Print this page

Exercises

(LO 1) **E10-1** **(Cost Elements and Asset Componentization)** The following assets have been recognized as items of property, plant, and equipment.

1. Head office boardroom table and executive chairs
2. A landfill site
3. Wooden pallets in a warehouse
4. Forklift vehicles in a manufacturing plant
5. Stand-alone training facility for pilot training, including a flight simulator and classrooms equipped with desks, whiteboards, and electronic instructional aids
6. Large passenger aircraft used in commercial flights
7. Medical office building
8. Computer equipment

Instructions

For each of the items listed:

(a) Identify what specific costs are likely to be included in the acquisition cost.

(b) Explain whether any components of this asset should be given separate recognition, and why.

(LO 2, 3) **E10-2** **(Purchase and Cost of Self-Constructed Assets)** Wen Corp. both purchases and constructs various pieces of equipment that it uses in its operations. The following items are for two different pieces of equipment and were recorded in random order during the calendar year 2011:

Purchase	
Cash paid for equipment, including sales tax of $8,000 and GST of $6,000	$114,000
Freight and insurance cost while in transit	2,000
Cost of moving equipment into place at factory	3,100
Wage cost for technicians to test equipment	4,000
Materials cost for testing	500
Insurance premium paid on the equipment during its first year of operation	1,500
Special plumbing fixtures required for new equipment	8,000
Repair cost on equipment incurred in first year of operations	1,300
Cash received from provincial government as incentive to purchase equipment	25,000

Construction	
Material and purchased parts (gross cost $200,000; failed to take 2% cash discount)	$200,000
Imputed interest on funds used during construction (equity/share financing)	14,000
Labour costs	190,000
Overhead costs (fixed $20,000; variable $30,000)	50,000
Profit on self-construction	30,000
Cost of installing equipment	4,400

Instructions

Calculate the total cost for each of these two pieces of equipment. If an item is not capitalized as an equipment cost, indicate how it should be reported.

(LO 2, 3, 9) **E10-3** **(Treatment of Various Costs)** Farrey Supply Ltd. is a newly formed public corporation that incurred the following expenditures related to land, buildings, machinery, and equipment:

Legal fees for title search		$ 520
Architect's fees		2,800
Cash paid for land and dilapidated building on it		112,000
Removal of old building	$20,000	
Less: Salvage	5,500	14,500
Surveying before construction		370
Interest on short-term loans during construction		7,400
Excavation before construction for basement		$ 19,000
Machinery purchased (subject to 2% cash discount, which was not taken)		65,000
Freight on machinery purchased		1,340
Storage charges on machinery, made necessary because building was still under construction when machinery was delivered		2,180
New building constructed (building construction took six months from date of purchase of land and old building)		485,000
Assessment by city for drainage project		1,600
Hauling charges for delivery of machinery from storage to new building		620
Installation of machinery		2,000
Trees, shrubs, and other landscaping after completion of building (permanent in nature)		5,400
Municipal grant to promote locating in the municipality		(8,000)

Instructions

(a) Determine the amounts that should be included in the cost of land, buildings, and machinery and equipment. Indicate how any amounts that are not included in these accounts should be recorded.

(b) Assume that the company was not a public company, and that it elected to use private entity GAAP. How would that affect the solution provided in part (a)?

(LO 2, 3) **E10-4** **(Entries for Asset Acquisition, Including Self-Construction)** The following are transactions related to Hood Limited:

(a) The City of Piedmont gives the company five hectares of land as a plant site. This land's market value is determined to be $81,000.

(b) Hood issues 13,000 no par value common shares in exchange for land and buildings. The property has been appraised at a fair market value of $990,000, of which $180,000 has been allocated to land, $567,000 to the structure of the buildings, $162,000 to the building services (wiring, plumbing, heating, air conditioning, elevators), and $81,000 to the interior coverings in the buildings (flooring, etc.). The Hood shares are not listed on any exchange, but a block of 100 shares was sold by a shareholder 12 months ago at $65 per share, and a block of 200 shares was sold by another shareholder 18 months ago at $58 per share.

(c) No entry has been made to remove amounts for machinery constructed during the year that were charged to the accounts Materials, Direct Labour, and Factory Overhead and should have been charged to plant asset accounts. The following information relates to the costs of the machinery that was constructed:

Construction materials used	$15,000
Direct materials used in calibrating the equipment	375
Factory supplies used	900
Direct labour incurred	34,000
Additional variable overhead (over regular) caused by construction of machinery, excluding factory supplies used	2,700
Fixed overhead rate applied to regular manufacturing operations	60% of direct labour cost
Cost of similar machinery if it had been purchased from outside suppliers	84,000

Instructions

Prepare journal entries on the books of Hood Limited to record these transactions. Assume that Hood Limited uses IFRS.

