Q16-1  The AICPA, through various committees, made pronouncements that guided the development of accounting practice to 1973. The major AICPA accounting standard setting committees were the Committee on Accounting Procedure (1937–1959) and the Accounting Principles Board (1959–1973).

Q16-2  In 1937, the AICPA created the Committee on Accounting Procedure, which issued a series of Accounting Research Bulletins (ARBs). The last ARB was issued in 1957 In 1959, this committee was replaced by the Accounting Principles Board (APB), which was also a committee of the AICPA. The APB issued 31 APB Opinions from 1962 to 1973, when it was replaced by the Financial Accounting Standards Board (FASB).

Q16-3  The FASB exists to study financial accounting problem areas and to issue guidelines for accountants to follow. The primary reporting standards issued by the FASB are called Statements of Financial Accounting Standards (SFAS). The FASB also issues Statements of Financial Accounting Concepts (SFAC), which are the basic conceptual framework for all accounting.

Q16-4  The Securities and Exchange Commission has the legal authority to prescribe accounting method for firms whose shares of stock are sold to the investing public on the stock exchanges. Since its creation in 1934, the SEC has concentrated on protection of investors through the public disclosure of financial information in a fair and accurate manner. Although the SEC has left the task of issuing detailed accounting rules to the accounting profession, the SEC has kept a watchful eye on the private standard setting bodies and influences them where it deems necessary.

Q16-5  Generally accepted accounting principles (GAAP) are a set of standards that provide guidance for accountants. They arise from two broad sources (1) authoritative pronouncements issued by recognized standard setting bodies and (2) those principles that have gained acceptance through widespread use. Users of accounting information will be more effective decision makers if they understand the accounting standards that underlie the preparation of financial statements.
Q16-6 Three revenue recognition bases are point of sale, collection, and percentage of completion. With certain exceptions, GAAP require that revenue be recognized at the point of sale, which is when the goods are exchanged or the services performed. Under the collection method, the realization of revenue is deferred until the cash is collected. This may be applied using either the cost recovery basis or the installment basis. Under the cost recovery basis, gross margin is not recognized until the total cost is recovered. It is a very conservative method. Under the installment basis, each dollar collected is considered to be a proportionate return of the cost of the merchandise and a realization of the gross margin. The percentage of completion method recognizes a portion of the gross margin each accounting period in relation to the portion of the estimated total cost which has been incurred that period.

Q16-7 The three objectives of financial reporting, as stated by Statement of Financial Accounting Concepts No.1, are that financial reporting should provide (1) information useful in making investment and credit decisions; (2) information useful in judging the amounts, timing, and certainty of future cash flows, and (3) information about the resources of the business, the claims on the resources, and the changes in the resources during the current period. This information should be presented so that it is understandable to people who have a reasonable knowledge of business and economic activities.

Q16-8 The two primary decision-specific qualities of accounting information are relevance and reliability. Information is relevant if it (1) is timely, (2) helps users form predictions about the future, and (3) provides feedback about the results of decisions. Information is reliable if it: (1) is verifiable; (2) is neutral; and (3) has representational faithfulness. Representational faithfulness means that an accounting measure or description closely resembles what it represents.

Q16-9 The overall constraints on accounting information are that (1) the benefits of providing the information should be greater than the cost of gathering and reporting the information and (2) the information should be provided only if it is material—that is, it will have an impact on or change the decision of the user.

Q16-10 International accounting pronouncements are called International Financial Reporting Standards or IFRS. The organization that is responsible for their publications is the International Accounting Standards Committee. The Committee was formed in 1973.

Q16-11 Countries that have already adopted or begun adopting IFRS include: Russia, Australia, Japan, the EU (including Great Britain), Hong Kong, South Africa, and Singapore.

