Financial Accounting Week 12 Chapter 8- Current and Long-Term Liabilities

Hello everyone! This week the resource will be walking through Current and Long Term Liabilities! Additionally, I will be providing Accounting group tutoring sessions from 6:30-7:30pm on Tuesdays over Microsoft Teams each week. If you would like to attend those sessions or want to schedule a 1-on-1 appointment with one of our fantastic accounting tutors, please visit www.baylor.edu/tutoring to make an appointment! -Jerry

Current Long-Term Liabilities- Obligations due within one year or operating cycle

Two kinds:

- Estimated amounts (Think: Income taxes payable)
- Known amounts (Think: Accounts payable)

Long-Term Liabilities- Obligations that extend beyond one year or operating cycle

Short-Term Notes-

- Due within the year
- Used to buy assets or generate cash
- Need to accrue interest expense and interest payable at the end of the payable
- Interest rates are recorded at annual amounts and must be adjusted to the term of the notes

Example: Baylor purchases soccer equipment for $10,000 on a Short-Term note with a stated rate of 12% for a term of 5 months. Give the journal entry for the purchase of the equipment and the payment of the note.

JE for Purchase:

DR: Equipment $10,000

CR: Short-Term Note Payable $10,000

JE for Payment of Note Payable:

DR: Note Payable: $10,000

DR: Interest Exp: $500 (10000*12%* 5/12)

CR: Cash: $15,000

Sales Tax Payable:

- Levied on retail sales
- Collected from customers and remitted to state

Example: Home Depot store's daily sales totaled $200,000 and an additional 8% ($10,000) of sales tax (assume this is all in cash).

JE: DR: Cash: (200,000*1.08) $216,000

CR: Sales Revenue: $200,000

CR: Sales Tax Payable: (200,000*.08) 16,000

(Source: Pearson Education)

Accrued Liabilities:

Come from expenses incurred but not paid

JE:

DR: Accrued Expense

CR: Accrued Liability

Typical Categories:

- Salary and Wages Payable
- Interest Payable
- Income Taxes Payable

Unearned Revenues:

- Happens when a business receives cash before performing the service obligation
- Results in a liability
- Ex: Bob the Tomato paid Larry the Cucumber $12000 in to mow his lawn over the next 12 months. Record the journal entry for the sale and fulfillment of the obligation for the next month
- A:
- Payment
- DR: Cash $12000
- CR: Unearned Revenue: $120000
- First month:
- DR: Unearned Revenue $1000
- CR: Revenue $1000

Warranty Expenses:

1st: Record estimated Warranty Expense using the following journal entry

- DR: Warranty Expense (Estimated Expense)
- CR: Estimated Warrantly Liability

2nd: Record the actual amount of the expense using the following entry:

- DR: Accrued Warranties Payable

- CR: Inventory

This video provides a great example:

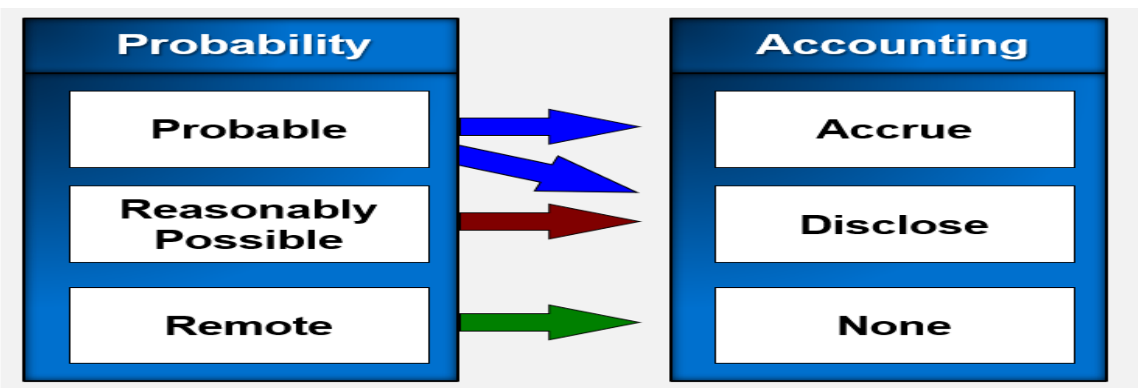
https://www.youtube.com/watch?v=DBIghRkyXIM&feature=youtu.be

