

Competency Exam – Practice

The competency exam consists of 15 multiple choice questions and one comprehensive Accounting Cycle Process problem. This competency exam practice document breaks the multiple choice questions and the Accounting Cycle Practice problem into two sections:

MULTIPLE CHOICE QUESTIONS

In order to prepare for the multiple choice questions on the competency exam, you should be prepared to answer questions based on the following topics:

- Understand the fundamental $A = L + E$ equation.
- What are assets?
- What are liabilities?
- Understand the concept of contra-accounts.
- Understand the normal balances of accounts.
- Who uses financial information?
- What does financial information capture and report?
- When do companies have to report financial information? When is their year end?
- Understand the matching principle.
- Understand the revenue principle.
- Understand how to record a liability.
- Understand how to record an asset.
- Understand cash dividends.
- Understand which accounts are affected by an adjusting journal entry.
- Understand why adjusting journal entries are made.
- What is net income?
- Be able to calculate and record Interest Expense or Interest Revenue
- Be able to calculate and record depreciation expense using straight line depreciation
- Be able to record a simple common stock and APIC transaction
- Be able to record a cash dividend transaction
- What are the different trial balances and when are they used?
- Understand the closing process.

SPECIFIC TRANSACTION EXAMPLES

The Competency Exam may include questions asking you to account for the sale of common stock by a company, transactions related to cash dividends, error corrections, and adjusting entries to reach a desired ending balance.

In addition to the comprehensive problem presented in this Practice Exam, you should familiarize yourself with these specific transaction examples.

Cash Dividends (Simplified)

For the purpose of this exam, a company accounts for the declaration, recording, and paying of cash dividends in one simplified transaction. This would normally occur over an extended period of time, require a calculation of the total dividend paid based on the dividend amount per share and the number of shares outstanding, and encompass multiple events.

Example: ABC Company issued and paid a cash dividend of \$5,500 on December 5.

Dr. Dividends Declared	\$5,500
Cr. Cash	\$5,500

Note: *The Dividend Declared account is a temporary account that is closed to retained earnings at the end of the period.*

Sale of Common Stock

When a company issues common stock for cash, generally there are two components of the selling price, a per-share par value and the additional paid-in capital. These concepts will be presented in more detail in future accounting classes. For this exam, familiarize yourself with how to calculate the gross proceeds from a sale of common stock and how to record the allocation of the sales proceeds to the two equity accounts affected by this transaction.

Example: DDB Company issued 1,000 shares of common stock with a par value of \$1 for \$18 per share.

Dr. Cash	\$18,000	(1,000 shares X \$18/share)
Cr. Common Stock (Par)	\$1,000	(1,000 shares X \$1/share)
Cr. Additional Paid-In Capital	\$17,000	(1,000 shares X \$17/share)

In this example, you are able to determine the additional paid-in capital (\$17) as the difference between the sale price (\$18) and the par value (\$1).

Error Corrections

There is more than one method to correct an accounting error. The multi-step approach involves reversing the original entry and entering a new one. A more direct approach is to correct the error with one entry that involves only the amount needed to correct the error.

Example: The amount recorded for Supplies paid on account was entered as \$517 but should have been \$157. Correct the error using only one entry.

Dr. Accounts Payable	\$360
Cr. Supplies	\$360

First, determine the difference between the correct and incorrect amounts (\$517 – \$157 = \$360) and if the accounts are overstated (higher than they should be) or understated (lower

than they should be). In this case, both accounts are overstated and you need to reduce them by \$360. Crediting Supplies (an asset account) and debiting Accounts Payable (a liability account) will reduce them by the amount needed to correct the error. The resulting effect is that each of these accounts would reflect balances related to this transaction of \$157.

Calculating an Accrual Amount to Reach a Desired Ending Balance

A company may purchase something (supplies), prepay an expense (rent), incur a liability (unearned revenue), or accrue an allowance (allowance for doubtful accounts) that must be adjusted at the end of the period to account for subsequent events that affected these account balances. Sometimes you may determine a desired ending balance and need to adjust the balance on the books to match that desired balance.

Example: JIT Company had a beginning balance of \$17,000 in Inventory. During the year they purchased \$25,000 more. After conducting a year-end physical inventory they determined the inventory on hand was \$12,500. Record the Costs of Goods sold for the year.

