December Exam 2015 - Solutions

1. Which of the following is an ethical concern of accountants?
   a. Earnings manipulation.
   b. Conservative accounting.
   c. Industry practices.
   d. None of the above.

2. The underlying theme of the conceptual framework is
   a. decision usefulness.
   b. understandability.
   c. faithful representation.
   d. comparability.

3. Recognition of expense related to amortization of an intangible asset illustrates which principle of accounting?
   a. Expense recognition.
   b. Full disclosure.
   c. Revenue recognition.

4. Materiality is used in all of the following situations of providing financial information, **except**:
   a. where an amount is of relative large size and importance.
   b. where it would impact the judgment of a reasonable person.
   c. where it would not make a difference in the actions of decision maker.
   d. where omission of the information would result in bias.

5. Earnings per share relate to
   a. preference shares only.
   b. ordinary shares only.
   c. both preference and ordinary shares.
   d. neither preference nor ordinary shares.

6. Which of the following is included in comprehensive income?
   a. Investments by owners.
   b. Unrealized gains on non-trading equity securities.
   c. Distributions to owners.
   d. Changes in accounting principles.

7. Fulton Company owns the following investments:

Trading securities (fair value)	$70,000
Non-trading securities (fair value)	35,000
Held-for-collection securities (amortized cost)	47,000

   Fulton will report investments in its current assets section of

a. $0.
b. exactly $70,000.
c. $70,000 or an amount greater than $70,000, depending on the circumstances.
d. exactly $105,000.

8. Using IFRS, which of the following items is matched correctly with its basis of valuation for purposes of reporting on the statement of financial position?

	Item		Basis of Valuation
I.	Inventory	A.	Cost
II.	Prepaid expenses	B.	Estimated amount collectible
III.	Receivables	C.	Lower-of-cost-or net realizable value

a. I and A
b. II and C
c. III and B
d. II and B

9. Which of the following is a contra account?
a. Premium on bonds payable
b. Unearned service revenue
c. Patents
d. Accumulated depreciation

10. Steinert Company has the following items at year-end:

Cash in bank	$30,000
Petty cash	500
Commercial paper with maturity of 2 months	8,200
Postdated checks	2,100

Steinert should report cash and cash equivalents of
a. $30,000.
b. $30,500.
c. $38,700.
d. $40,800.

11. Net realizable value is
a. fair value plus estimated costs to complete and make a sale.
b. selling price.
c. selling price plus estimated costs to complete and make a sale.
d. selling price less estimated costs to complete and make a sale.

12. Oslo Corporation has two products in its ending inventory, each accounted for at the lower of cost or net realizable value. Specific data with respect to each product follows:

	Product #1	Product #2
Selling price	$60	$130
Historical cost	40	70
Cost to sell	10	26
Cost to complete	15	40

In pricing its ending inventory using the lower-of-cost-or-net realizable value, what unit values should Oslo use for products #1 and #2, respectively?

a. $35 and $64.
b. $50 and $104.
c. $40 and $70.
d. $45 and $90.

13. Cotton Hotel Corporation recently purchased Emporia Hotel and the land on which it is located with the plan to tear down the Emporia Hotel and build a new luxury hotel on the site. The cost of the Emporia Hotel should be

a. depreciated over the period from acquisition to the date the hotel is scheduled to be torn down.
b. written off as loss in the year the hotel is torn down.
c. capitalized as part of the cost of the land.
d. capitalized as part of the cost of the new hotel.

14. Assets that qualify for interest cost capitalization include

a. assets under construction for a company's own use.
b. assets that are ready for their intended use in the earnings of the company.
c. assets that are not currently being used because of excess capacity.
d. All of these assets qualify for interest cost capitalization.

15. An expenditure made in connection with a machine being used by a company should be

a. expensed immediately if it merely extends the useful life but does not improve the quality.
b. expensed immediately if it merely improves the quality but does not extend the useful life.
c. capitalized if it maintains the machine in normal operating condition.
d. capitalized if it increases the quantity of units produced by the machine.

16. Under IFRS, how is the account revaluation surplus reported?

a. As “other revenues and expenses” on the income statement.

b. As part of other comprehensive income which can be reported presented in separate statement, combined with income statement, or in changes in stockholders' equity statement.
c. It is included with Reserves in the stockholders' equity section of the Statement of Financial Position.
d. The account is not reported in the financial statements.