Q16-12 The major reason for considering changing price levels in financial reports is the many different levels of purchasing power represented by the numbers reported in the statements. Financial statements may not be an accurate financial picture during periods of changing price levels.
Illustrations of distortions in conventional financial statements are:

a. During inflation depreciation would be understated.
b. During inflation property, plant, and equipment would be understated.
c. During inflation the amounts for total revenues would not be comparable between years.

Note: Many others are possible.

The gross plant cost in conventional financing statements will be $7 million. This will probably not be a fair statement because of the adding of dollars of unequal purchasing power.

The amount of expense is measured by the cost of the asset consumed. Since depreciation measures the cost of consuming property, plant, and equipment, which is normally not new, the effects of inflation will be more pronounced because of the longer period of time. For many companies, fixed assets are purchased over a wide range of years.

Exchange gains and losses arise in import/export transactions due to changes in currency rates. These changes affect the value of receivables and payables.

A currency exchange rate represents the price of one currency stated in terms of another.

**SOLUTIONS TO EXERCISES**

**E16-18 Accounting Standards**

LG 1

a. Materiality. Omission of the immaterial assets from a balance sheet would not affect decisions of a user of the balance sheet or income statement.

b. Periodicity and Matching. The life of a firm consists of equal-length reporting periods. We make the adjustments so that statements for the period match revenues and expenses.

c. Consistency. Once we choose an acceptable accounting method, we should follow it in all future accounting periods so that statements covering different time periods are comparable.

d. Objective evidence. To the greatest extent possible, the amounts used in recording events are based on objective evidence. Two separate accountants, independently recording transactions from source documents, should arrive at the same results.
E16-19 Installment Basis

Cost percentage = \( \frac{245}{350} = 70\% \)

Gross margin percentage = \( \frac{105}{350} = 30\% \)

<table>
<thead>
<tr>
<th></th>
<th>Cost Recognized</th>
<th>Gross Margin Recognized</th>
</tr>
</thead>
<tbody>
<tr>
<td>January:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>$50 x 0.60</td>
<td>$30</td>
<td>$20</td>
</tr>
<tr>
<td>$50 x 0.40</td>
<td></td>
<td></td>
</tr>
<tr>
<td>February:</td>
<td>$42</td>
<td></td>
</tr>
<tr>
<td>$70 x 0.60</td>
<td></td>
<td></td>
</tr>
<tr>
<td>$70 x 0.40</td>
<td>$28</td>
<td></td>
</tr>
<tr>
<td>March:</td>
<td>$48</td>
<td></td>
</tr>
<tr>
<td>$80 x 0.60</td>
<td></td>
<td></td>
</tr>
<tr>
<td>$80 x 0.40</td>
<td>$32</td>
<td></td>
</tr>
</tbody>
</table>

E16-20 Percentage of Completion Method of Revenue Recognition

Contract price \( \$15,000,000 \)

Expected costs \( \$12,000,000 \)

Expected gross margin \( \$3,000,000 \)

Times percentage of completion \( \frac{\$7,500,000}{\$12,000,000} \) \( 62.5\% \)

Gross margin for 2011 \( \$3,000,000 \times 0.625 \) \( \$1,875,000 \)

E16-21 Impact of International Accounting Standards

Since a change to IFRS would require Overseas Company to drop their use of LIFO, they will experience an increase in net income as follows:

Change in inventory, January 1, 2011

<table>
<thead>
<tr>
<th></th>
<th>LIFO</th>
<th>FIFO</th>
</tr>
</thead>
<tbody>
<tr>
<td>$145,000</td>
<td>180,000</td>
<td></td>
</tr>
</tbody>
</table>

Increase in cost of goods sold \( \$35,000 \)

Change in inventory, December 31, 2011

<table>
<thead>
<tr>
<th></th>
<th>LIFO</th>
<th>FIFO</th>
</tr>
</thead>
<tbody>
<tr>
<td>$152,000</td>
<td>198,000</td>
<td></td>
</tr>
</tbody>
</table>

Decrease in cost of goods sold \( \$46,000 \)

Increase in net income \( \$11,000 \)
Brad Company determined its reported income of $700,000 using historical cost figures. On a current cost basis, cost of goods sold would have been $25,000 higher, since beginning inventory restated to current cost would have been the same as ending inventory. Also, depreciation expense on a historical cost basis was $300,000. If the company had used current cost, depreciation expense would have been $600,000 ($6,000,000 x .10). This would have reduced net income to $375,000.

