

Module 4: ACC 2200 Intermediate Accounting Topics Pack

Introduction

Intermediate accounting builds on the concepts learned in introductory accounting courses.

Students begin to study more detailed accounting topics including:

- inventory valuation
- long-term assets
- depreciation methods
- liabilities
- bonds payable

These topics help accountants measure the financial position of a company more accurately.

Understanding how these accounts are recorded and reported is essential for solving accounting problems and preparing financial statements.

Inventory Concepts

Inventory represents goods that a company intends to sell to customers.

Inventory is classified as a current asset because it is expected to be sold within one operating cycle.

Companies must track:

- the cost of inventory purchased
- the cost of inventory sold
- the value of remaining inventory

Inventory Systems

There are two primary systems used to record inventory.

Perpetual Inventory System

A perpetual inventory system updates inventory records continuously.

Each purchase and sale of inventory is recorded immediately.

Advantages include:

- accurate inventory records at all times
- easier tracking of cost of goods sold
- better inventory control

Periodic Inventory System

A periodic inventory system updates inventory balances only at the end of the accounting period.

The company performs a physical inventory count and calculates cost of goods sold.

Formula used:

Beginning Inventory

- Purchases

= Cost of Goods Available for Sale

- Ending Inventory

= Cost of Goods Sold

Cost Flow Assumptions

Inventory valuation requires companies to assign costs to inventory sold and remaining inventory.

There are several cost flow methods.

FIFO (First-In, First-Out)

Under FIFO, the first units purchased are assumed to be sold first.

Characteristics:

- oldest inventory costs are assigned to cost of goods sold
- ending inventory reflects the most recent costs

FIFO typically results in:

- lower cost of goods sold
- higher gross profit during periods of rising prices

LIFO (Last-In, First-Out)

Under LIFO, the most recently purchased units are assumed to be sold first.

Characteristics:

- newest inventory costs are assigned to cost of goods sold
- older costs remain in ending inventory

LIFO typically results in:

- higher cost of goods sold
- lower net income during periods of rising prices

Weighted Average Method

The weighted average method calculates an average cost per unit.

Formula:

Average Cost per Unit

= Cost of Goods Available for Sale ÷ Total Units Available

This average cost is used to value both:

- cost of goods sold
- ending inventory

Example: Inventory Valuation

Beginning Inventory:
100 units at \$10 each

Purchase:
200 units at \$12 each

Total units available = 300 units

Total cost available =

$$\begin{aligned} &(100 \times 10) + (200 \times 12) \\ &= 1000 + 2400 \\ &= \$3400 \end{aligned}$$

Average cost per unit:

$$3400 \div 300 = \$11.33$$

Long-Term Assets

Long-term assets are assets used in operations for more than one year.

Examples include:

- equipment
- buildings
- vehicles
- machinery

These assets gradually lose value as they are used.

This reduction in value is called depreciation.

Depreciation

Depreciation allocates the cost of a long-term asset over its useful life.

Three commonly used depreciation methods include:

- straight-line method
- units-of-production method
- double-declining balance method

Straight-Line Depreciation

The straight-line method spreads the cost evenly over the useful life of the asset.

Formula:

Depreciation Expense
= (Cost - Salvage Value) ÷ Useful Life

Example

Equipment cost: \$20,000

Salvage value: \$2,000

Useful life: 6 years

Calculation:

$(20,000 - 2,000) \div 6$

= $18,000 \div 6$

= \$3,000 per year

Journal entry:

Debit: Depreciation Expense 3,000

Credit: Accumulated Depreciation 3,000

Units-of-Production Method

This method bases depreciation on actual usage of the asset.

Step 1: Calculate depreciation per unit

$(\text{Cost} - \text{Salvage Value}) \div \text{Total Units of Production}$

Step 2: Multiply by units produced during the period.

This method is commonly used for equipment whose usage varies.

Double-Declining Balance Method

This method accelerates depreciation.

More depreciation expense is recorded during the early years of an asset's life.

Step 1:

Double Declining Rate

= $2 \times (1 \div \text{Useful Life})$

Step 2:

Depreciation Expense

= Book Value × Double Declining Rate

Liabilities

Liabilities represent obligations that must be paid in the future.

Liabilities may be classified as:

- current liabilities
- long-term liabilities

Current Liabilities

Current liabilities are obligations expected to be paid within one year.

Examples include:

- accounts payable
- salaries payable
- interest payable
- short-term notes payable

Notes Payable

A note payable is a written promise to pay a specified amount at a future date.

Notes usually include interest.

Interest formula:

Interest = Principal × Rate × Time

Example: Recording a Note Payable

Company borrows \$5,000 cash.

Journal entry:

Debit: Cash 5,000

Credit: Notes Payable 5,000

Bonds Payable

Large companies often raise money by issuing bonds.

A bond represents a long-term borrowing agreement.

Investors purchase bonds and receive interest payments.

Bonds Issued at Par

If bonds are issued at face value, the entry is:

Debit: Cash

Credit: Bonds Payable

Bonds Issued at Discount

If bonds are sold below face value:

Debit: Cash

Debit: Discount on Bonds

Credit: Bonds Payable

Bonds Issued at Premium

If bonds are sold above face value:

Debit: Cash

Credit: Bonds Payable

Credit: Premium on Bonds

Common Student Errors

Students often experience difficulty with:

- selecting the correct inventory method
- calculating depreciation correctly
- confusing book value and asset cost
- misunderstanding bond discounts and premiums

To avoid these errors:

- clearly identify the accounting method being used
- follow each formula step by step
- check calculations carefully

Practice Problems

Problem 1

Beginning inventory = 50 units at \$8

Purchase = 150 units at \$10

Find the average cost per unit using the weighted average method.

Problem 2

Equipment cost = \$15,000

Salvage value = \$3,000

Useful life = 4 years

Calculate annual depreciation using the straight-line method.

Problem 3

A company borrows \$8,000 from a bank by signing a note payable.

Record the journal entry.

Problem 4

Define current liabilities.

Practice Problem Answers**Problem 1**

Cost available:

$$\begin{aligned} &(50 \times 8) + (150 \times 10) \\ &= 400 + 1500 \\ &= 1900 \end{aligned}$$

Units available:

$$200$$

Average cost:

$$1900 \div 200 = \$9.50 \text{ per unit}$$

Problem 2

$$\begin{aligned} &(15,000 - 3,000) \div 4 \\ &= 12,000 \div 4 \end{aligned}$$

$$\text{Annual depreciation} = \$3,000$$

Problem 3

Debit: Cash 8,000

Credit: Notes Payable 8,000

Problem 4

Current liabilities are obligations that must be paid within one year or one operating cycle.

Examples include accounts payable and salaries payable.