(LO 2, 4) **E10-5** **(Acquisition Costs of Equipment)** Lili Corporation acquires new equipment at a cost of $100,000 plus 8% provincial sales tax and 5% GST. (GST is a recoverable tax.) The company paid $1,700 to transport the equipment to its plant. The site where the equipment was to be placed was not yet ready and Lili Corporation spent another $500 for one month's storage costs. When installed, $300 of labour and $200 of materials were used to adjust and calibrate the machine to the company's exact specifications. The units produced in the trial runs were subsequently sold to employees for $400. During the first two months of production, the equipment was used only at 50% of its capacity. Labour costs of $3,000 and material costs of $2,000 were incurred in this production, while the units sold generated $5,500 of sales. Lili paid an engineering consulting firm $11,000 for its services in recommending the specific equipment to purchase and for help during the calibration phase. Borrowing costs of $1,100 were incurred because of the one-month delay in installation.

Instructions

Determine the capitalized cost of the equipment and explain why the remainder of the costs have not been capitalized.

(LO 2, 4) **E10-6** **(Directly Attributable Costs)** DAC Manufacturing Inc. is installing a new plant at its production facility. It has incurred these costs:

1. Cost of the manufacturing plant (cost per supplier's invoice plus taxes)	$2,500,000
2. Initial delivery and handling costs	200,000
3. Cost of site preparation	600,000
4. Consultants used for advice on the acquisition of the plant	700,000
5. Interest charges paid to supplier of plant for deferred credit	200,000
6. Estimated dismantling costs to be incurred after seven years	300,000
7. Operating losses before commercial production	400,000

Instructions

Advise DAC Manufacturing Inc. on the costs that can be capitalized in accordance with IAS 16.

(LO 2, 4) **E10-7** **(Acquisition Costs of Realty)** The following expenditures and receipts are related to land, land improvements, and buildings that were acquired for use in a business enterprise. The receipts are in parentheses.

(a) Money borrowed to pay a building contractor (signed a note), $(275,000)
(b) A payment for construction from note proceeds, $275,000
(c) The cost of landfill and clearing, $8,000
(d) Delinquent real estate taxes on property, assumed by a purchaser, $7,000
(e) A premium on a six-month insurance policy during construction, $6,000
(f) Refund of one month's insurance premium because construction was completed early, $(1,000)
(g) An architect's fee on a building, $22,000
(h) The cost of real estate purchased as a plant site (land $200,000; building $50,000), $250,000
(i) A commission fee paid to a real estate agency, $9,000
(j) The installation offences around a property, $4,000
(k) The cost of razing and removing a building, $11,000
(l) Proceeds from the salvage of a demolished building, $(5,000)
(m) Interest paid during construction on money borrowed for construction, $13,000
(n) The cost of parking lots and driveways, $19,000
(o) The cost of trees and shrubbery that were planted (non-permanent in nature, to be replaced every 20 years), $14,000
(p) Excavation costs for new building, $3,000
(q) The GST on an excavation cost, $150

Instructions

Identify each item by letter and list the items in columnar form, as shown below. Using the column headings that follow, write the letter for each item in the first column and its amount under the column heading where it would be recorded. All receipt amounts should be reported in parentheses. For any amounts that should be entered in the Other Accounts column, also indicate the account title.

Item	Land	Land Improvements	Building	Other Accounts

(LO 2, 4) **E10-8** **(Acquisition Costs of Realty)** Glesen Corp. purchased land with two old buildings on it as a factory site for $460,000. The property tax assessment on this property was $350,000: $250,000 for the land and the rest for the buildings. It took six months to tear down the old buildings and construct the factory.

The company paid $50,000 to raze the old buildings and sold salvaged lumber and brick for $6,300. Legal fees of $1,850 were paid for title investigation and drawing up the purchase contract. Payment to an engineering firm was made for a land survey, $2,200, and for drawing the factory plans, $82,000. The land survey had to be made before final plans could be drawn. The liability insurance premium that was paid during construction was $900. The contractor's charge for construction was $3,640,000. The company paid the contractor in two instalments: $1,200,000 at the end of three months and $2,440,000 upon completion. The architects and engineers estimated the cost of the building to be 55% attributable to the structure, 35% attributable to the building services (wiring, plumbing, heating, air conditioning), and the remainder attributable to the roof structure as each of these elements is expected to have a different useful life. Interest costs of $170,000 were incurred to finance the construction.