**E16-23** Computing Foreign Currency Exchange Gains or Losses

**LG 5**

**GENERAL JOURNAL**

<table>
<thead>
<tr>
<th>Date</th>
<th>Account Description</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 10</td>
<td>Accounts Receivable</td>
<td>828,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sales</td>
<td></td>
<td>828,000</td>
</tr>
<tr>
<td></td>
<td>Sale for 920,000 Euros at a rate of $0.90 per mark.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31</td>
<td>Accounts Receivable</td>
<td></td>
<td>46,000</td>
</tr>
<tr>
<td></td>
<td>Foreign Currency Exchange Gain</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To record gain prior to closing books at rate of $0.95 per Euro.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td>Cash</td>
<td>782,000</td>
<td></td>
</tr>
<tr>
<td>Jan. 9</td>
<td>Foreign Currency Exchange Loss</td>
<td></td>
<td>92,000</td>
</tr>
<tr>
<td></td>
<td>Accounts Receivable</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To record collection of 920,000 marks at rate of $0.85 per Euro.</td>
<td></td>
<td>874,000</td>
</tr>
</tbody>
</table>

**E16-24** Foreign Currency Transactions

**LG 5**

1. The decline in the price of the yen represents a loss to Tolland Company. The receivable will be worth less in 60 days.
2. Sale date $20,000 = 2,500,000 yen
   Due date 2,500,000 yen = $17,500
   Loss = $20,000 - $17,500 = $2,500

**E16-25** Foreign Currency Transactions

**LG 5**

1. The decrease in the price of HK$ represents a loss to Bester. The payable will cost more to settle in sixty days.

16-5
2. Purchase date $10,000 = 83,333.33 HK$
   Due date 83,333.33 HK$ = $8,333.33
   Loss = $8,333.33 - $10,000 = $1,666.67

E16-26  Hedging Strategy
LG 6

The company president should enter into a contract to buy Euros at the current exchange rate to offset the loss due to the decline in value.

SOLUTIONS TO PROBLEMS

P16-27  Identifying GAAP
LG 1

a. Scott Sales follows the entity concept. Separate accounting records must be kept for each enterprise. The company and its president are separate entities.

b. Scott Sales is not following the periodicity concept. In order to assess the financial progress and position of a firm, she should allocate revenues and expenses to a period of time to determine net income for that period. The process is not perfect, but it is necessary to make decisions concerning the business enterprise.

c. Scott Sales is following the matching concept and conservatism. The estimate of bad debts results in an amount for Bad Debts Expense on the income statement, which is matched with revenues for the period. The provision of an estimated Allowance for Doubtful Accounts results in showing net accounts receivable on the balance sheet at their net realizable value.

d. Scott Sales is not following the concepts of revenue realization and objectivity. A verbal statement of intention to purchase merchandise does not provide the objective evidence necessary to recognize revenue.

e. Scott Sales is not following the concepts of conservatism, historical cost, and objectivity. Under GAAP, we value assets at historical cost, and do not recognize revenues until they are realized (which occurs when the assets are actually sold).

f. Scott Sales is incorrect in terms of matching on the income statement. In a period of inflation, FIFO matches old, low costs with current revenues and therefore tends to overstate reported net income. The company president is correct about inventory valuation on the balance sheet, since the FIFO inventory value will approximate the current value of the inventory.