Contingent Liabilities:

- A potential liability that depends on the future outcomes of past events
- Examples: Lawsuits, tax disputes, etc
- We record these base on the likelihood of the liability being realized
- If Probable, accrue (journalize) and disclose in the notes of the financial statements
- If reasonably possible, disclose in the financial statements
- If remotely probable, do nothing

This is illustrated by the following table:

(Source: Pearson Education)



Ways to Finance a Business:

- **Bonds (Debt):**

  Pros:

  1. Does not dilute control
  2. Typically higher EPS than issuing stock
  3. Interest Expense is tax deductible

  Cons:

  1. Risk

- **Issuing Stock:**

  Pros:

  1. Avoids liabilities and interest expenses

  Cons:

1. Dilutes EPS
2. Dilutes control of organization

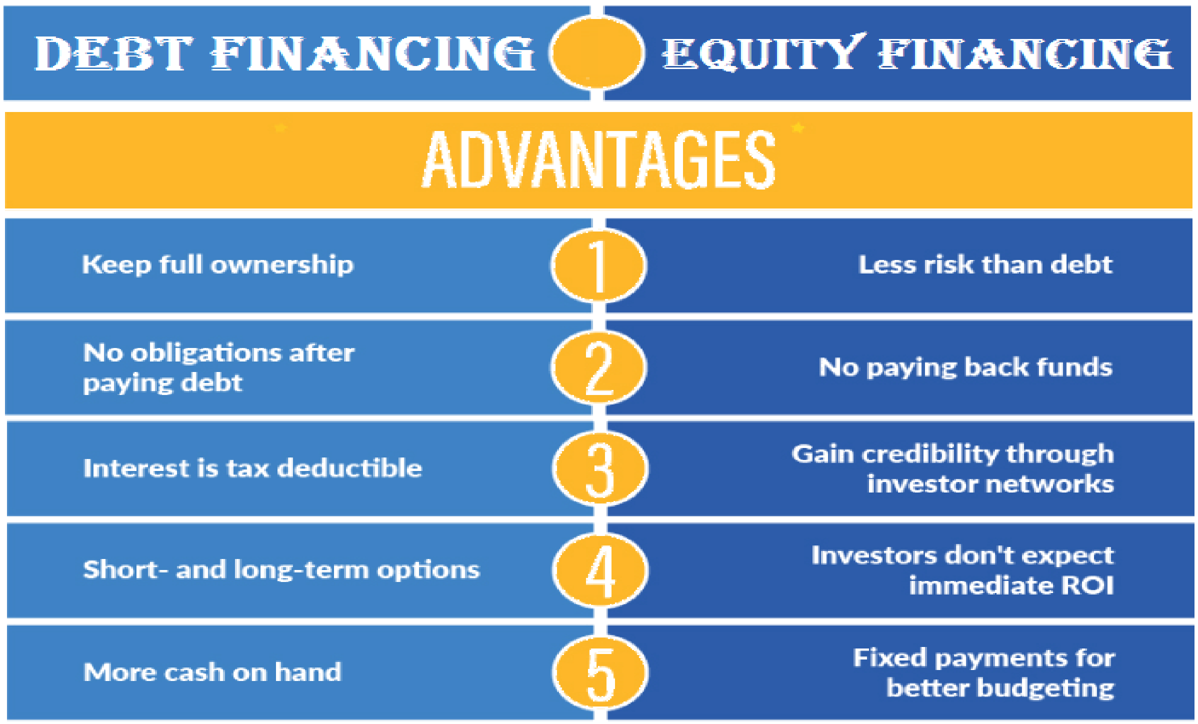
- **Retained Earnings:**

  Pros:

  1. Low risk

  Cons:

  1. Hard to raise large amounts of cash



(Source: Wikifinance)

Sources:

Pearson Education

Edspira

https://wikifinancepedia.com/finance/debt-financing-vs-equity-financing-advantages-disadvantages