

Current Liabilities, Payroll & Long-Term Liabilities

Chapter 10

Learning Objective 1

Account for current liabilities of known amount

Current Liabilities of Known Amount

Accounts Payable

Short-Term Notes Payable

Sales Tax Payable

Copyright (c) 2009 Prentice Hall. All rights reserved.

3

Current Liabilities of Known Amount Continued

Current portion of Long-Term Notes Payable

Accrued Expenses

Unearned revenues

Copyright (c) 2009 Prentice Hall. All rights reserved.

4

Exercise 10-21

GENERAL JOURNAL				
DATE		DESCRIPTION	DEBIT	CREDIT
2011				
3	1	Equipment		
		Notes payable		
<i>Purchase equipment by signing a note payable</i>				
12	31	Interest expense		
		Interest payable		
<i>Accrued interest on note payable</i>				

Copyright (c) 2009 Prentice Hall. All rights reserved.

5

Exercise 10-21 (continued)

GENERAL JOURNAL				
DATE		DESCRIPTION	DEBIT	CREDIT
2012				
3	1	Interest payable		
		Interest expense		
		Notes payable		
		Cash		
<i>To record payment of note and interest</i>				

Copyright (c) 2009 Prentice Hall. All rights reserved.

6

Learning Objective 2

Account for current liabilities that must be estimated

Estimated Warranty Payable

- ▶ Companies guarantee products through warranty agreements
- ▶ Warranty expense is estimated in same period as sale of product

JOURNAL

Date	Accounts	Debit	Credit
	Warranty Expense	\$\$\$\$	
	Estimated Warranty Payable		\$\$\$\$

Copyright (c) 2009 Prentice Hall. All rights reserved.

8

Contingent Liabilities

- ▶ Potential liability
- ▶ Depends on a future event
- ▶ Accounting treatment depends on likelihood that the future event will create a liability

Copyright (c) 2009 Prentice Hall. All rights reserved.

9

Accounting for Contingent Liabilities

Likelihood of Loss	How to Report
Remote	?
Reasonably possible	?
Probable	?

Copyright (c) 2009 Prentice Hall. All rights reserved.

10

Learning Objective 3

Calculate payroll and payroll tax amounts

Payroll Terms

Salary	?
Wages	?
Commission	?
Bonus	?
Benefits	?

Copyright (c) 2009 Prentice Hall. All rights reserved.

12

Payroll Terms

- ▶ Straight time
- ▶ Overtime

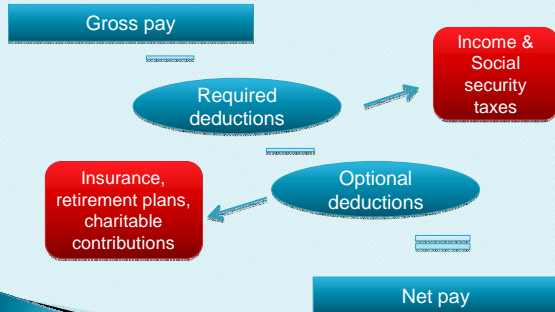
Gross pay

- Total amount earned during a pay period
- Expense to the employer

Net pay

- Take-home pay
- The amount the employee keeps

Payroll Withholding Deductions



Income Tax Withholdings

- ▶ Government requires employers to deduct income tax from employees' gross pay
- ▶ Amount depends on:
 - Gross pay
 - The number of *withholding allowances* employee claims on Form W-4

FICA Tax (Social Security)

- ▶ Two components:
 - Old age, survivors' and disability insurance (OASDI)
 - Health insurance (Medicare)

Employer Payroll Taxes

- ▶ In addition to employee withholdings, employers pay at least three taxes based on payroll:
 - Social Security (FICA) tax
 - State unemployment compensation tax (SUTA)
 - Federal unemployment compensation tax

Learning Objective 4

Journalize basic payroll transactions

Payroll Entries

Salaries
expense

Employee
benefits

Employer
Payroll
Taxes

Copyright (c) 2009 Prentice Hall. All rights reserved.

20

Salary Expense

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
	Salary expense		
	Employee income tax payable		
	FICA tax payable		
	Payable to health insurance		
	Payable to United Way		
	Salary payable		

Copyright (c) 2009 Prentice Hall. All rights reserved.