Instructions

Determine the land and building costs as they should be recorded on the books of Glesen Corp. Assume that the land survey was for the building.

(LO 2, 4) **E10-9** **(Natural Resource—Oil)** Oil Products Limited leases property on which oil has been discovered. The lease provides for an immediate payment of $550,000 to the lessor before drilling has begun and an annual rental of $42,000. In addition, the lessee is responsible for cleaning up the waste and debris from drilling and for the costs associated with reconditioning the land for farming when the wells are abandoned. It is estimated that the cleanup and reconditioning obligation has a present value of $31,000.

Instructions

Determine the amount that should be capitalized in the Oil Property asset account as a result of the lease agreement.

(LO 2, 3, 10) ***E10-10** **(Asset Acquisition)** Hayes Industries Corp. purchased the following assets and also constructed a building. All this was done during the current year.

Assets 1 and 2

These assets were purchased together for $100,000 cash. The following information was gathered:

Description	Initial Cost on Seller's Books	Depreciation to Date on Seller's Books	Book Value on Seller's Books	Appraised Value
Machinery	$100,000	$50,000	$50,000	$90,000
Office Equipment	60,000	10,000	50,000	30,000

Asset 3

This machine was acquired by making a $10,000 down payment and issuing a $30,000, two-year, zero-interest-bearing note. The note is to be paid off in two $15,000 instalments made at the end of the first and second years. It was estimated that the asset could have been purchased outright for $35,000.

Asset 4

A truck was acquired by trading in an older truck that has the same value in use. The newer truck has options that will make it more comfortable for the driver; however, the company remains in the same economic position after the exchange as before. Facts concerning the trade-in are as follows:

Cost of truck traded	$100,000
Accumulated depreciation to date of sale	40,000
Fair market value of truck traded	80,000
Cash received	10,000
Fair market value of truck acquired	70,000

Asset 5

Office equipment was acquired by issuing 100 no par value common shares. The shares had a market value of $11 per share.

Construction of Building

A building was constructed on land that was purchased last year at a cost of $150,000. Construction began on February 1 and was completed November 1. The payments to the contractor were as follows:

Date	Payment
Feb. 1	$120,000
June 1	360,000
Sept. 1	480,000
Nov. 1	100,000

To finance construction of the building, a $600,000, 12% construction loan was taken out on February 1. During the beginning of the project, Hayes invested the portion of the construction loan that was not yet expended and earned investment income of $4,600. The loan was repaid on November 1. The firm had $200,000 of other outstanding debt during the year at a borrowing rate of 8% and a $350,000 loan payable outstanding at a borrowing rate of 6%.

Instructions

Record the acquisition of each of these assets.

(LO 3) **E10-11 (Acquisition Costs of Trucks)** Jackson Corporation operates a retail computer store. To improve its delivery services to customers, the company purchased four new trucks on April 1, 2011. The terms of acquisition for each truck were as follows:

1. Truck #1 had a list price of $17,000 and was acquired for a cash payment of $15,900.
2. Truck #2 had a list price of $18,000 and was acquired for a down payment of $2,000 cash and a non-interest-bearing note with a face amount of $16,000. The note is due April 1, 2012. Jackson would normally have to pay interest at a rate of 10% for such a borrowing, and the dealership has an incremental borrowing rate of 8%.
3. Truck #3 had a list price of $18,000. It was acquired in exchange for a computer system that Jackson carries in inventory. The computer system cost $13,500 and is normally sold by Jackson for $17,100. Jackson uses a perpetual inventory system.
4. Truck #4 had a list price of $16,000. It was acquired in exchange for 1,000 common shares of Jackson Corporation. The common shares are no par value shares with a market value of $ 15 per share.

Instructions

Prepare the appropriate journal entries for Jackson Corporation for the above transactions. If there is some uncertainty about the amount, give reasons for your choice.

(LO 3) **E10-12 (Correction of Improper Cost Entries)** Plant acquisitions for selected companies are as follows:

1. Bella Industries Inc. acquired land, buildings, and equipment from a bankrupt company, Torres Co., for a lump-sum price of $700,000. At the time of purchase, Torres' assets had the following book and appraisal values:

	Book Value	Appraisal Value
Land	$200,000	$150,000
Buildings	250,000	350,000
Equipment	300,000	300,000

To be conservative, Bella Industries decided to take the lower of the two values for each asset it acquired. The following entry was made:

Land	150,000	
Buildings	250,000	
Equipment	300,000	
Cash		700,000

Bella Industries expects the building structure to last another 20 years; however, it expects that it will have to

replace the roof in the next five years. Torres Co. indicated that, on initial construction of the building, the roof amounted to 20% of the value of the building. In meetings with contractors, due to the unique design and materials required to replace the roof, the contractors stated that the roof structure is currently worth 15% of the value of the building purchase.

