1. The Johnson Company bought a truck costing $24,000 two and a half years ago. The truck's estimated life was four years at the time of purchase. It was accounted for by using straight line depreciation with zero salvage value. The truck was sold yesterday for $19,000. What taxable gain must be reported on the sale of the truck?

**SOLUTION:** Yearly depreciation on the truck is

$24,000 / 4 = $6,000

and depreciation for 2.5 years is

$6,000 × 2.5 = $\_\_\_\_\_\_\_\_\_\_?

Therefore the truck's Net Book Value at the time of sale is

$24,000 − $\_\_\_\_\_\_\_\_\_\_? = $9,000

and the taxable gain is calculated as follows:

Sales price $\_\_\_\_\_

Cost \_\_\_\_\_

Gain $10,000

2. If the Johnson Company of Problem 1 is subject to a marginal tax rate of 34%, what is the cash flow associated with the sale of the used truck?

**SOLUTION:**

Johnson will pay tax on the $10,000 profit on the sale calculated in Problem 1 at 34%.

$10,000 × .\_\_\_\_\_\_\_ = $\_\_\_\_\_\_\_\_\_\_\_\_

(hint) Cash flow is the sale proceeds of $19,000 less the tax paid.

Note: The truck’s cost in the profit calculation in Problem 1 is its net book value on Johnson’s books. Although that figure is subtracted from the price received for the truck to calculate accounting profit, no cash was expended at the time of sale associated with that cost. Hence cash flow is just revenue minus tax.

5. McFadden Corp. reports the following balances on their December 31, 20X2 Balance Sheet:

($000)

Accounts Payable 60

Accounts Receivable 120

Accumulated Depreciation 350

Inventory 150

Fixed Assets (Net) 900

Long Term Debt 400

Paid in Excess 160

Retained Earnings 380

Total Assets 1,240

Total Liabilities 500 (long term debt + current liabilities)

All of the remaining accounts are listed below. Calculate the balance in each.

Answers are given below, explain how each was arrived at,

Accruals

Cash

Common Stock

Fixed Assets (Gross)

Total Current Assets

Total Current Liabilities

Total Equity

**SOLUTION:** Answers are given below, explain how each was arrived at,

Assets ($000) Liabilities & Equity ($000)

Cash $ 70 Account Payable $ 60

Accounts Receivable 120 Accruals 40

Inventory 150 Total Current Liabilities 100

Total Current Assets 340

Long Term Debt 400

Fixed Assets (Gross) 1,250

Accumulated Depreciation (350) Common Stock 200

Fixed Assets (Net) 900 Paid In Excess 160

Retained Earnings 380

Total Assets $1,240 Total Equity 740

Total Liabilities & Equity $1,240