistant has prepared the following drafts of the statements:

XYZ Company Income Statement <u>December 31, 20x4</u>		
Net Sales .....		\$ 500,000
Cost of Goods Sold .....		<u>280,000</u>
Gross Margin .....		\$ 220,000
Operating Expenses		
Salaries and Wages Expense .....	\$ 80,000	
Depreciation Expense .....	30,000	
Miscellaneous Expense .....	<u>20,000</u>	
Total Operating Expenses .....		<u>130,000</u>
Net Income Before Extraordinary items and Income Taxes .....		
		\$ 90,000
Extraordinary Items		
Loss Due to Flood* (Note 1) .....	\$ 30,000	
Depreciation Expense Erroneously Omitted From Last Years Financial Statements. The Amount Represents Depreciation on a Building Newly Constructed in 20x3 .....	<u>5,000</u>	<u>35,000</u>
Net Income Before Income Taxes .....		
		\$ 55,000
Income Taxes .....		<u>22,000</u>
Net Income .....		\$ 33,000

\*This item was deemed to be an extraordinary item in accordance with the criteria specified by the Accounting Principles Board.

XYZ Company		
Retained Earnings Statement		
<u>December 31, 20x4</u>		
Retained Earnings, January 1, 20x4 .....		\$ 450,000
Add: Net Income .....		<u>33,000</u>
		\$ 483,000
Deduct: Dividends Declared .....	\$ 10,000	
Loss Resulting From an Unsuccessful Defense in a Lawsuit Arising From a Breach of Contract in a Prior Year .....	20,000	<u>30,000</u>
Retained Earnings, December 31, 20x4 .....		\$ 453,000

Using the information contained in the above statements and assuming all amounts to be material, prepare a corrected income statement and a corrected retained earnings statement. You may assume that all revenues are taxable and all expenses are tax deductible. You may ignore per share calculations and presentation. Assume that the tax rate is a straight 40%.

SELF STUDY PROBLEM 8-1  
ANSWERS

Kalmire Company		
Income Statement		
<u>For the Year Ended December 31, 20x5</u>		
Net Sales .....		\$ 150,000
Cost of Goods Sold .....		<u>40,000</u>
Gross Margin .....		110,000
Operating Expenses .....		<u>20,000</u>
Income Before Taxes and Extraordinary Items	90,000	
Less: Applicable Income Taxes .....	\$ 36,000	
Additional Federal Income Tax		
Assessment for Prior Years .....	<u>10,000</u>	<u>46,000</u>
Income Before Extraordinary and Other Items	44,000	
Extraordinary Loss Due to an Earthquake		
(Less Applicable Income Taxes of \$12,000) .	\$ 18,000	
Cumulative Effect on Prior Years of Change in Depreciation Method (Less Applicable Income Taxes of \$4,000) .....	<u>6,000</u>	( <u>24,000</u> )
Net Income .....		<u>\$ 20,000</u>

Kalmire Company		
Retained Earnings Statement		
<u>For the Year Ended December 31, 20x5</u>		
Retained Earnings, December 31, 20x4 .....		\$ 400,000
Add: Net Income .....		<u>20,000</u>
		420,000
Deduct: Dividends Declared .....		<u>25,000</u>
Retained Earnings, December 31, 20x5 .....		<u>\$ 395,000</u>

SELF STUDY PROBLEM 8-2  
ANSWERS

Whopper Company	
Income Statement	
<u>For the Year Ended December 31, 20x5</u>	
Net Sales .....	\$ 650,000
Costs and Expenses:	
Cost of Goods Sold .....	\$ 300,000
Operating Expenses .....	100,000
Loss Due to Reduction of Inventory to Market .....	50,000
Loss Resulting From an Unsuccessful Defense in a Lawsuit Arising From a Breach of Contract in a Prior Period ....	10,000
Income Taxes .....	<u>76,000</u>
Total Costs and Expenses .....	<u>536,000</u>
Income Before Extraordinary Items .....	114,000
Extraordinary Loss Due to an Earthquake (Less Applicable Income Tax Benefits of \$32,000) .....	<u>48,000</u>
Net Income .....	<u><u>\$ 66,000</u></u>