17. A patent should be amortized over
    a. twenty years.
    b. its useful life.
    c. its useful life or twenty years, whichever is longer.
    d. its useful life or twenty years, whichever is shorter.

18. On June 2, 2015, Olsen Inc. purchased a trademark with a cost €2,360,000. The trademark is classified as an indefinite-life intangible asset. At December 31, 2015 and December 31, 2016, the following is available for impairment testing:

	12/31/2015	12/31/2016
Fair value less costs to sell	€2,280,000	€2,265,000
Value-in-use	€2,340,000	€2,390,000

The 2016 income statement will report
    a. no Impairment Loss or Recovery of Impairment.
    b. Impairment Loss of €20,000.
    c. Recovery of Impairment of €20,000.
    d. Recovery of Impairment of €50,000.

19. Which of the following items is a current liability?
    a. Bonds (for which there is an adequate sinking fund properly classified as a long-term investment) due in three months.
    b. Bonds due in three years.
    c. Bonds (for which there is an adequate appropriation of retained earnings) due in eleven months.
    d. Bonds to be refunded when due in eight months, there being no doubt about the marketability of the refunding issue.

20. A contingent liability
    a. always exists as a liability but its amount and due date are indeterminable.
    b. is accrued even though not probable.
    c. is always the result of a loss contingency.
    d. is not reported as a liability if not probable.

21. Provisions are contingent liabilities which are accrued because the likelihood of an unfavorable outcome is
    a. virtually certain.
    b. greater than 50%.
    c. at least 75%.
    d. possible.

22. In January 2015, Finley Corporation, a newly formed company, issued 10,000 shares of its $10 par ordinary shares for $15 per share. On July 1, 2015, Finley Corporation reacquired 1,000 shares of its outstanding shares for $12 per share. The acquisition of these treasury shares
    a. decreased total shareholders' equity.
    b. increased total shareholders' equity.
    c. did not change total shareholders' equity.
    d. decreased the number of issued shares.

23. At December 31, 2016, Hancock Company had 500,000 ordinary shares issued and outstanding, 400,000 of which had been issued and outstanding throughout the year and 100,000 of which were issued on October 1, 2016. Net income for the year ended December 31, 2016, was $1,020,000. What should be Hancock's 2016 earnings per share, rounded to the nearest penny?
    a. $2.02
    b. $2.55
    c. $2.40
    d. $2.27

c $$\frac{\$1{,}020{,}000}{400{,}000 + \left(100{,}000 \times \frac{3}{12}\right)} = \$2.40.$$

24. On January 15, 2015, Bella Vista Company enters into a contract to build custom equipment for ABC Carpet Company. The contract specified a delivery date of March 1. The equipment was not delivered until March 31. The contract required full payment of $75,000 30 days after delivery. This contract should be
    a. recorded on January 15, 2015.
    b. recorded on March 1, 2015.
    c. recorded on March 31, 2015.
    d. recorded on April 30, 2015.

25. Consigned goods are recognized as revenues by the
    a. consignor when a sale to a third party has occurred.
    b. consignor when the merchandise has been shipped to a consignee.

c. consignee when a sale to a third party has occurred.

d. consignor when it receives payment from consignee for goods sold.

26. Green Construction Co. has consistently used the percentage-of-completion method of recognizing revenue. During 2015, Green entered into a fixed-price contract to construct an office building for $24,000,000. Information relating to the contract is as follows:

	At December 31	
	2015	2016
Percentage of completion	15%	45%
Estimated total cost at completion	$18,000,000	$19,200,000
Gross profit recognized (cumulative)	1,200,000	2,880,000

Contract costs incurred during 2016 were

a. $5,760,000.

b. $5,940,000.

c. $6,300,000.

d. $8,640,000.

b ($19,200,000 × 45%) – ($18,000,000 × 15%) = $5,940,000.

27. The primary difference between a direct-financing lease and a sales-type lease is the

a. manner in which rental receipts are recorded as rental income.

b. amount of the depreciation recorded each year by the lessor.

c. recognition of the manufacturer's or dealer's profit at the inception of the lease.

d. allocation of initial direct costs by the lessor to periods benefited by the lease arrangements.

