École de gestion TELFER School of Management

LIÉE au LINKED with LEADERSHIP

ADM3340A Fall 2013 **Student Name SOLUTIONS**

Quiz #1 **Student ID:** _____

[marked out of 50 for convenience: worth 5% of ADM3340's course mark]

Question 1 (19 marks)
Provide clear, concise answers for the following.

1. According to GAAP, what are intangible assets? (3 marks)

_____

_____

_____

_____

_____

_____

2. How are research costs accounted for? (1mark)

_____

_____

3. How are development costs accounted for under IFRS? (2 marks)

_____

_____

_____

4. What are the two models that are used to measure intangible assets after initial acquisition? Which of the models is/are permitted by IFRS? Which of the models is/are permitted by ASPE? (2 marks)

_____

_____

_____

_____

_____

5. What are the factors that should be considered when determining the useful life of limited life intangible assets? (4 marks)

_____

_____

_____

_____

_____

6. List five major categories of intangible assets? (5 marks)

_____

_____

_____

_____

_____

_____

7. What are the two models that are used to account for the impairment of intangible assets? Which is used by ASPE? Which is used by IFRS? (2 marks)

_____

_____

_____

_____

Solution

1. Intangible assets are assets that are:
   individually identifiable;
   have a non-physical existence; and
   are non-monetary in nature.

2. Research costs do not, by definition, meet the criteria for recognition as an asset. As a result, they must be recognized as expenses when they are incurred.

3. Development costs may be recognized as intangible assets,
   provided that future economic benefits can be demonstrated.
   that demonstration includes the satisfaction of six specific conditions.

4. The models are:
   the cost model; and
   the revaluation model. (which is applicable only if an active market exists for the intangible asset).
   the first is used for both ASPE and IFRS while the latter is used only in IFRS.

5. The factors to be considered are
   the expected use of the asset;
   legal or regulatory provisions;
   potential obsolescence; and
   the expected expenditures for its maintenance.

6. The major categories of intangible assets are:
   marketing-related;
   customer-related;
   artistic-related;
   contract-based; and
   technology-based.

7. The two models are:
   the cost recovery impairment model; and
   the rational entity impairment model.
   the first is used for ASPE and the latter is used in IFRS.

Question 2 (13 marks)
As the recently appointed auditor for Daleara Corporation, you have been asked to examine selected accounts before the six-month financial statements of June 30, 2014, are prepared. The controller for Daleara Corporation mentions that only one account is kept for intangible assets. The entries in Intangible Assets since January 1, 2014, are as follows:

INTANGIBLE ASSETS

			Debit	Credit	Balance
Jan.	4	Research costs	1,050,000		1,050,000
	5	Legal costs to obtain patent	45,000		1,095,000
	31	Payment of seven months' rent on Property leased by Daleara (February to August)	49,000		1,144,000
Feb.	11	Proceeds from issue of common shares		310,000	834,000
Mar.	31	Unamortized bond discount on a note payable issued on 31 March 2014 and due March 31, 2018	14,000		848,000
Apr.	30	Promotional expenses related to start-up of business	157,000		1,005,000
June	1	Development stage costs (meet all six development stage criteria)	215,000		1,220,000
	30	Operating losses for first six months	316,000		1,536,000

Required
Prepare the journal entry or entries that are necessary to correct this account. Assume that the patent has a useful life of 10 years.

SOLUTION
This is EXERCISE 12-5 from your textbook.

Research and Development Expense	1,050,000	
Intangible Assets - Development Costs.....	215,000	
Intangible Assets - Patents	45,000	
Rent Expense [(5 ÷ 7) X $49,000]	35,000	
Prepaid Rent [(2 ÷ 7) X $49,000].....	14,000	
Advertising Expense	157,000	
Income Summary	316,000	
Discount on Note Payable.....	13,125*	
Interest Expense	875	
Common Shares		310,000
Intangible Assets		1,536,000

* Assuming straight-line amortization:
($14,000 ÷ 48* months) X 3 = $875; $14,000 – $875 = $13,125

Amortization Expense	2,250	
Accumulated Amortization - Patents		2,250

[($45,000 ÷ 10) X 1/2]

* This assumes the note payable was issued on 30 March 2014: hence the 48 months for the straight-line amortization calculation.

Question 3 (18 marks)

On January 1, 2013 Billabong Limited issued a $10,000 note in exchange for professional services it received. The note bears a 4.00% annual rate of interest and will be repaid at the end of 2015. Billabong Limited has assessed this note and prevailing interest rates and has decided that it will use 6.00% when valuing the note.

