Due June 11, 2004

15.511
Problem Set 1
Use of the Balance Sheet Equation to record transactions and for the preparation of financial statements

On July 1, 2000, TIM, Inc. started as a business entity. A summary of transactions through December 31, 2000 is presented below.

1. Stockholders invested $50,000 in cash in Bank Boston in the name of the business.
2. New computer equipment is purchased for $6,000 in cash. Equipment will be used for 3 years.
3. Office rent for half a year is paid in advance, $8,000.
4. Dividends of $500 paid to existing shareholders.
5. Paid $10,000 to employees for services provided.
7. Provided (and completed) design services on account to customers, $30,000.
8. Collected cash of $2,000 for services billed in 7.

Required:

a) Prepare a tabular analysis of the transactions using the Balance Sheet Equation (BSE) through December 31, 2000. Be sure to label your transactions.

b) Prepare the balance sheet as of December 31, 2000. From what part of the BSE table did you get the information to prepare the balance sheet?

c) Prepare the income statement for the period from July 1, 2000 through December 31, 2000. From what part of the BSE table did you get the information to prepare the income statement?

d) How much cash flowed in and out of TIM, Inc. in the period from July 1, 2000 through December 31, 2000? How much of this cash inflow or outflow do you consider relevant to TIM, Inc.’s operations?

e) Compare the net cash flow that is considered relevant to operations (from (d) above) and TIM, Inc.’s profits in the same period. What transactions and events account for the difference?

f) Which of the accounts you created in the BSE table are considered “temporary”, and which ones are considered “permanent”? Briefly explain the difference.