2. Hari Enterprises purchased store equipment by making a $2,000 cash down payment and signing a $23,000, one-year, 10% note payable. The purchase was recorded as follows:

Store Equipment	27,300	
Cash		2,000
Note Payable		23,000
Interest Payable		2,300

3. Kim Company purchased office equipment for $20,000, terms 2/10, n/30. Because the company intended to take the discount, it made no entry until it paid for the acquisition. The entry was:

Office Equipment	20,000	
Cash		19,600
Purchase Discounts		400

4. Kaiser Inc. recently received land at zero cost from the Village of Chester as an inducement to locate its business in the village. The appraised value of the land was $27,000. The company made no entry to record the land because it had no cost basis.

5. Zimmerman Company built a warehouse for $600,000. It could have contracted out and purchased the building for $740,000. The controller made the following entry:

Warehouse	740,000	
Cash		600,000
Profit on Construction		140,000

Instructions

Digging Deeper

(a) Prepare the entry that should have been made at the date of each acquisition. Round to the nearest dollar.

(b) Prepare the correcting entry that is required in each case to correct the accounts. In other words, do not simply reverse the incorrect entry and replace it with the entry in part (a).

(c) List the accounting principle, assumption, or constraint from the conceptual framework that has been violated in each case.

(LO 3) **E10-13** **(Entries for Equipment Acquisitions)** Geddes Engineering Corporation purchased conveyor equipment with a list price of $50,000. Three independent cases that are related to the equipment follow. Assume that the equipment purchases are recorded gross.

1. Geddes paid cash for the equipment 15 days after the purchase, along with 5% GST and provincial sales tax of $3,210. The vendor's credit terms were 1/10, n/30.
2. Geddes traded in equipment with a book value of $2,000 (initial cost $40,000), and paid $40,500 in cash one month after the purchase. The old equipment could have been sold for $8,000 at the date of trade, but was accepted for a trade-in allowance of $9,500 on the new equipment.
3. Geddes gave the vendor a $10,000 cash down payment and a 9% note payable with blended principal and interest payments of $20,000 each, due at the end of each of the next two years.

Instructions

Digging Deeper

(a) Prepare the general journal entries that are required to record the acquisition and payment in each of the three independent cases above. Round to the nearest dollar.

(b) Compare the treatment of the cash discount in item 1 above with the accounting for purchase discounts for inventories using the net method in Chapter 8.

(LO 3) **E10-14** **(Entries for Acquisition of Assets)** Information for Zoe Ltd. follows:

1. On July 6, Zoe acquired the plant assets of Desbury Company, which had discontinued operations. The property's appraised value was:

Land	$ 400,000
Building—Structure	1,000,000
Building—Services	200,000
Machinery and equipment	800,000
Total	$2,400,000

Zoe gave 12,500 of its no par value common shares in exchange. The shares had a market value of $168 per share on the date of the property purchase.

2. Zoe had the following cash expenses between July 6 and December 15, the date when it first occupied the building:

Repairs to building	$105,000
Construction of bases for machinery to be installed later	135,000
Driveways and parking lots	122,000
Remodelling of office space in building, including new partitions and walls	61,000
Special assessment by city on land	18,000

On December 20, Zoe purchased machinery for $260,000, subject to a 2% cash discount, and paid freight on the machinery of $10,500. The machine was dropped while being placed in position, which resulted in repairs costing $12,000. The company paid the supplier within the discount period.

Instructions

(a) Prepare the entries for these transactions on the books of Zoe Ltd.

(b) Prepare the entry for the purchase and payment of the machinery in item 2, assuming the discount was not taken.

(LO 3) **E10-15** **(Purchase of Equipment with Non-Interest-Bearing Debt)** Mohawk Inc. decided to purchase equipment from Central Ontario Industries on January 2, 2011, to expand its production capacity to meet customers' demand for its product. Mohawk issued an $800,000, five-year, non-interest-bearing note to Central Ontario for the new equipment when the prevailing market interest rate for obligations of this nature was 12%. The company will pay off the note in five $160,000 instalments due at the end of each year of the note's life.

Instructions

(Round to nearest dollar in all calculations.)

(a) Prepare the journal entry(ies) at the date of purchase.

