Problem 8

Mont Blanc Corporation is a small business operating in a state where a tax on income is contrary to the state's constitution. In an effort to raise revenue, the state has imposed a tax on business receipts for services provided to customers (total revenues, whether collected during the period or not). The tax is equal to 1% of revenues in excess of $300,000.

Mont Blanc prepared its state tax return by adding up the total deposits to the company's bank account during the year. Total deposits were $1,240,000, and the company paid taxes of $9,400 (($1,240,000 – $300,000) × 1%).

Assume you are an auditor for the state, and Mont Blanc has been randomly selected for a routine review. You immediately find that the company does not maintain a typical journal/ledger system, and is fundamentally clueless about proper accounting procedures.

You have discovered the following limited information as part of your examination:

Fact 1	Total deposits included $450,000 that resulted from issuing shares to stockholders.
Fact 2	The total deposits included $75,000 of interest income on investments.
Fact 3	The total deposits included $2,700 that was the result of a bank error. The bank subsequently discovered the error, and removed the funds from Moncrief's account.
Fact 4	Mont Blanc provides some services for cash, and portions of that money are never deposited to a bank. The company maintains a cash receipts book and you have determined that $74,100 was collected from customers but never deposited.
Fact 5	Bank deposits during the period included a $3,600 refund check from a vendor relating to an overpayment for supplies.
Fact 6	The company deposits included $42,000 that was the result of a refund of an overpayment of federal income taxes.
Fact 7	During the year, Mont Blanc collected a customer deposit toward a future contract. This $30,000 advance was deposited and subsequently refunded when both parties mutually agreed to cancel the contract.
Fact 8	Mont Blanc has many customers for which services are provided on account. As of the beginning of the year, the balance due from customers was $390,000. By the end of the year, accounts receivable had grown to $1,170,000. Mont Blanc has never experienced a problem with non-payment, and all customers pay their accounts in full within 90 days of a transaction.

a) Prepare an analysis to determine the correct amount of revenue for purposes of computing the tax.
b) Prepare journal entries for the "revenue" cycle, as well as the other cash items described.
c) Prepare a general ledger account supporting the revenue calculation.

Worksheet 8 (a)

a)

Gross receipts as reported	$	3,720,000
Fact 1: Remove stockholder investments		(450,000)
Fact 2:		
Fact 3:		
Fact 4:		
Fact 5:		
Fact 6:		
Fact 7:		
Fact 8:		
Fact 8:		
Corrected gross receipts		

b)

GENERAL JOURNAL			
Date	**Accounts**	**Debit**	**Credit**
Fact 1	Cash	450,000	
	Capital Stock		450,000
	Record stockholder investment		

Worksheet 8 (c)

REVENUES				
Date	**Description**	**Debit**	**Credit**	**Balance**
	Balance forward	-	-	-
		-	-	-
		-	-	-
		-	-	-

Solution 8 (a)

a) The following schedule reveals the corrected revenue calculations. Mont Blanc owes an additional \$2,508 in gross receipts tax ((\$3,970,800 – \$3,720,000) × 1%).

Gross receipts as reported	$	3,720,000
Fact 1: Remove stockholder investments		(450,000)
Fact 2: Remove interest income		(75,000)
Fact 3: Remove deposit error		(2,700)
Fact 4: Add cash revenues never deposited		74,100
Fact 5: Remove refund included in revenues		(3,600)
Fact 6: Remove tax refund deposit		(42,000)
Fact 7: Remove customer deposit refunded		(30,000)
Fact 8: Subtract collections of beginning receivables		(390,000)
Fact 8: Add services provided on account not yet collected		1,170,000
Corrected gross receipts	$	3,970,800

b)

GENERAL JOURNAL			
Date	**Accounts**	**Debit**	**Credit**
Fact 1	Cash	450,000	
	Capital Stock		450,000
	Record stockholder investment		
Fact 2	Cash	75,000	
	Interest Revenue		75,000
	Record interest earnings		
Fact 3	No entry		
	Bank error only		

Fact 4	Cash	74,100	
	Revenues		74,100
	Record service provided for cash		
Fact 5	Cash	36,000	
	Supplies Expense		36,000
	Reduce supplies for refund		
Fact 6	Cash	42,000	
	Tax Expense		42,000
	Reduce taxes for refund		
Fact 7	*No net adjustment needed*		
Fact 8	Cash	390,000	
	Accounts Receivable		390,000
	Record collection of receivables		
Fact 8	Accounts Receivable	1,170,000	
	Revenues		1,170,000
	Services provided on account		
Balance	Cash	2,726,700	
	Revenues		2,726,700
	All other revenues ($3,970,800 - $74,100 - $1,170,000 = $2,726,700)		

Solution 8 (c)

REVENUES				
Date	**Description**	**Debit**	**Credit**	**Balance**
	Balance forward	-	-	-
	Fact 4	-	74,100	74,100
	Fact 8	-	1,170,000	1,244,100
	Balance	-	2,726,700	3,970,800