

**SOLUTIONS****Learning Goal 3****Reinforcement Problems****LG 3-1.**

- a. Creditors and the owner(s). They provide property and services.
  - b. The creditors have provided resources to the business for which the business has not paid them. The owner also provided resources and has the legal right to claim the value of the assets, *except* for the amount needed to pay the creditors.
  - c. Because the owner's management efforts will cause the total business assets (wealth) to increase or decrease, and this changes the owner's claim.
  - d. Owner services do *not* have a fixed dollar value like wages. Owner services are an investment of time and effort. This value shows up as the increase or decrease in the wealth of the business, which changes the owner's claim. (However, this is different in a corporation, where an owner can also be an employee; see Learning Goal 5.)
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**LG 3-2.**

- a. Yes. \$800.
  - b. Yes. Initially \$500, and then the claim is reduced to \$400 after the payment is made.
  - c. Yes. The owner's claim increases by \$5,000.
  - d. The effect of the owner's services can only be measured by the change in the wealth of the business as a result of business operations. Owner's services are not wages—the owner is not an employee of himself—so the \$30 per hour is irrelevant.
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**LG 3-3.** “Owner's equity” is the owner's claim on the assets. It is secondary to the creditors' claim.

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**LG 3-4.** “Liabilities” are debts of the business. They have the first claim on assets. Some examples are wages owed to employees, debts to vendors, and unpaid bank loans.

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**LG 3-5.** While it is true that the creditors and the owner directly provide assets to a business, they also provide services. Both liability and owner's claims on the assets arise not only for the assets provided, but also for services provided. (The owner's good or bad management “services” indirectly change the owner's claim.)

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**LG 3-6.** No. “Priority” means: (A) all business debts must be paid when they are due, regardless of what the owner might want, and (B) when a business is terminated and liquidated, all existing debts have priority over the owner's claim on assets. The owner can withdraw assets at any time. However, debts still have to be paid in the manner stated above, and if the owner withdraws too much, he is legally obligated to reinvest enough money to make sure the debts are paid.

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**SOLUTIONS****Learning Goal 3, continued****LG 3-7.**

Description of Equity Characteristic	Creditors' Equity	Owner's Equity
a. It always has the first claim on assets.	✓	
b. It is increased by owner's hard work and risk-taking.		✓
c. It is usually called "liabilities."	✓	
d. It is known as a "residual" claim on assets.		✓
e. They are the debts of the business.	✓	
f. It is increased when the owner invests in his/her business.		✓
g. It is created when someone other than the owner provides assets or services to the business that are not immediately paid for.	✓	
h. Together they always add up to the total amount of assets.	✓	✓