

On November 1, 2005, Janet Morton and Kim Wong formed Pet Kingdom, Inc., to sell pets and pet supplies. Pertinent information regarding Pet Kingdom is summarized as follows:

- Pet Kingdom's business address is 1010 Northwest Parkway, Dallas, TX 75225; its telephone number is (214) 555-2211; and its e-mail address is petkingdom@pki.com.
- The employer identification number is 11-1111111, and the principal business activity code is 453910.
- Janet and Kim each own 50% of the common stock; Janet is president and Kim is vice president of the company. No other class of stock is authorized.
- Both Janet and Kim are full-time employees of Pet Kingdom. Janet's Social Security number is 123-45-6789, and Kim's Social Security number is 987-65-4321.

- Pet Kingdom is an accrual method, calendar year taxpayer. Inventories are determined using FIFO and the lower of cost or market method. Pet Kingdom uses the straight-line method of depreciation for book purposes and accelerated depreciation (MACRS) for tax purposes.
- During 2013, the corporation distributed cash dividends of \$250,000.

Pet Kingdom's financial statements for 2013 are shown below.

**Income Statement**

Income			
Gross sales			\$ 5,750,000
Sales returns and allowances			<u>(200,000)</u>
Net sales			\$ 5,550,000
Cost of goods sold			<u>(2,300,000)</u>
Gross profit			\$ 3,250,000
Dividends received from stock investments in less-than-20%-owned U.S. corporations			43,750
Interest income:			
State bonds	\$ 15,000		
Certificates of deposit	<u>20,000</u>		<u>35,000</u>
Total income			\$ 3,328,750
Expenses			
Salaries—officers			
Janet Morton	\$262,500		
Kim Wong	<u>262,500</u>	\$525,000	
Salaries—clerical and sales			725,000
Taxes (state, local, and payroll)			238,000
Repairs and maintenance			140,000
Interest expense:			
Loan to purchase state bonds	\$ 9,000		
Other business loans	<u>207,000</u>	216,000	
Advertising			58,000
Rental expense			109,000
Depreciation*			106,000
Charitable contributions			38,000
Employee benefit programs			60,000
Premiums on term life insurance policies on lives of Janet Morton and Kim Wong; Pet Kingdom is the designated beneficiary			<u>40,000</u>
Total expenses			<u>(2,255,000)</u>
Net income before taxes			\$ 1,073,750
Federal income tax			<u>(356,023)</u>
Net income per books			<u>\$ 717,727</u>

\* Depreciation for tax purposes is \$136,000. You are not provided enough detailed data to complete a Form 4562 (depreciation). If you solve this problem using H&R BLOCK Tax Software, enter the amount of depreciation on line 20 of Form 1120.

**Balance Sheet**

<b>Assets</b>	<b>January 1, 2013</b>	<b>December 31, 2013</b>
Cash	\$ 1,200,000	\$ 1,037,750
Trade notes and accounts receivable	2,062,500	2,147,000
Inventories	2,750,000	3,030,000
Stock investment	1,125,000	1,125,000
State bonds	375,000	375,000
Certificates of deposit	400,000	400,000
Prepaid Federal tax	-0-	3,977
Buildings and other depreciable assets	5,455,000	5,455,000
Accumulated depreciation	(606,000)	(712,000)
Land	812,500	812,500
Other assets	140,000	128,500
Total assets	<u>\$13,714,000</u>	<u>\$13,802,727</u>
<b>Liabilities and Equity</b>	<b>January 1, 2013</b>	<b>December 31, 2013</b>
Accounts payable	\$ 2,284,000	\$ 1,975,000
Other current liabilities	175,000	155,000
Mortgages	4,625,000	4,575,000
Capital stock	2,500,000	2,500,000
Retained earnings	4,130,000	4,597,727
Total liabilities and equity	<u>\$13,714,000</u>	<u>\$13,802,727</u>

During 2013, Pet Kingdom made estimated tax payments of \$90,000 each quarter to the IRS. Prepare a Form 1120 for Pet Kingdom for tax year 2013. Suggested software: H&R BLOCK Tax Software.