

Due on June 15, 2003

15.511

Problem Set 2

Chemalite

The following questions refer to the *Chemalite, Inc* case in the course pack (Wilson, David A. "Chemalite, Inc." Boston, MA: Harvard Business School, 2003. Case No. 9-177-078). You should ignore the 5 questions at the end of the case and answer the following in their place.

1. Record the effects of Chemalite's 1991 events on a Balance Sheet Equation (BSE) worksheet, filling in appropriate account headings at the top. When you have completed the event analysis, compute the ending balances for each account. Alternatively, you may use journal entries and T-accounts to do the problem.

Note:

- (a) Label each event in the first column, using a "P" prefix for those transactions that occurred prior to Chemalite's start of operations (P1, P2, etc. for events during January 2, 1991 through June 30, 1991); a "T" prefix for those transactions that occurred on the last half of 1991 (T1, T2, etc.) and an "O" prefix for the other remaining events (O1, O2, etc...)
 - (b) For each event that affects Retained Earnings (RE), provide a brief description in the last column (i.e., Revenue, R&D expense).
 - (c) If an identified event does not affect the BSE, briefly (10 words or so) explain why
2. Several of the events you recorded in Question 1 required you to make one or more assumptions. Pick two such events and briefly (25 words or less for each) explain your rationale for the assumption(s) you made.
 3. Prepare year-end financial statements for Chemalite, Inc. - Balance Sheet, Income Statement, and Statement of Retained Earnings.
 4. Refer to the Cash account in column 1. Classify whether the transaction that affects cash is related to the firm's operations, investments, or financing activities. Prepare a report that lists transactions in these three categories and the corresponding amount of cash inflow or outflow (this report is called the direct statement of cash flows). How much of the total cash change is related to operations? How much is related to financing? How much is related to investments?
 5. Based on the information in 3) and 4), explain the apparent contradiction in Alexander's mind on why Chemalite's bank account fails to reflect his sense that the firm is "doing quite well".