(b) Prepare the journal entry(ies) at the end of the first year to record the payment and interest, assuming that the company uses the effective interest method.

(c) Prepare the journal entry(ies) at the end of the second year to record the payment and interest.

(d) Assuming that the equipment has a 10-year life and no residual value, prepare the journal entry that is needed to record depreciation in the first year. (The straight-line method is used.)

(LO 3) **E10-16** **(Purchase of Equipment with Debt)** On September 1, 2011, Reta Corporation purchased equipment for $30,000 by signing a two-year note payable with a face value of $30,000 due on September 1, 2013. The going rate of interest for this level of risk was 8%. The company has a December 31 year end.

Instructions

(a) Calculate the cost of the equipment assuming the note is as follows:

1. An 8% interest-bearing note, with interest due each September 1.
2. A 2% interest-bearing note, with interest due each September 1.
3. A non-interest-bearing note.

(b) Record all journal entries from September 1, 2011, to September 1, 2013, for the three notes in (a). Ignore depreciation of the equipment.

(CGA-Canada adapted)

(LO 3) **E10-17 (Asset Exchange, Monetary Transaction)** Cannondale Company purchased an electric wax melter on April 30, 2012, by trading in its old gas model and paying the balance in cash. The following data relate to the purchase:

List price of new melter	$15,800
Cash paid	10,000
Cost of old melter (five-year life, $700 residual value)	11,200
Accumulated depreciation on old melter (straight-line)	6,300
Second-hand market value of old melter	5,200

Instructions

Assuming that Cannondale's fiscal year ends on December 31 and depreciation has been recorded through December 31, 2011, prepare the journal entry(ies) that are necessary to record this exchange. Give reasons for the accounting treatment you used.

(LO 3) **E10-18 (Non-Monetary Exchange)** Starr Company Limited exchanged equipment that it uses in its manufacturing operations for similar equipment that is used in the operations of Ping Company Limited. Starr also paid Ping $1,500 in cash. The following information pertains to the exchange:

	Starr Co.	Ping Co.
Equipment (cost)	$31,000	$34,000
Accumulated depreciation	22,000	16,000
Fair value of equipment	15,500	17,000
Cash paid	1,500	

Instructions

Digging Deeper

(a) Prepare the journal entries to record the exchange on the books of both companies if the exchange is determined to have commercial substance.

(b) Repeat part (a), assuming the exchange is determined not to have commercial substance.

(c) List some of the factors that the accountant would need to consider in order to determine whether the transaction has commercial substance.

(LO 3) **E10-19 (Non-Monetary Exchanges)** Carver Inc. recently replaced a piece of automatic equipment at a net price of $4,000, f.o.b. factory. The replacement was necessary because one of Carver's employees had accidentally backed his truck into Carver's original equipment and made it inoperable. Because of the accident, the equipment had no resale value to anyone and had to be scrapped. Carver's insurance policy provided for a replacement of its equipment and paid the price of the new equipment directly to the new equipment manufacturer, minus the deductible amount paid to the manufacturer by Carver. The $4,000 that Carver paid was the amount of the deductible that it has to pay on any single claim on its insurance policy. The new equipment represents the same value in use to Carver. The used equipment had originally cost $65,000. It also had a book value of $45,000 at the time of the accident and a second-hand market value of $50,800 before the accident, based on recent transactions involving similar equipment. Freight and installation charges for the new equipment cost Carver an additional $1,100 cash.

Instructions

(a) Prepare the general journal entry to record the transaction to replace the equipment that was destroyed in the accident.

(b) Repeat part (a), but assume that the new equipment will result in significant savings to Carver since the new equipment is more efficient and requires less staff time to operate.

(LO 3) **E10-20 (Non-Monetary Exchanges)** Jamil Jonas is an accountant in public practice. Not long ago, Jamil struck a deal with his neighbour Ralph to prepare Ralph's business income tax and GST returns for 2011 in exchange for Ralph's services as a landscaper. Ralph provided labour and used his own equipment to perform landscaping services for Jamil's personal residence for which he would normally charge $500. Jamil would usually charge $650 for the number of hours spent completing Ralph's returns but considers the transaction well worth it since he really dislikes doing his own landscaping.

Instructions

How would each party record this transaction? Prepare the journal entries for both Jamil's and Ralph's companies.