Whopper Company	
Retained Earnings Statement	
<u>For the Year Ended December 31, 20x5</u>	
Retained Earnings, December 31, 20x4 .....	\$ 900,000
Add: Net Income .....	<u>66,000</u>
	966,000
Deduct: Dividends Declared .....	<u>50,000</u>
Retained Earnings, December 31, 20x5 .....	<u><u>\$ 916,000</u></u>

SELF STUDY PROBLEM 8-3  
ANSWERS

Calculation of income figures:

Net Sales .....		\$ 600,000
Cost of Goods Sold .....		<u>300,000</u>
Gross Margin .....		\$ 350,000
Operating Expenses		
Selling Expense .....	\$ 100,000	
General & Administrative Expense .....	<u>100,000</u>	<u>200,000</u>
Income Before Taxes and Extraordinary Item .....		\$ 150,000
Applicable Income Taxes (40%) .....		<u>60,000</u>
Income Before Extraordinary Item .....		\$ 90,000
Extraordinary Loss, Net of Tax Effect of \$32,000		
(\$80,000 x 40%) .....		<u>48,000</u>
Net Income .....		<u><u>\$ 42,000</u></u>

Calculation of weighted average number of shares of stock outstanding:

Months	Shares	Shares adjusted for stock split	Product
(a)	(b)	(c)	(a) x (c)
3	5,000	10,000	30,000
4	7,500	15,000	60,000
3	15,000	15,000	45,000
<u>2</u>	13,500	13,500	<u>27,000</u>
12			162,000

Weighted average number of shares of stock outstanding =  $162,000/12 = 13,500$

Per Share of Common Stock

Income Before Extraordinary Item (\$90,000/13,500) .....	\$ 6.67
Extraordinary Loss, Net of Tax Effect (\$48,000/13,500) .....	<u>3.56</u>
Net Income (\$42,000/13,500 or plug figure) .....	<u><u>\$ 3.11</u></u>

SELF STUDY PROBLEM 8-4  
ANSWERS

Number of Shares Outstanding

Months (a)			Unadjusted Shares (b)	Shares adjusted for stock split (c)	Product (a) x (c)
1/1 to 4/30	4 months		10,000,000	20,000,000	80,000,000
5/1 to 9/30	5 months		13,000,000	26,000,000	130,000,000
10/1 to 12/31	<u>3 months</u>		26,000,000	26,000,000	<u>78,000,000</u>
	12 months				288,000,000

Weighted average number of shares of stock outstanding =  $288,000,000 / 12 = 24,000,000$

Per Share of Common Stock

Income Before Extraordinary Item (\$6,400,000/24,000,000) .....	\$	0.27
Extraordinary Loss, Net of Tax Effect (\$2,420,000/24,000,000) .		<u>0.06</u>
Net Income (\$4,980,000/24,000,000 or plug figure) .....	\$	<u><u>0.21</u></u>

SELF STUDY PROBLEMS 8-5 AND 8-6  
ANSWERS

Problem 8-5

Number of Shares Outstanding

	Months (a)	Shares (b)	Product (a) x (b)
7/1 to 3/31	9 months	6,000,000	54,000,000
4/1 to 6/30	<u>3 months</u>	7,000,000	<u>21,000,000</u>
	12 months		75,000,000

Weighted average number of shares of stock outstanding =  $75,000,000/12 = 6,250,000$

Per Share of Common Stock

Income Before Extraordinary Item (\$9,752,000/6,250,000) .....	\$	1.56
Extraordinary Loss, Net of Tax Effect (\$1,687,000/6,250,000) ..		<u>0.27</u>
Net Income (\$8,065,000/6,250,000 or plug figure) .....	\$	<u>1.29</u>

Problem 8-6

Calculation of weighted average number of shares of stock outstanding:

Year	Months	Shares	Shares adjusted for stock dividend
20x5	2	100,000	$100,000 \times 110\% \times 110\% = 121,000$
	10	110,000	$110,000 \times 110\% = 121,000$
20x6	2	110,000	$110,000 \times 110\% = 121,000$
	10	121,000	121,000

Note: As a result of a stock dividend, shares outstanding for all prior periods would be appropriately adjusted. Given that there were no other transactions affecting the shares outstanding except the stock dividends, all prior shares are adjusted to the same total, 121,000 shares.