21

Benefits Expense

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
	Health insurance expense		
	Life insurance expense		
	Retirement plan expense		
	Employee benefits payable		

Copyright (c) 2009 Prentice Hall. All rights reserved.

22

Payroll Tax Expense

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
	Payroll tax expense		
	FICA tax payable		
	Federal unemployment tax payable		
	State unemployment tax payable		

Copyright (c) 2009 Prentice Hall. All rights reserved.

23

Exercise 10-25

Hours	Pay rate	Total
40	\$14	\$560
<u>22</u>	<u>\$21</u>	<u>462</u>
62		\$1,022

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
	Salary expense	1,022	
	Employee income tax payable		73
	FICA tax payable		78
	Payable to United Fund		10
	Salary payable		861

Copyright (c) 2009 Prentice Hall. All rights reserved.

24

Internal Control over Payroll

Controls for efficiency

- ▶ Use of two payroll bank accounts
- ▶ Use of computer processing

Controls to Safeguard Payroll Disbursements

- ▶ Hiring and firing separate from accounting
- ▶ Use of photo IDs & time clocks

Separation of Duties

Human Resources

- Hire & fire

Payroll

- Keep employee earnings records

Accounting

- Records payroll transactions

Treasurer

- Distributes paychecks

Learning Objective 5

Describe bonds payable

Bonds Payable

- ▶ Large company issue bonds to public to raise money
- ▶ Company pays interest (usually semi-annually) to bondholders

Bond Terms

Principal or Maturity value

- Amount borrower must pay back on maturity date

Maturity date

- Date on which borrower must pay principal to the bondholders

Stated interest rate

- Annual rate of interest borrower pays to bondholders

Types of Bonds

- ▶ Term bonds
- ▶ Serial bonds
- ▶ Secured bonds
- ▶ Debenture

Bond Pricing

Maturity(par) value

- \$1,000 bond issued for \$1,000
- No discount or premium

Discount

- \$1,000 bond issued for \$980
- Issued below maturity value

Premium

- \$1,000 bond issued for \$1,015
- Issued above maturity value

Copyright (c) 2009 Prentice Hall. All rights reserved.

31

Bond Prices

- ▶ Quoted as a percent of maturity value

A \$1,000 bond quoted a price of 101.5 would sell for \$1,015

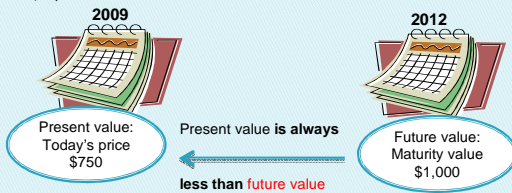
A \$1,000 bond quoted a price of 89.75 would sell for \$897.50

Copyright (c) 2009 Prentice Hall. All rights reserved.

32

Present Value

- ▶ Money earns income over time
- ▶ Investors will pay less than \$1,000 now to receive \$1,000 in the future



Copyright (c) 2009 Prentice Hall. All rights reserved.

33

Bond Interest Rates

Stated interest rate

Market interest rate

Stated interest rate	Market interest rate	Issue price of bonds payable
9%	= 9%	Maturity value
9%	< 10%	Discount (below maturity value)
9%	> 8%	Premium (above maturity value)

Copyright (c) 2009 Prentice Hall. All rights reserved.

34

Learning Objective 6

Measure interest expense on bonds using the straight-line amortization method

Accounting for Bonds Issued at Maturity Value

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
Issue date	Cash		
	Bonds payable		
	<i>To record issuance of 8% bonds at maturity value</i>		
Int. pmt dates	Interest expense		
	Cash		
	<i>To record semi-annual interest payment</i>		

Copyright (c) 2009 Prentice Hall. All rights reserved.

36

Accounting for Bonds Issued at Maturity Value (continued)

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
Maturity date	Bond payable		
	Cash		
	<i>To record payment of bonds at maturity</i>		

Copyright (c) 2009 Prentice Hall. All rights reserved.

37

Accounting for Bonds Issued at a Discount

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
Issue date	Cash		
	Discount on bonds payable		
	Bonds payable		
	<i>To record issuance of \$100,000, 10-year, 8% bonds at 98</i>		

Copyright (c) 2009 Prentice Hall. All rights reserved.