28. Which of the following is not a basic assumption underlying the financial accounting structure?

a. Economic entity assumption.

b. Going concern assumption.

c. Periodicity assumption.

d. Historical cost assumption.

29. Which of the following does not describe intangible assets?

a. They lack physical existence.

b. They are monetary assets.

c. They provide long-term benefits.

d. They are classified as long-term assets.

30. Which of the following are reported at fair value?

a. Debt investments.
b. Equity investments.
c. Both debt and equity investments.
d. None of these answers choices are correct.

Classification of cash flows.

Note that X in the following statement of cash flows identifies a dollar amount and the letters (A) through (F) identify specific items which appear in the major sections of the statement prepared using the indirect method.

Statement of Cash Flows

Cash flows from operating activities				
Net income			X	
Adjustments to reconcile net income to net cash provided by operating activities:				
Add			+X	(A)
Deduct			–X	(B)
Net cash provided by operating activities			X	
Cash flows from investing activities				
Inflows	+X	(C)		
Outflows	–X	(D)		
Net cash provided (used) by investing activities			X	
Cash flows from financing activities				
Inflows	+X	(E)		
Outflows	–X	(F)		
Net cash provided (used) by financing activities			X	
Net increase (decrease) in cash			X	

Instructions

For each of the following items, indicate by letter in the blank spaces below, the section or sections where the effect would be reported. Use the code (A through F) from above. If the item is not required to be reported on the statement of cash flows, write the word "none" in the blank. Assume that accepted accounting standards have been followed in determining net income and that there are no short-term securities which are considered cash equivalents.

____ 1. Issued preference shares in exchange for equipment.

____ 2. Sales discounts lapsed and not taken by customers. (Sales recorded at net originally.)

____ 3. Accrued estimated income taxes for the period. These taxes will be paid next year.

____ 4. Amortization of premium on bonds payable.

____ 5. Premium amortized on investment in bonds.

____ 6. The book value of trading investments was reduced to fair value.

____ 7. Purchase of available-for-sale investments.

____ 8. Declaration of share dividends (not yet issued).

____ 9. Decrease in Retained Earnings Appropriated for Self-insurance.

____ 10. Bad debts (under allowance method) estimated and recorded for the period (receivables classified as current).

____ 11. Gain on disposal of old machinery.

____ 12. Payment of cash dividends (previously declared in a prior period).

____ 13. Trading investments are sold at a loss.

____ 14. Two-year notes issued at discount for a patent.

____ 15. Amortization of discount on notes receivable (long-term).

Solution 23-150

1. None	6. A	11. B
2. B	7. D	12. F
3. A	8. None	13. A and C
4. B	9. None	14. None
5. A	10. A	15. B

Valuation of Statement of Financial Position Items.

Use the code letters listed below (a – l) to indicate, for each statement of financial position item (1 – 13) listed below the usual valuation reported on the statement of financial position.

______ 1.	Share capital–ordinary	______ 7.	Long-term bonds payable
______ 2.	Prepaid expenses	______ 8.	Land (in use)
______ 3.	Property, plant, and equipment	______ 9.	Land (future plant site)
______ 4.	Accounts receivable	______ 10.	Patents

_____	5.	Copyrights	_____	11.	Trading securities
_____	6.	Inventory	_____	12.	Accounts payable

a. Par value
b. Current cost of replacement
c. Amount payable when due, less unamortized discount or plus unamortized premium
d. Amount payable when due
e. Fair value at statement of financial position date
f. Net realizable value
g. Lower-of-cost-or-net-realizable value
h. Original cost less accumulated amortization
i. Original cost less accumulated depletion
j. Original cost less accumulated depreciation
k. Historical cost
l. Unexpired or unconsumed cost

Solution 5-119

1.	a	5.	h	9.	k
2.	l	6.	g	10.	h
3.	j	7.	c	11.	e
4.	f	8.	k	12.	D

CASE (18 %)
On 1 April 20X8 Pillar acquired 90% of the equity shares in Steeple. Steeple's retained profits at the date of acquisition were $2,640,000.