(LO 3) **E10-21** **(Government Assistance)** Lightstone Equipment Ltd. wanted to expand into New Brunswick and was impressed by the provincial government's grant program for new industry. After being sure that it would qualify for the grant program, it purchased property in downtown Saint John on June 15, 2011. The property cost $235,000 and Lightstone spent the next two months gutting the building and reconstructing the two floors to meet the company's needs. The building has a useful life of 20 years and an estimated residual value of $65,000. In late August, the company moved into the building and began operations. Additional information follows:

1. The property was assessed at $195,000, with $145,000 allocated to the land.
2. Architectural drawings and engineering fees related to the construction cost $18,000.
3. The company paid $17,000 to the contractor for gutting the building and $108,400 for construction. Lightstone expects that these improvements will last for the remainder of the life of the building.
4. The provincial government contributed $75,000 toward the building costs.

Instructions

(a) Assuming that the company uses the cost reduction method to account for government assistance, answer the following:

1. What is the cost of the building on Lightstone Equipment's balance sheet at August 31, 2011, its fiscal year end?
2. What is the effect of this capital asset on the company's income statement for the company's year ended August 31, 2012?

(b) Assuming the company uses the deferral method to account for government assistance, answer the following:

1. What is the cost of the building on Lightstone Equipment's balance sheet at August 31, 2011?
2. What is the effect of this capital asset on the company's income statement for the company's year ended August 31, 2012?

Digging Deeper

(c) Compare the balance sheet and income statement presentations for the two alternative treatments for government assistance for the fiscal year ended August 31, 2012.

(LO 6) **E10-22** **(Measurement after Acquisition-Revaluation Model)** A partial balance sheet of Bluewater Ltd. on December 31, 2010, showed the following property, plant, and equipment assets after recording depreciation for that fiscal year:

Building—Structure	$300,000	
Less: accumulated depreciation	100,000	$200,000
Manufacturing equipment	$120,000	
Less: accumulated depreciation	40,000	80,000

The company has adopted the revaluation model for its building structure and equipment. Bluewater uses straight-line depreciation for its building structure (remaining useful life of 20 years, no residual value) and for its manufacturing equipment (remaining useful life of 8 years, no residual value). The use of the revaluation model has resulted in the recognition in prior periods of an asset revaluation surplus for the building structure of $14,000. Bluewater aggregates all of the assets accounted for under the revaluation model into one revaluation surplus account. On December 31, 2010, an independent appraiser assessed the fair value of the building structure to be $160,000 and that of the equipment to be $90,000.

Instructions

(a) Prepare the necessary general journal entry(ies), if any, to revalue the building and the manufacturing equipment as at December 31, 2010.

(b) Prepare the entries to record depreciation expense for the year ended December 31, 2011.

(LO 6) **E10-23** **(Measurement after Acquisition—Revaluation Model)** On January 1, 2011, ABC Company acquires a building at a cost of $100,000. The building is expected to have a 25-year life and no residual value. The asset is accounted for under the revaluation model and revaluations are carried out every three years. On December 31, 2013, the fair value of the building is appraised at $90,000, and on December 31, 2016, its fair value is $75,000.

Instructions

(Round to the nearest dollar in all calculations.)

(a) Prepare the entry(ies) required on December 31, 2011.

(b) Prepare the entry(ies) required on December 31, 2012.

(c) Prepare the entry(ies) required on December 31, 2013.

(d) Prepare the entry(ies) required on December 31, 2014.

(e) Prepare the entry(ies) required on December 31, 2016.

(LO 5, 7) **E10-24** **(Measurement after Acquisition—Fair Value Model versus Cost Model)** Plaza Holdings Inc., a listed company in Canada, ventured into construction of a mega shopping mall in Edmonton, which is rated as the largest shopping mall in North America. The company's board of directors, after much market research, decided that instead of selling the shopping mall to a local investor who had approached them several times during the construction period with excellent offers that he steadily increased during the year of construction, the company would hold this property for the purposes of capital appreciation and earning rental income from mall tenants. Plaza Holdings retained the services of a real estate company to find and attract many important retailers to rent space in the shopping mall, and within months of completion at the end of 2011, the shopping mall was fully occupied.

According to the company's accounting department, the total construction cost of the shopping mall was $50 million. The company used an independent appraiser to determine the mall's fair value annually. According to the appraisal, the fair values of the shopping mall at the end of 2011 and at each subsequent year end were:

2011	$50 million
2012	$60 million
2013	$63 million
2014	$58 million

The independent appraiser felt that the useful life of the shopping mall was 20 years and its residual value was $5 million.

Instructions

Describe the impact on the company's income statement and prepare the necessary journal entries for 2012, 2013, and 2014 if it decides to treat the shopping mall as an investment property under IAS 40:

(a) Using the fair value model.

(b) Using the cost model.

Note that the mall's rental income and expenses would be the same under both options, and thus can be omitted from the analysis for this exercise.