g. Scott Sales is following the concept of materiality. The expenditure of less than $50 is not significant enough to influence a decision by a user of the accounting information.
P16-28  Identifying Violations of Generally Accepted Accounting Principles
LG 1

a. Materiality.
b. Revenue recognition, conservatism.
c. Matching.
d. Objectivity.
e. Entity, full disclosure.
f. Historical cost, conservatism, revenue realization.
g. Consistency, matching, full disclosure

P16-29  Evaluating Financial Statements to Conform to GAAP
LG 1

DENVER COMPANY
Income Statement
For the Year Ended December 31, 2011

Revenues
Sales $ 510,000

Expenses
Cost of goods sold $ 280,000
Selling expenses 40,000
General and administrative expenses 50,000
Research and development expense 50,000
Depreciation expense 25,000
Total expenses 445,000
Net income $ 65,000

DENVER COMPANY
Statement of Owners' Equity
For the Year Ended December 31, 2011

Common stock, January 1, 2011 $ 0
Additional investments by owners
Common stock, December 31, 2011 200,000 $ 200,000

Retained earnings, January 1, 2011 $ -0-
Add: net income 65,000
Deduct: dividends (10,000)
Retained earnings, December 31, 2011 55,000
Owners' equity, December 31, 2011 $ 255,000
DENVER COMPANY
Balance Sheet
December 31, 2011

Assets

Current assets
Cash $ 115,000
Merchandise inventory 160,000
Total current assets $ 275,000

Property, plant, and equipment
Delivery trucks $ 100,000
Deduct: Accumulated depreciation 25,000
Total property, plant, and equipment 75,000

Total assets $ 350,000

Liabilities

Current liabilities:
Accounts payable $ 25,000
Expenses payable 20,000
Total current liabilities $ 45,000

Long-term liabilities:
Notes payable, due 2013 50,000
Total liabilities $ 95,000

Owners’ Equity

Common stock 200,000
Retained earnings 55,000
Total liabilities and owners’ equity $ 350,000

Selected notes to financial statements:

1. The company determines the inventory cost by the last-in, first-out (LIFO) method. Prior to January 1, 2011, it used the first-in, first-out (FIFO) method. (Instructor note: Point out that the change to average cost in 2012 would violate the consistency principle.)

2. The company values the delivery equipment at cost less accumulated depreciation computed by the straight-line method using an estimated useful life of four years.

3. The company expenses research and development expenditures in the year incurred.

4. Customers have placed sales orders totaling $150,000 in December 2011. Delivery is planned for February 2012. (Instructor note: This is an optional disclosure. Frequently, information on sales back orders is placed in the letter to stockholders or/in the description of segments of the company.)
1. IFRS permits revaluation of assets and GAAP does not. In a period of rising prices, revaluation of assets would increase total assets on the balance sheet and increase owners' equity. The revaluation would increase the cost amount of the asset thus increasing the depreciation expense and accumulated depreciation. The increase in depreciation expense would decrease net income and owner's equity. The increase in accumulated depreciation would decrease total assets. This latter change would be spread over the useful life of the asset.

2. IFRS does not permit the reporting of extraordinary items on the income statement while GAAP requires the segregation of extraordinary items. An extraordinary item is an item of gain or loss that is unusual in the nature of the business and infrequent in occurrence. This change would not change the net income, but it would change the categorization of a potentially significant amount on the income statement. This would have the potential of a significant change in operating income.

3. IFRS does not permit the use of LIFO for inventory valuation whereas GAAP does. During a period of rising prices, changing from LIFO to another inventory method such as FIFO would decrease cost of goods sold on the income statement and increase net income. On the balance sheet, the current asset inventory would increase. The higher net income would increase owners’ equity.