Dr.	Cost of Goods Sold	\$29,500	Recognize Expense
Cr.	Inventory	\$29,500	Decrease Inventory (Asset)

Remember 'BASE'

<i>Beginning Balance</i>	\$17,000
<i>Add: Purchases</i>	\$25,000
<i>Subtract: Sales</i>	<u>x</u>
<i>Ending Balance</i>	\$12,500

$$\begin{aligned} \$17,000 + \$25,000 - x &= \$12,500 \\ \$42,000 - x &= \$12,500 \\ x &= \$42,000 - \$12,500 \\ x &= \$29,500 \end{aligned}$$

Other Accrual Adjustments

You should also know how to perform the following initial and period-end adjusting entries:

Prepaid Expense

Example: On November 1, FLY Company paid \$6,000 in advance for rent for the next six months. The period ends December 31.

Initial Entry

Dr.	Prepaid Rent	\$6,000	Increase Asset
Cr.	Cash	\$6,000	Decrease Asset (Spent \$)

Year-end Adjusting Entry

Dr.	Rent Expense	\$2,000	Recognize Expense
Cr.	Prepaid Rent	\$2,000	Decrease Asset

The adjusting entry recognizes that the company incurred a rent expense for two months (2 X \$1,000/month [\$6,000/6 months]), which reduced their asset (Prepaid Rent) to \$4,000. The remaining balance will be expensed as incurred in the next period.

Unearned Revenue

Example: On September 1, Orville Norville paid BUG Company \$600 in advance for pest control services. Before the end of the year he used \$450 worth of services.

Initial Entry for BUG

Dr.	Cash	\$600	Increase Asset
Cr.	Unearned Revenue	\$600	Increase Liability

Unearned Revenue is a liability because BUG has not yet performed services to earn the revenue and is obligated to Norville.

Year-end Adjusting Entry

Dr.	Unearned Revenue	\$450	Decrease Liability
Cr.	Service Revenue	\$450	Recognize Revenue

After the adjustment, BUG will have \$150 remaining in Unearned Revenue related to Norville.

ACCOUNTING CYCLE PRACTICE PROBLEM

The following practice problem is an example of the material that will be tested on the competency exam. The actual exam is not as long as the practice problem and will not have you completing all parts below, but this comprehensive practice problem will prepare you for the Accounting Process Cycle problem in the competency exam. Use the information and worksheets to practice the problem. The answers have been provided. Use the following information and complete the instructions below:

For the past several years, John Addams has operated a part-time business from his home. As of April 1, 2002, John decided to move to rented quarters and to operate the business, which was to be known as Addams & Family Inc., on a full-time basis. Addams & Family entered into the following transactions during April:

- April 4 The following assets were received from John Addams: cash, \$10,000; accounts receivable, \$1,500; supplies, \$1,250; and office equipment, \$7,500. There were no liabilities received.
- April 4 Paid three months' rent on a lease rental contract, \$4,500.
- April 4 Paid the premium on property and casualty insurance policies for the year, \$1,800.
- April 6 Received cash from clients as an advance payment for services to be provided, \$3,000.
- April 7 Purchased additional office furniture on account from Morrilton Company, \$1,800.
- April 8 Received cash from clients on account, \$800.
- April 11 Paid cash for newspaper advertisement, \$120.
- April 12 Paid Morrilton Company \$800 for debt incurred on April 7.
- April 15 Recorded services provided on account for the period April 4-15, \$2,250
- April 15 Paid part-time receptionist for two weeks salary, \$400.
- April 15 Recorded cash from cash clients for fees earned April 4-15, \$3,175.
- April 18 Paid cash for supplies, \$750.
- April 22 Recorded services provided on account for April 18-22, \$1,100.
- April 22 Recorded cash from cash clients for fees earned April 18-22, \$1,850.
- April 25 Received cash from clients on account, \$1,600.
- April 27 Paid part-time receptionist for two week's salary, \$400.
- April 28 Paid telephone bill for April, \$130.
- April 29 Paid electric bill for April, \$200.
- April 29 Recorded cash from cash clients for fees earned April 25-29, \$2,050.
- April 29 Recorded services provided on account for April 25-29, \$1,000.
- April 29 John received \$4,500 from the company as his salary.

Instructions: (The first transaction has been recorded and posted for you).