Per Share of Common Stock	<u>20x6</u>	<u>20x5</u>
Income before extraordinary item	\$5.79	\$5.45
20x6: \$700,000/121,000		
20x5: \$660,000/121,000		
Extraordinary loss, net of taxes	<u>\$0.50</u>	<u>\$ --</u>
20x6: \$ 60,000/121,000		
Net income	\$5.29	\$5.45
20x6: \$650,000/121,000 or plug figure		

SELF STUDY PROBLEM 8-7  
ANSWERS

Lambert Company  
Income Statement  
For the Year Ended December 31, 20x4

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Net Sales .....		\$ 500,000
Costs and Expenses		
Cost of Goods Sold .....		280,000
Salaries and Wages Expense .....		80,000
Depreciation Expense .....		30,000
Adjustment for Understatement of Prior Year's Uncollectible Accounts Expense .....		20,000
Shutdown Expenses Incurred by the Company during a Major Strike by its Operating Employees in 20x4 .....		30,000
Miscellaneous Expense .....		<u>20,000</u>
Total Costs and Expenses .....		460,000
Income Before Income Taxes and Extraordinary items .....		40,000
Applicable Income Taxes .....		<u>16,000</u>
Income Before Extraordinary Item .....		24,000
Extraordinary Item		
Extraordinary Loss Due to Destruction of One of the Company's Storage Facilities Resulting from a Tornado, Net of Tax Effect of \$8,000 .....		<u>12,000</u>
Net Income .....		<u><u>\$ 12,000</u></u>

Lambert Company  
Retained Earnings Statement  
For the Year Ended December 31, 20x4

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Retained Earnings, December 31, 20x3 .....		\$ 450,000
Add: Net Income .....		<u>12,000</u>
		462,000
Deduct: Dividends Declared .....		<u>10,000</u>
Retained Earnings, December 31, 20x4 .....		<u><u>\$ 452,000</u></u>

SELF STUDY PROBLEM 8-8  
ANSWERS

XYZ Company  
Income Statement  
For the Year Ended December 31, 20x4

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Net Sales .....	\$ 500,000
 Costs and Expenses	
Cost of Goods Sold .....	280,000
Salaries and Wages Expense .....	80,000
Depreciation Expense .....	30,000
Loss Resulting From an Unsuccessful Defense in a Lawsuit Arising From a Breach of Contract in a Prior Year .....	20,000
Miscellaneous Expense .....	<u>20,000</u>
Total Costs and Expenses .....	430,000
 Income Before Income Taxes and Extraordinary Item .....	 70,000
 Applicable Income Taxes .....	 <u>28,000</u>
 Income Before Extraordinary Item .....	 42,000
 Extraordinary Loss Due to Flood, Net of Tax Effect of \$12,000 .....	 <u>18,000</u>
 Net Income .....	 <u>\$ 24,000</u>

XYZ Company  
Retained Earnings Statement  
For the Year Ended December 31, 20x4

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Retained Earnings, December 31, 20x3, as reported .....	\$ 450,000
Deduct: Correction of Prior Year Error -- Depreciation Expense Erroneously Omitted From Last Years Financial Statements, Net of Tax Effect of \$2,000 .....	 <u>3,000</u>
Retained Earnings, December 31, 20x3, as adjusted .....	\$ 447,000
Add: Net Income .....	<u>24,000</u>
	471,000
Deduct: Dividends Declared .....	<u>10,000</u>
Retained Earnings, December 31, 20x4 .....	<u>\$ 461,000</u>