P16-31 Calculate the Impact on Income Statement and Balance Sheet by a Change from GAAP to IFRS

Change in inventory method from LIFO to FIFO
  Change in inventory, January 1, 2011
  LIFO $ 80,000
  FIFO 100,000
    Increase in cost of goods sold $20,000
  Change in inventory, December 31, 2011
  LIFO $ 70,000
  FIFO 92,000
    Decrease in cost of goods sold 18,000
    Increase in cost of goods sold $2,000

The inventory method change would cause a decrease in net income on the income statement and an increase in total assets and owners’ equity on the balance sheet.

Revaluation of factory equipment

Increasing the valuation of factory equipment from $140,000 to $180,000 would cause an increase in total assets and owners’ equity on the balance sheet by $40,000.
Increasing the valuation of factory equipment from $140,000 to $180,000 would also cause an increase in depreciation.

Depreciation under GAAP

\[
\frac{($140,000 - $0)}{10} = $14,000 \text{ per year.}
\]

Depreciation under IFRS

\[
\frac{($180,000 - $0)}{10} = $18,000 \text{ per year.}
\]

The revaluation of factory equipment would increase depreciation expense on the income statement decreasing net income by $4,000 each year for 10 years. This would in turn decrease net income and owners’ equity. It would also increase accumulated depreciation by $4,000 a year each year for 10 years, which would decrease total assets. This change would be spread over the useful life of the asset.

P16-32 Interpreting Information for Starbucks Corporation
LG 4

Requirement 1.

LIFO helps protect Starbucks against the effects of inflation in a period of rising prices by matching against the current period’s revenues (which are stated in current dollars) the most recent cost of merchandise acquired for sale. Therefore, sales stated in current dollars are matched against costs of merchandise stated in approximately current dollars.

Requirement 2.

LIFO does not benefit Starbucks in its attempt to report the effects of inflation on inventories on the balance sheet. Since LIFO states the inventories at the oldest costs, the assets would be shown on the balance sheet at dollars of an older purchasing power and would not reflect the cost of replacing those assets. Also, LIFO would not benefit Starbucks in the case of a LIFO liquidation where older, lower costs would be matched against current revenues.

P16-33 Foreign Currency Transactions
LG 5

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<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 5</td>
<td>Accounts Receivable, Hamburg Company Sales</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To record sale, $0.75 = 1 euro.</td>
<td></td>
<td>15,000</td>
</tr>
<tr>
<td>9</td>
<td>Accounts Receivable, North Hampton Importers Sales</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To record sale, $1.20 = 1 pound.</td>
<td></td>
<td>5,000</td>
</tr>
</tbody>
</table>
15 Accounts Receivable, Mexico-American
   Sales
   To record sales, $0.08 = 1 peso.
   4,000

28 Cash
   Accounts Receivable, Hamburg
   Company
   Foreign Currency Exchange Gain
   To record collection, $0.80 = 1 euro.
   16,000
       15,000
       1,000

31 Foreign Currency Exchange Loss
   Accounts Receivable, Mexico-
   American
   To record decline in dollar to franc
   (50,000 pesos x $.07).
   500

31 Accounts Receivable, North Hampton
   Importers
   Foreign Currency Exchange Gain
   To record increase in dollar to pound
   [$5,000 ÷ $1.20 = 4,166.67 pounds
   208
   4,166.67 x 1.25 = $5,208.33

P16-34 Foreign Currency Transactions
LG 5

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2011
Dec. 8 Accounts Receivable, Banhoff Bakers
   Sales
   To record sale, $0.80 = 1 euro
   (5,000 bushels x 5 euros = 25,000 euros
   x $.80 = $20,000).
   20,000

12 Accounts Receivable, Tokyo Exchange
   Sales
   To record sale, $.0075 = 1 yen
   (10,000 bushels x 350 yen
   = 3,500,000 yen x .0075 = $26,250).
   26,250

20 Accounts Receivable, Pastries of Montreal
   Sales
   To record sales, $0.9 = $1 Canadian
   (2,000 bushels x $2.50 = $5,000 Canadian
   x $.9 = $4,500).
   4,500
29  Cash (3,500,000 x .0070)  24,500
    Foreign Currency Exchange Loss  1,750
    Accounts Receivable, Tokyo Exchange  26,250
    To record collection, $1 = 135 yen.