(LO 5, 7) **E10-25** **(Measurement after Acquisition—Fair Value Model)** Nevine Corporation owns and manages a small 10-store shopping centre and classifies the shopping centre as an investment property. Nevine has a May 31 year end and initially recognized the property at its acquisition cost of $10.8 million on June 2, 2010. The acquisition cost consisted of the purchase price of $10 million, costs to survey and transfer the property of $500,000 and legal fees for the acquisition of the property of $300,000. Nevine determines that approximately 25% of the shopping centre's value is attributable to the land, with the remainder attributable to the building. The following fair values are determined:

Date	Fair Value
May 31, 2011	$10,500,000
May 31, 2012	$10,400,000
May 31, 2013	$11,000,000

Nevine expects the shopping centre building to have a 35-year useful life and a residual value of $1.1 million. Nevine uses the straight-line method for depreciation.

Instructions

(a) Assume that Nevine decides to apply the cost model. What journal entries, if any, are required each year, and how will the investment property be reported on each year-end balance sheet?

(b) Assume that Nevine decides to apply the fair value model. Prepare the journal entries, if any, required at each year end. In addition, explain how the property would be reported if Nevine prepared a balance sheet shortly after acquisition in 2010.

(LO 8) **E10-26** **(Analysis of Subsequent Expenditures)** On January 1, 2011, the accounting records of Robinson Limited included a debit balance of $15 million in the building account and of $12 million in the related accumulated depreciation account. The building was purchased in January 1971 for $15 million, and was estimated to have a 50-year useful life with no residual value. Robinson uses the straight-line depreciation method for all its property, plant, and equipment. During 2011, the following expenditures relating to the building were made:

1. The original roof of the building was removed and replaced with a new roof. The old roof cost $1 million and the new roof cost $2.5 million. It is expected to have a 15-year useful life.
2. The ongoing frequent repairs on the building during the year cost $57,000.
3. The building's old heating system was replaced with a new one. The new heating system cost $700,000 and is estimated to have a seven-year useful life and no residual value. The cost of the old heating system is unknown.
4. A natural gas explosion caused $44,000 of damage to the building. This major repair did not change the estimated useful life of the building.

Instructions

Prepare the journal entries to record the expenditures related to the building during 2011.

(CGA-Canada adapted)

(LO 8) **E10-27** **(Analysis of Subsequent Expenditures)** The following transactions occurred during 2011. Assume that depreciation of 10% per year is charged on all machinery and 5% per year on buildings, on a straight-line basis, with no estimated residual value. Assume also that depreciation is charged for a full year on all fixed assets that are acquired during the year, and that no depreciation is charged on fixed assets that are disposed of during the year.

Jan. 30	A building that cost $132,000 in 1994 was torn down to make room for a new building structure. The wrecking contractor was paid $5,100 and was permitted to keep all materials salvaged.
Mar. 10	A new part costing $2,900 was purchased and added to a machine that was purchased in 2009 for $16,000. The new part replaced an original machine part, and resulted in a 25% increase in the efficiency of the equipment. The old part's cost was not separable from the original machine's cost.
Mar. 20	A gear broke on a machine that cost $9,000 in 2006, and the gear was replaced at a cost of $85. The replacement does not extend the machine's useful life.
May 18	A special base that was installed for a machine in 2005 when the machine was purchased had to be replaced at a cost of $5,500 because of defective workmanship on the original base. The cost of the machinery was $14,200 in 2005. The cost of the base was $3,500, and this amount was charged to the Machinery account in 2005.
June 23	One of the buildings was repainted at a cost of $6,900. It had not been painted since it was constructed in 2007.

Instructions

(a) Prepare general journal entries for the transactions. (Round to nearest dollar.)

(b) Assume that on March 20, the gear replacement extends the machine's useful life. How would your journal entry change?

(LO 8) **E10-28** **(Analysis of Subsequent Expenditures)** Plant assets often require expenditures subsequent to acquisition. It is important that they be accounted for properly. Any errors will affect both the balance sheets and income statements for several years.

