

Accounting 402
Illustration of Error corrections
(APB #9, APB #20, FASB #16)
(Codification Section 250-10)

Partial income statement and retained earnings statement data was obtained from the records of McGraw, Inc. for 20X6 and 20X5:

	<u>20X6</u>	<u>20X5</u>
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Delivery expense	\$ 5,000	\$ 32,000
Depreciation expense	20,000	18,000
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	~~~~~	~~~~~
Income tax expense	12,000	14,000
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	~~~~~	~~~~~
Net income	<u>40,000</u>	<u>44,000</u>
Retained Earnings Statement:		
Retained earnings-beginning	\$ 114,000	\$ 70,000
Add: Net income	40,000	44,000
Retained earnings-ending	<u>\$ 154,000</u>	<u>\$ 114,000</u>

During 20X7, McGraw discovered that a delivery truck, purchased in 20X5, was erroneously charge to Delivery Expense. The truck cost \$25,000, had a 5 year life, and no salvage value. McGraw uses the straight-line depreciation method. McGraw's tax rate is 40%.

Discuss and illustrate the accounting and financial reporting implications of this situation for McGraw, Inc.

EFFECT OF ERROR--20X5	<u>Amount</u>	<u>Over/ Under</u>
Income statement:		
Delivery expense--		
Depreciation expense--		
Income tax expense--		
Net income--		
Balance sheet:		
Fixed assets		
Accumulated depreciation		
Net fixed assets--		
Income tax payable--		
Retained earnings--		

EFFECT OF ERROR--20X6	<u>Amount</u>	<u>Over/ Under</u>
Income statement:		
Delivery expense--		
Depreciation expense--		
Income tax expense--		
Net income--		
Balance sheet:		
Fixed assets		
Accumulated depreciation		
Net fixed assets--		
Income tax payable--		
Retained earnings--		

Journal entry to correct error [made during 20X7]

<u>Account</u>	<u>Debit</u>	<u>Credit</u>

FINANCIAL STATEMENT PRESENTATION-SINGLE PERIOD

Income statement:

20X7

Delivery expense

Depreciation expense

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Income tax expense

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Net income

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Retained earnings statement:

Beginning retained earnings-- as previously reported

Prior period adjustment-- error correction, net of applicable
income taxes of \$ _____

Beginning retained earnings- as restated

Add: Net income

Retained earnings-ending

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FINANCIAL STATEMENT PRESENTATION-Two year comparative statements

Income statement:

20X7

20X6

Delivery expense

Depreciation expense

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Income tax expense

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Net income

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Retained earnings statement:

Beginning retained earnings-- as previously reported

\$ 114,000

Prior period adjustment-- error correction, net of applicable income taxes of \$ _____

Beginning retained earnings- as restated

Add: Net income

Retained earnings-ending

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FINANCIAL STATEMENT PRESENTATION-Three year comparative statements

Income statement:

20X7

20X6

20X5

Delivery expense

Depreciation expense

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Income tax expense

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Net income

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Retained earnings statement:

Beginning retained earnings

Add: Net income

Retained earnings-ending

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