31  Foreign Currency Exchange Loss  1,250
    Accounts Receivable, Banhoff Bakers  1,250
    To record decline in dollar to euro
    ((25,000 euros x $.75) – $20,000).

31  Accounts Receivable, Pastries of Montreal
    Foreign Currency Exchange Gain  250  250
    To record increase in dollar to Canadian dollar
    (($5,000 Canadian x $0.95) – $4,500).

SOLUTION TO PRACTICE CASE

Preparing Corrected Financial Statements
LG 1

Requirement 1.

CYCLE COMPANY
Income Statement
For the Year Ended December 31, 2011

Revenues
  Sales  $ 800,000

Expenses
  Cost of goods sold  $ 560,000
  Selling expenses  90,000
  General and administrative expenses  44,000
  Patent amortization expense  10,000
  Depreciation expense  19,000
  Total expenses  $ 723,000

Net income  $ 77,000
Practice Case (continued)

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the company at December 31, 2011, and the results of operations for 2011, in conformity with generally accepted accounting principles.

January 30, 2012

Avery & Avery

**SOLUTION TO BUSINESS DECISION AND COMMUNICATION PROBLEM**

**Are dividends in order?**

**LG 4**

Following is a typical student response to this communications problem, actual responses may vary in content and style but should contain as much of this basic information as possible.

To: President
From: Student name
Subject: Dividend Plan

This memo is a response to your proposal to pay dividends of $300,000 from this year's profits of $360,000. It is true that such an action would appear to leave $60,000 in the company for growth. However, the amounts the company reports on the income statement are based on historical cost and do not take into consideration the effects of inflation.

If we adjusted the income statement for the effects of changes in purchasing power, many of the amounts would be higher than those on the historical cost or traditional income statement. Since we determine expenses by measuring the cost of the asset consumed, the change in the amount of the expense due to inflation will be greater the older the asset. Thus, expenses that consume cash will have a very small change when adjusted for inflation. Yet expenses that result from the use of property, plant, and equipment will have a much larger change.
Our company uses a large number of assets that were purchased in 2005 when the firm was founded. Thus, inflation would have caused the constant dollar amount for assets to be significantly increased. Because of this increase, the depreciation expense would also be significantly larger on a historical cost/constant dollar basis than it was on a historical cost basis. With an inflation rate of 6% from 2005 through 2010 and 4% in 2011, the depreciation expense adjusted for general inflation would be much higher on a price-level adjusted basis. Thus, our historical cost depreciation of $125,000 would be much higher.

Based upon this, you should re-consider paying dividends for 2011.

**SOLUTION TO ETHICAL DILEMMA**

The following is a typical response to this ethical issue. Actual responses may vary in content and style, but should contain as much of the basic information as possible.

To: Controller, Hextall Company  
From: Student Name  
Subject: Accounting for International Transactions

According to U.S. GAAP, we are required to convert the financial statements of our Canadian subsidiary to U.S. dollars. We are required to convert the assets and liabilities of the foreign subsidiary at the exchange rate on the balance sheet date. The owners' equity section is converted using historical rates. Stock is converted using the rate at the time in which the subsidiary was acquired. Retained earnings is converted using the average exchange over the reporting period.

Any change in currency exchange will give rise to a situation where the difference between assets and liabilities does not equal owners' equity. To reconcile this difference, we must report a foreign currency translation adjustment. This adjustment is the amount necessary to balance the assets and equities. In our case, a negative foreign currency translation adjustment will appear as part of owners' equity section on the balance sheet.