1. Record the transactions stated above in good general journal form.
2. Post the transactions to T-accounts.
3. Record and post the following adjustments:
 - a. Insurance expired in April, \$150.
 - b. Supplies on hand April 29, \$1,020.
 - c. Depreciation for the office equipment in April, \$500.
 - d. Accrued receptionist salary on April 30, \$20.
 - e. Rent expired in April, \$1,500.
 - f. Earned \$2,000 of services that were previously paid for on 4/6.
5. Prepare an Income Statement, Statement of Retained Earnings and Balance Sheet.
6. Record and post closing entries.
7. Prepare a post-closing trial balance.

Cash	
4/4	10,000
End Bal	

End Bal	

Office Equipment	
4/4	7,500
End Bal	

End Bal	

Accounts Receivable	
4/4	1,500
End Bal	

End Bal	

Supplies	
4/4	1,250
End Bal	

End Bal	

End Bal	

End Bal	

<u>Contributed Capital</u>	
	20,250 4/4
End Bal	

End Bal	

<u>Service Revenue</u>	
End Bal	

End Bal	

End Bal	

End Bal	

End Bal	

End Bal	

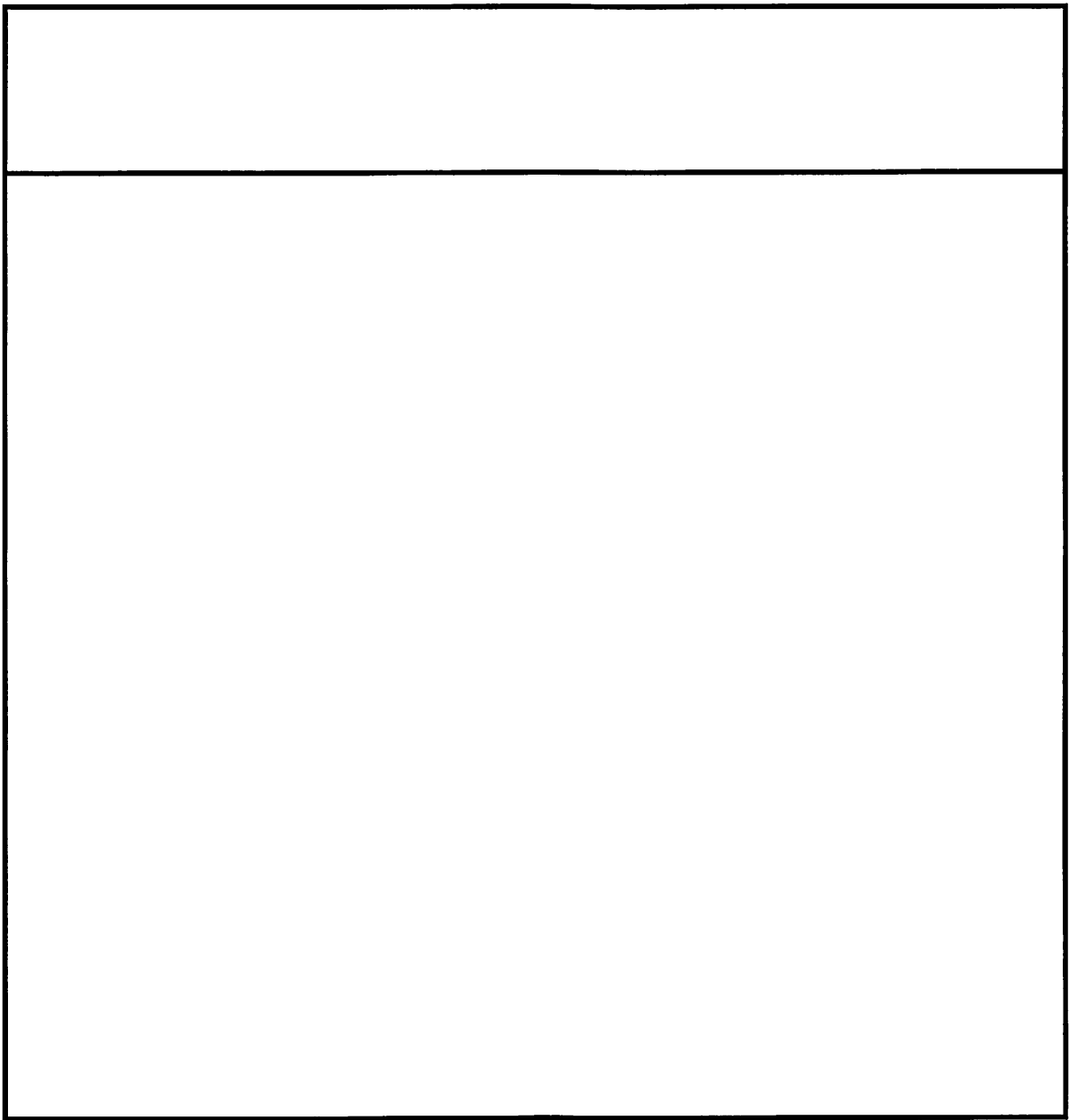
End Bal	

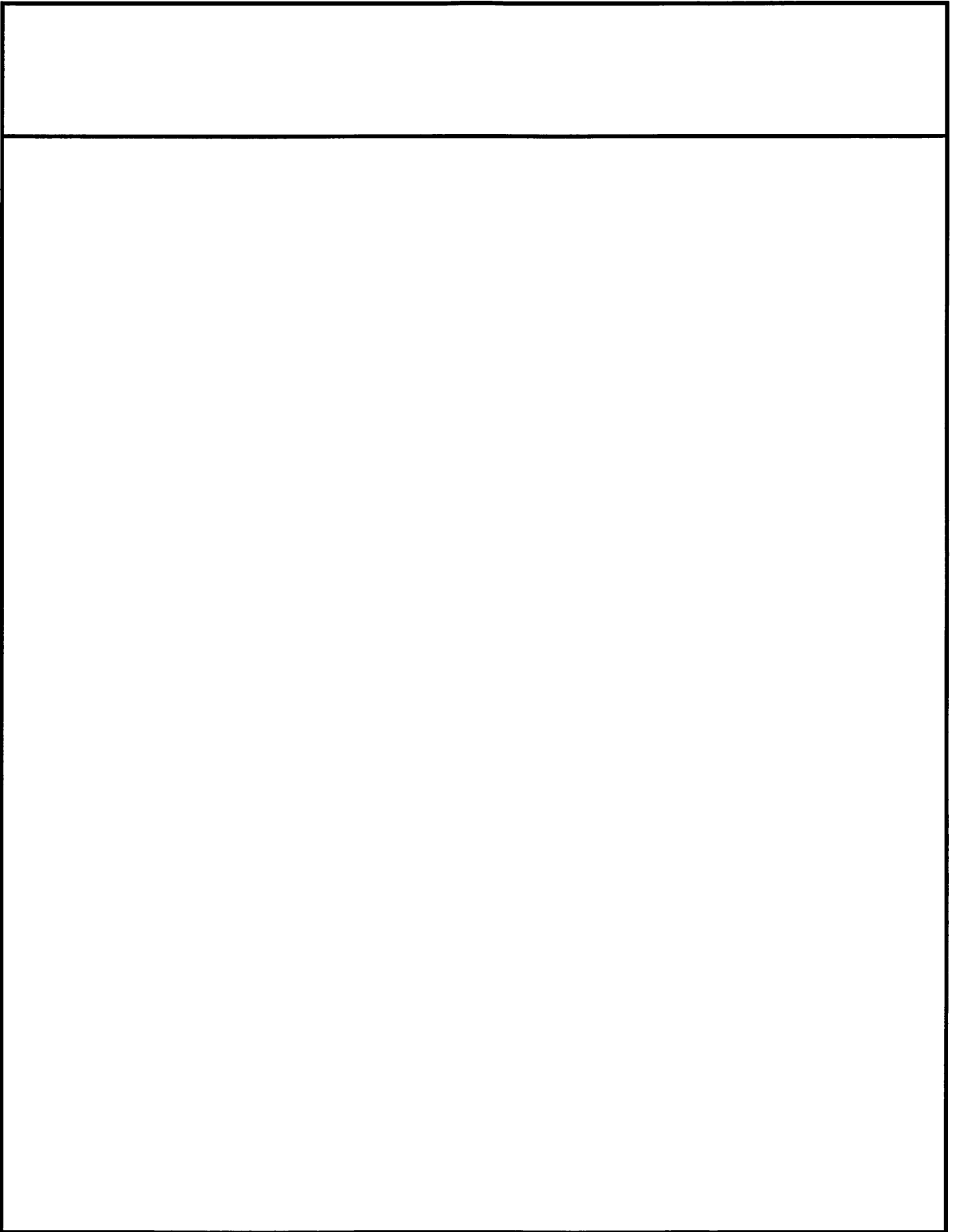
End Bal	

End Bal	

Addams & Family Inc.
Adjusted Trial Balance
For the Year Ended December 31st, 2010