Balance sheets as of March 20X9

	Pillar		*Steeple*	
	$'000	$'000	$'000	$'000
Non-current assets				
Property, plant and equipment	2,544		2,388	
Intangible – Software	-		2,520	
Investments – equity in Steeple	5,036		-	
- others	214		252	
		7,794		5,160
Current Assets				
Inventories	863		672	
Receivables	629		394	
Steeple current account	90		-	

Cash	24		-	
		1,606		1,066
		9,400		6,226
Capital and Reserves				
Equity shares of $1 each		2,400		1,800
Share premium	2,400		600	
Retained earnings	3,360	5,760	2,706	3,306
		8,160		5,106
Non-current liabilities				
Government grants		276		240
Current liabilities				
Trade payables	690		566	
Pillar current account	-		72	
Income taxes payable	274		210	
Operating overdraft	-		32	
		964		880
		9,400		6,226

1. The software of Steeple represents the depreciated cost of the development of an integrated business accounting package. It was completed at a capitalized cost of $2,880,000 and went on sale on 1 April 20X8. Steeple's directors are depreciating the software on straight-line basis over an eight-year life (i.e. $360,000 per annum). However, the directors of Pillar are of the opinion that a six-year life would be more appropriate as sales of business software rarely exceed this period.

2. At the date of acquisition Pillar sold an item of plant to Steeple for $240,000. This plant had cost Pillar $200,000. Steeple has charged depreciation of $24,000 on this plant since it was acquired.

3. The inventory of Pillar on 31 March 20X9 contains goods at a transfer price of $30,000 that were supplied by Steeple who had marked them up with a profit of 25% on cost.

4. On March 20X9 Steeple remitted to Pillar a cash payment of $18,000. This was not received by Pillar until early April.

Required:
Prepare the consolidated balance sheet of Pillar as at March 20X9

Pillar
Consolidated balance sheet at 31 March 20x9

	$000	*$000*
Assets		
Non-current assets		
Property, plant and equipment (W1)	4,896	
Software (W2)	2,400	
Goodwill (W4)	500	
Investments (214+252)	466	
		8,262
Current assets		
Inventories (W5)	1,529	
Trade receivables (629+394)	1,023	
Cash and bank (24+18 cash in transit)	42	
		2,594
		10,856
Equity and liabilities		
Capital and reserves		
Equity shares $1 each		2,400
Reserves		
Share premium	2,400	
Retained earnings (W6)	3,274	5,674
		8,074
Minority interest (W7)		494
		8,568
Non-current liabilities		
Government grants (276+240)		516
Current liabilities		
Trade payables (690+566)	1,256	
Operating overdraft	32	
Provision for income taxes (274+210)	484	
		1,772
		10,856

Workings

(W1) Property, plant and equipment

Consolidation adjustment

	Steeple's books	*Consolidated figures*	*Difference*
	$000	*$000*	*$000*
Cost	240	200	40
Depreciation for year (10% on cost)	(24)	(20)	(4)
NBV at 31 March 20x9	216	180	36

Balance sheet:	$000
Amounts per question (2,544+2,388)	4,932
Unrealised profit	(40)
Depreciation	4
	4,896

(W2) Software	*Steeple's books*	*Consolidated figures*	*Difference*
	$000	*$000*	*$000*
Capitalised amount	2,880	2,880	
	(360)	(480)	120 Additional depreciation
Carrying value 31 March 20x9	2,520	2,400	

(W3) Net assets in subsidiary

	At date of acquisition	*At balance sheet date*
	$000	*$000*
Share capital	1,800	1,800
Share premium	600	600
Retained earnings	2,640	2,706
	5,040	5,106

(W4) Goodwill	*$000*	*$000*
Cost of investment		5,036
Less: share of net assets acquired:		
90% x 5,040 (W3)		4,536
		500

(W5) Inventories	*$000*
Amounts per question (863+672)	1,535
Unrealised profit in inventories (30x25/125)	(6)
	1,529

(W6) Retained earnings	*$000*	*$000*
Pillar		3,360
Steeple		
At 31 March 20x9	2,706	
Additional depreciation: software	(120)	
Unrealised profit on plant	(36)	
Unrealised profit in inventories	(6)	
	2,544	
At acquisition	(2,640)	
	(96)	
Group share (90%)		(86)
		3,274

(W7) Minority interest	*$000*	*$000*
Share of net assets		
10%x(5,106 (W3) – 120 – 36 - 6)		494

(W8) Elimination of current account	*$000*
Steeple's with Pillar per question	90
Deduct cash in transit regarding this balance	(18)
Adjusted figure to cancel	72