Purchasing futures contracts based on our expectations of future changes in the relative value of Canadian currency represents a separate transaction from the accounting described above. Therefore, we cannot “offset” such transactions to avoid reporting our foreign holdings on the balance sheets. Such reporting would be a violation of GAAP and can result in severe legal liability.
Income Statement Responses:

1. Total revenues in 2008 ($10,383,000,000) are higher than the total for 2006 ($7,786,900,000).

2. The percent increase in total revenues from 2006 to 2008 is:

   \[ 33.3\% = \frac{100 \times 2,596,100,000^{*}}{7,786,900,000} = \frac{10,383,000,000 - 7,786,900,000}{\text{Total revenues increased 33.3\% from 2006 to 2008.}} \]

3. The cost of goods sold percent increased from 40.8\% in 2006 to 44.7\% in 2008. The gross margin percent decreased from 59.2\% in 2006 to 55.3\% in 2008. This is an unfavorable trend.

4. The percentage of total operating expenses to total revenues increased from 47.7\% in 2006 to 50.4\% in 2008. This is unfavorable. The operating income percent decreased from 11.5\% in 2006 to 4.9\% in 2008. This is an unfavorable trend.

5. The percent of net income to total revenues decreased from 7.2\% in 2006 to 3.0\% in 2008. This is an unfavorable trend.

Balance Sheet Responses:

6. Total assets at September 28, 2008 ($5,672,600,000) are higher than the total at October 1, 2006 ($4,428,900,000).

7. The percent increase in total assets from October 1, 2006 to September 28, 2008 is:

   \[ 28.1\% = \frac{100 \times 1,243,700,000^{*}}{4,428,900,000} = \frac{5,672,600,000 - 4,428,900,000}{\text{Total revenues and total assets have increased over the three-year period.}} \]

8. The largest asset investment for the company is property and equipment. This item makes up 52.1\% of the company's assets at the end of the most recent year.

9. The percent increase in property and equipment between 2006 and 2008 is:

   \[ 29.2\% = \frac{100 \times 668,600,000^{*}}{2,287,800,000} = \frac{2,956,400,000 - 2,287,800,000}{\text{The percent increase in property and equipment between 2006 and 2008 is:}} \]
Property and equipment increased by 29.2% compared to an increase in total revenues of 33.3%. This is favorable. Property and equipment is increasing at a slower rate that total revenues.

10. On the balance sheet, refer to the common-size percent for total liabilities each year. The percent of liabilities has increased from 49.7% of total assets in 2006 to 56.1% in 2008. This is unfavorable.

**Integrative Income Statement and Balance Sheet**

11. This company is operating less efficiently in 2008 than in 2007. We conclude this by comparing the total asset turnover for the two years that were 1.93 times in 2007 and 1.88 times in 2008. Each dollar of investment in assets generated less revenue in 2008 than in 2007. This is unfavorable.

**Ratio Analysis Responses:**

12. The current ratio is higher in 2008 than in 2006.

13. The quick ratio is the same in 2008 and in 2006.

14. For the year ended September 28, 2008, the accounts receivable turnover ratio 1 is worse this year compared to the previous year. In 2008, the accounts receivable turnover ratio 1 is 21.17 times. This is a decrease from 25.77 times in 2007. This is unfavorable.

15. For the year ended September 28, 2008, the accounts receivable turnover ratio 2 (based on year-end receivables) is worse at 18.42 times compared to the 2008 accounts receivable turnover ratio 1 (based on average receivables) at 21.17 times.

16. For the year ended September 28, 2008, the inventory turnover ratio 1 is better this year compared to the previous year. In 2008, the inventory turnover ratio is 6.71 times. This is an increase from 3.56 times. This is favorable.

17. For the year ended September 28, 2008, the inventory turnover ratio 2 (based on year-end inventory) is the same at 6.71 times compared to the 2008 inventory turnover ratio 1 (based on average inventory) at 6.71 times.

18. The return on total assets (ROA) ratio is worse in 2008 than in 2007. In 2008, the ROA is 5.73%. This is a decrease from 13.76% in 2007. This is unfavorable.