	<u>Debit</u>	<u>Credit</u>
Cash		
Accounts Receivable		
Prepaid Rent		
Prepaid Insurance		
Supplies		
Office Equipment		
Accumulated Depreciation, Equipment		
Accounts Payable		
Salaries Payable		
Unearned Revenue		
Contributed Capital		
Retained Earnings		
Dividends Declared		
Service Revenue		
Insurance Expense		
Depreciation Expense		
Rent Expense		
Supplies Expense		
Salaries Expense		
Telephone Expense		
Utilities Expense		
Advertising Expense		





Addams & Family Inc.
Post-Closing Trial Balance
For the Year Ended December 31st, 2010

	<u>Debit</u>	<u>Credit</u>
Cash		
Accounts Receivable		
Prepaid Rent		
Prepaid Insurance		
Supplies		
Office Equipment		
Accumulated Depreciation, Equipment		
Accounts Payable		
Salaries Payable		
Unearned Revenue		
Contributed Capital		
Retained Earnings		
Dividends Declared		
Service Revenue		
Insurance Expense		
Depreciation Expense		
Rent Expense		
Supplies Expense		
Salaries Expense		
Telephone Expense		
Utilities Expense		
Advertising Expense		

Competency Exam
Accounting Cycle Process Problem
Solution

General Journal			
Date	Account Title	Debit	Credit
4/4	Cash	10,000	
	Accounts Receivable	1,500	
	Supplies	1,250	
	Office Equipment	7,500	
	Contributed Capital		20,250
4/4	Prepaid Rent	4,500	
	Cash		4,500
4/4	Prepaid Insurance	1,800	
	Cash		1,800
4/6	Cash	3,000	
	Unearned Revenue		3,000
4/7	Office Equipment	1,800	
	Accounts Payable		1,800
4/8	Cash	800	
	Accounts Receivable		800
4/11	Advertising Expense	120	
	Cash		120
4/12	Accounts Payable	800	
	Cash		800
4/15	Accounts Receivable	2,250	
	Service Revenue		2,250
4/15	Salaries Expense	400	
	Cash		400
4/15	Cash	3,175	
	Service Revenue		3,175

General Journal

Date	Account Title	Debit	Credit
4/18	Supplies	750	
	Cash		750
4/22	Accounts Receivable	1,100	
	Service Revenue		1,100
4/22	Cash	1,850	
	Service Revenue		1,850
4/25	Cash	1,600	
	Accounts Receivable		1,600
4/27	Salaries Expense	400	
	Cash		400
4/28	Telephone Expense	130	
	Cash		130
4/29	Utilities Expense	200	
	Cash		200
4/29	Cash	2,050	
	Service Revenue		2,050
4/29	Accounts Receivable	1,000	
	Service Revenue		1,000
4/29	Salaries Expense	4,500	
	Cash		4,500

Cash			
4/4	10,000	4,500	4/4
4/6	3,000	1,800	4/4
4/8	800	120	4/11
4/15	3,175	800	4/12
4/22	1,850	400	4/15
4/25	1,600	750	4/18
4/29	2,050	400	4/27
		130	4/28
		200	4/29
		4,500	4/29
End Bal	8,875		

Prepaid Insurance		
4/4	1,800	
		150 AJE (a)
End Bal	1,650	

Office Equipment		
4/4	7,500	
4/7	1,800	
End Bal	9,300	

Accounts Receivable			
4/4	1,500	800	4/8
4/15	2,250	1,600	4/25
4/22	1,100		
4/29	1,000		
End Bal	3,450		

Accumulated Depr		
		500 AJE (c)
End Bal		500

Accounts Payable		
		1,800 4/7
4/12	800	
End Bal		1,000

Supplies			
4/4	1,250		
4/18	750		
		980	AJE (b)
End Bal	1,020		

Salaries Payable		
		20 AJE (d)
End Bal		20

Prepaid Rent			
4/4	4,500		
		1,500	AJE (e)
End Bal	3,000		

Unearned Revenue		
		3,000 4/6
AJE (f)	2,000	
End Bal		1,000

Contributed Capital	
	20,250 4/4
End Bal	20,250

Retained Earnings	
	0 4/1
End Bal	-

Service Revenue	
	2,250 4/15
	3,175 4/15
	1,100 4/22
	1,850 4/22
	2,050 4/29
	1,000 4/29
	2,000 AJE (f)
End Bal	13,425