Instructions

For each of the following items, indicate whether the expenditure should be capitalized (C) or expensed (E) in the period when it was incurred:

1. _____ A betterment
2. _____ Replacement of a minor broken part on a machine
3. _____ An expenditure that increases an existing asset's useful life
4. _____ An expenditure that increases the efficiency and effectiveness of a productive asset but does not increase its residual value
5. _____ An expenditure that increases the efficiency and effectiveness of a productive asset and its residual value
6. _____ An expenditure that increases a productive asset's output quality
7. _____ An overhaul to a machine that increases its fair market value and its production capacity by 30% without extending the machine's useful life
8. _____ Ordinary repairs
9. _____ A major overhaul
10. _____ Interest on borrowing that is necessary to finance a major overhaul of machinery that extends its life
11. _____ An expenditure that results in a 10%-per-year production cost saving
12. _____ Costs of a major overhaul that brings the asset's condition back to "new," with no change in the estimated useful life

(LO 2, 10) *E10-29 **(Capitalization of Borrowing Costs)** On December 31, 2010, Omega Inc. borrowed $3 million at 12% payable annually to finance the construction of a new building. In 2011, the company made the following expenditures related to this building structure (unless otherwise noted): March 1, $360,000; June 1, $600,000; July 1, $1.5 million (of which $400,000 was for the roof); December 1, $1.5 million (of which $700,000 was for the building services including wiring, heating, air conditioning, and plumbing). Additional information follows:

1. Other debt outstanding:

   $4-million, 10-year, 13% bond, dated December 31, 2004, with interest payable annually

   $1.6-million, six-year, 10% note, dated December 31, 2008, with interest payable annually

2. The March 1, 2011, expenditure included land costs of $150,000.
3. Interest revenue earned in 2011 on the unused idle construction loan amounted to $49,000.

Instructions

(a) Determine the interest amount that could be capitalized in 2011 in relation to the building construction.

(b) Prepare the journal entry to record the capitalization of borrowing costs and the recognition of interest expense, if any, at December 31, 2011.

(LO 2, 10) *E10-30 **(Capitalization of Borrowing Costs)** The following three situations involve the capitalization of borrowing costs.

1. **Situation 1**

   On January 1, 2011, Oksana Inc. signed a fixed-price contract to have Builder Associates construct a major head office facility at a cost of $4 million. It was estimated that it would take three years to complete the project. Also on January 1, 2011, to finance the construction cost, Oksana borrowed $4 million that is repayable in 10 annual instalments of $400,000, plus interest at the rate of 10%. During 2011, Oksana made deposit and progress payments totalling $1.5 million under the contract; and the weighted-average amount of accumulated expenditures was $800,000 for the year. The excess amount of borrowed funds was invested in short-term securities, from which Oksana realized investment income of $25,000.

2. **Situation 2**

   During 2011, Midori Ito Corporation constructed and manufactured certain assets and incurred the following interest cost in connection with these activities:

Borrowing Costs Incurred	
Warehouse constructed for Ito's own use	$30,000
Special-order machine for sale to unrelated customer, produced according to customer's specifications	9,000
Inventories routinely manufactured, produced on a repetitive basis	8,000

   All of these assets required an extended time period for completion.

3. Situation 3

Fleming, Inc. has a fiscal year ending April 30. On May 1, 2011, Fleming borrowed $10 million at 11% to finance construction of its own building. Repayments of the loan are to begin the month after the building's completion. During the year ended April 30, 2012, expenditures for the partially completed structure totalled $7 million. These expenditures were incurred evenly throughout the year. Interest that was earned on the part of the loan that was not expended amounted to $650,000 for the year.

Instructions

(a) For situation 1, what amount should Oksana report as capitalized borrowing costs at December 31, 2011?

(b) For situation 2, assuming the effect of interest capitalization is material, what is the total amount of borrowing costs to be capitalized?

(c) For situation 3, how much should be shown as capitalized interest on Fleming's financial statements at April 30, 2012? (CPA adapted)

(LO 2, 10) ***E10-31** **(Capitalization of Borrowing Costs)** In early February 2011, Huey Corp. began construction of an addition to its head office building that is expected to take 18 months to complete. The following 2011 expenditures relate to the addition:

Feb. 1	Payment #1 to contractor	$120,000
Mar. 1	Payment to architect	24,000
July 1	Payment #2 to contractor	60,000
Dec. 1	Payment #3 to contractor	180,000
Dec. 31	Asset carrying amount	$384,000

On February 1, Huey issued a $100,000 three-year note payable at a rate of 12% to finance most of the initial payment to the contractor. No other asset-specific debt was entered into. Details of other interest-bearing debt during the period are provided in the table below:

Other debt instruments outstanding—2011	Principal amount
7% 10-year bonds, issued June 15, 2005	$500,000
6% 12-year bonds, issued May 1, 2011	$300,000
9% 15-year bonds, issued May 1, 1996, matured May 1, 2011	$300,000

Huey's fiscal year end is December 31.

Instructions

What amount of interest should be capitalized according to IAS 23?