Required

(1) Prepare Billabong Limited's journal entry to record the issuance of this note. (6 marks)
(2) Prepare Billabong Limited's amortization table for this note. (9 marks)
(3) Prepare Billabong Limited's journal entry on December 31, 2013 for this note. (3 marks)

Accounting for Note Payable using the amortized cost measurement model.

Face value of the note	$ 10,000
Number of years from issuance to the note's maturity date	3
Stated rate	4.00%
Market rate	6.00%
Yearly interest payment	$ 400
Present Value Interest Factor (PVIF) of interest annuity	2.673012
PVIF of maturity value	0.839619
PV of interest	$ 1,069.20
PV of maturity value	$ 8,396.19
PV of the expected cash outflows on the note	$ 9,465.40
Discount on the note payable	$ 534.60

You can enter data in the yellow-shaded cells only.

Date of issuance of the note	Dr	Cr
Professional services expense	$ 9,465.40	
Notes payable		$ 10,000.00
Discount on the note payable	$ 534.60	

	A	B	C	D	E = $10,000 x 4.00%	F = C x 6.00%	G = F - E	H = D - G	I = C+G
25		Year	Amortized cost [unamortized carrying amount] of the note at BOY**	Discount on the note payable at the BOY	Credit Cash a/c	Debit Interest expense a/c	Credit: Discount on the note payable a/c] [Amortization of discount on the note payable]	Discount on the note payable at the EOY**	Amortized cost [unamortized carrying amount] of the note at EOY
26		1	$ 9,465.40	$ 534.60	$ 400	$ 567.92	$ 167.92	$ 366.68	$ 9,633.32
27		2	$ 9,633.32	$ 366.68	$ 400	$ 578.00	$ 178.00	$ 188.68	$ 9,811.32
28		3	$ 9,811.32	$ 188.68	$ 400	$ 588.68	$ 188.68	$ 0.00	$ 10,000.00
66		TOTALS			$ 1,200.00	$ 1,734.60	$ 534.60		

67 ** BOY = beginning of the year; EOY = end of the year.

Financial Tables

Table 2: PRESENT VALUE of $1.00 that is received in the future.

Periods/Per	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	11%	12%
1	0.9900990	0.9803922	0.9708738	0.9615385	0.9523810	0.9433962	0.9345794	0.9259259	0.9174312	0.9090909	0.9009009	0.8928571
2	0.9802960	0.9611688	0.9425959	0.9245562	0.9070295	0.8899964	0.8734387	0.8573388	0.8416800	0.8264463	0.8116224	0.7971939
3	0.9705901	0.9423223	0.9151417	0.8889964	0.8638376	0.8396193	0.8162979	0.7938322	0.7721835	0.7513148	0.7311914	0.7117802
4	0.9609803	0.9238454	0.8884870	0.8548042	0.8227025	0.7920937	0.7628952	0.7350299	0.7084252	0.6830135	0.6587310	0.6355181
5	0.9514657	0.9057308	0.8626088	0.8219271	0.7835262	0.7472582	0.7129862	0.6805832	0.6499314	0.6209213	0.5934513	0.5674269
6	0.9420452	0.8879714	0.8374843	0.7903145	0.7462154	0.7049605	0.6663422	0.6301696	0.5962673	0.5644739	0.5346408	0.5066311

Table 4: PRESENT VALUE of Annuity of $1.00 in arrears.

Periods/Per	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	11%	12%
1	0.990099	0.980392	0.970874	0.961538	0.952381	0.943396	0.934579	0.925926	0.917431	0.909091	0.900901	0.892857
2	1.970395	1.941561	1.913470	1.886095	1.859410	1.833393	1.808018	1.783265	1.759111	1.735537	1.712523	1.690051
3	2.940985	2.883883	2.828611	2.775091	2.723248	2.673012	2.624316	2.577097	2.531295	2.486852	2.443715	2.401831
4	3.901966	3.807729	3.717098	3.629895	3.545951	3.465106	3.387211	3.312127	3.239720	3.169865	3.102446	3.037349
5	4.853431	4.713460	4.579707	4.451822	4.329477	4.212364	4.100197	3.992710	3.889651	3.790787	3.695897	3.604776
6	5.795476	5.601431	5.417191	5.242137	5.075692	4.917324	4.766540	4.622880	4.485919	4.355261	4.230538	4.111407