Insurance Expense	
AJE (a)	150
End Bal	150

Depr Exp	
AJE (c)	500
End Bal	500

Rent Expense	
AJE (e)	1,500
End Bal	1,500

Supplies Expense	
AJE (b)	980
End Bal	980

Salaries Expense	
4/15	400
4/27	400
4/29	4,500
AJE (d)	20
End Bal	5,320

Telephone Expense	
4/28	130
End Bal	130

Utilities Expense	
4/29	200
End Bal	200

Advertising Expense	
4/11	120
End Bal	120

Addams & Family Inc.
Adjusted Trial Balance
For the Year Ended December 31st, 2010

	<u>Debit</u>	<u>Credit</u>
Cash	\$ 8,875	
Accounts Receivable	3,450	
Prepaid Rent	3,000	
Prepaid Insurance	1,650	
Supplies	1,020	
Office Equipment	9,300	
Accumulated Depreciation, Equipment		\$ 500
Accounts Payable		1,000
Salaries Payable		20
Unearned Revenue		1,000
Contributed Capital		20,250
Retained Earnings		0
Dividends Declared		0
Service Revenue		13,425
Insurance Expense	150	
Depreciation Expense	500	
Rent Expense	1,500	
Supplies Expense	980	
Salaries Expense	5,320	
Telephone Expense	130	
Utilities Expense	200	
Advertising Expense	120	
	<u>\$ 36,195</u>	<u>\$ 36,195</u>

Addams & Family Inc.
Income Statement
For the Year Ended April 30, 2010

Revenues

Service Revenue	\$ 13,425
Total Revenues	<u>13,425</u>

Expenses

Insurance Expense	150
Depreciation Expense	500
Rent Expense	1,500
Supplies Expense	980
Salaries Expense	5,320
Telephone Expense	130
Utilities Expense	200
Advertising Expense	120
Total Expenses	<u>8,900</u>

Net Income (Loss)	<u><u>\$ 4,525</u></u>
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Addams & Family Inc.
Statement of Retained Earnings
For the Year Ended April 30, 2010

Beg Retained Earnings, 4/1/10	\$ 0
Add: Net Income	4,525
Less: Dividends	<u>0</u>
End Retained Earnings, 4/30/10	<u><u>\$ 4,525</u></u>

Addams & Family Inc.

Balance Sheet

At April 30, 2010

Assets

Current Assets

Cash	\$ 8,875	
Accounts Receivable	3,450	
Prepaid Rent	3,000	
Prepaid Insurance	1,650	
Supplies	1,020	

Total Current Assets \$ 17,995

Property Plant & Equipment

Office Equipment	9,300	
Accumulated Depreciation	(500)	

Property Plant & Equipment, Net 8,800

Total Assets 26,795

Liabilities & Stockholders' Equity

Liabilities

Current Liabilities

Accounts Payable	1,000	
Salaries Payable	\$ 20	

Total Current Liabilities 1,020

Unearned Revenue 1,000

Total Liabilities 2,020

Stockholders' Equity

Contributed Capital 20,250

Retained Earnings 4,525

Total Stockholders' Equity 24,775

Total Liabilities & Stockholders' Equity \$ 26,795

Addams & Family Inc.
 Post-Closing Trial Balance
 For the Year Ended December 31st, 2010

	Debit	Credit
Cash	\$ 8,875	
Accounts Receivable	3,450	
Prepaid Rent	3,000	
Prepaid Insurance	1,650	
Supplies	1,020	
Office Equipment	9,300	
Accumulated Depreciation, Equipment		500
Accounts Payable		1,000
Salaries Payable		20
Unearned Revenue		1,000
Contributed Capital		20,250
Retained Earnings		4,525
Dividends Declared		0
Service Revenue		0
Insurance Expense	0	
Depreciation Expense	0	
Rent Expense	0	
Supplies Expense	0	
Salaries Expense	0	
Telephone Expense	0	
Utilities Expense	0	
Advertising Expense	0	
	\$ 27,295	\$ 27,295