38

Carrying Value of Bonds Payable

Long-term liabilities

Bonds payable	\$100,000	
Less: Discount on bonds payable	<u>(\$2,000)</u>	\$98,000

Copyright (c) 2009 Prentice Hall. All rights reserved.

39

Accounting for Bonds Issued at a Discount

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
Int. pmt date	Interest expense	4,100	
	Discount on bonds payable		100
	Cash		4,000

Copyright (c) 2009 Prentice Hall. All rights reserved.

40

Accounting for Bonds Issued at a Premium

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
Issue date	Cash		
	Premium on bonds payable		
	Bonds payable		
	<i>To record issuance of \$100,000, 10-year, 8% bonds at 98</i>		

Copyright (c) 2009 Prentice Hall. All rights reserved.

41

Carrying Value of Bonds Payable

Long-term liabilities

Bonds payable	\$100,000	
Plus: Premium on bonds payable	<u>\$4,000</u>	\$104,000

Copyright (c) 2009 Prentice Hall. All rights reserved.

42

Accounting for Bonds Issued at a Premium

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
Int. pmt date	Interest expense		
	Premium on bonds payable		
	Cash		

Copyright (c) 2009 Prentice Hall. All rights reserved.

43

Carrying Value

<u>Bonds payable</u>	<u>Premium</u>
\$100,000	\$200 \$4,000

	\$3,800

Copyright (c) 2009 Prentice Hall. All rights reserved.

44

Adjusting Entries for Bonds Payable

- Interest payments seldom occur at year-end
 - Interest must be accrued

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
12 31	Interest expense		
	Discount on bonds payable		
	Interest payable		
	<i>(100,000 x 8% x 3/12)</i>		

Copyright (c) 2009 Prentice Hall. All rights reserved.

45

Adjusting Entries for Bonds Payable

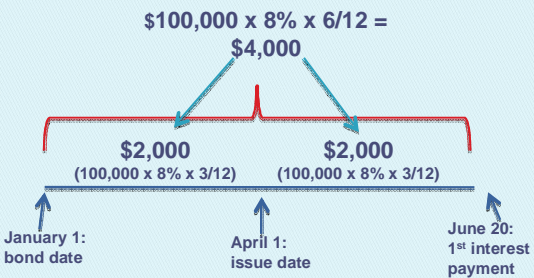
- The following interest payment entry will take into account the adjusting entry previously made

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
3 31	Interest payable		
	Interest expense		
	Discount on bonds payable		
	Cash		
	<i>(100,000 x 8% x 1/12)</i>		

Copyright (c) 2009 Prentice Hall. All rights reserved.

46

Issuing Bonds Between Interest Payment Dates



Copyright (c) 2009 Prentice Hall. All rights reserved.

47

Issuing Bonds Between Interest Payment Dates

GENERAL JOURNAL			
DATE	DESCRIPTION	DEBIT	CREDIT
4 1	Cash		
	Bonds payable		
	Interest payable		
6 30	Interest expense		
	Interest payable		
	Cash		

Copyright (c) 2009 Prentice Hall. All rights reserved.

48

Learning Objective 7

Report liabilities on the balance sheet

Any Company Classified Balance Sheet (partial) December 30, 2010	
Liabilities	
Current liabilities:	
Accounts payable	7,200
Salaries payable	1,500
Unearned revenue	400
FICA tax payable	100
Employee income tax payable	150
Interest payable	2,100
Current portion of long-term debt	5,000
Total current liabilities	16,450
Long-term liabilities:	
Note payable	50,000
Bonds payable, net of discount	98,200
Total long-term liabilities	148,200
Total liabilities	164,650

Copyright (c) 2009 Prentice Hall. All rights reserved.

50

Learning Objective 8

Compare issuing bonds to issuing stock

Bonds versus Stock

Issuing bonds

- ▶ Must pay interest and principal to bondholders
- ▶ Reduces net income
- ▶ Can increase earnings per share

Issuing stock

- ▶ Does not have to be "paid off"
- ▶ Does not affect net income
- ▶ Increases number of shares outstanding

Copyright (c) 2009 Prentice Hall. All rights reserved.

52

End of Chapter 10