

BUSI 2001D – Intermediate Accounting 1
Winter 2013
Test 1 – February 8th, 2013, 6:30p.m.-8:00p.m.



Name: _____

Student #: _____

- 1) There are 45 marks available on this exam
- 2) This exam comprises of 5 questions and has 8 pages.
- 3) This is a closed note, closed book examination.
- 4) All answers should be entered in this booklet.
- 5) You may use a calculator during the examination
- 6) Show all your work and calculations.
- 7) **Good Luck!**

Question 1 (7 marks) (14 minutes)

HBH Appliance Shop has a balance of \$14,000 in its prepaid rent account on August 31, 2004. The company is in the process of preparing financial statements for the year ended August 31, 2005. Beginning July 1, 2005 HBH pays \$4,000 a month for the rent of its store. The terms of the lease require that rent be paid six months in advance on January 1 and July 1 of each year. Before July 1, 2005 HBH paid \$3,500 a month in rent. The prepaid rent at the beginning of the year represents 4 months of prepaid rent at the old location.

Required

Prepare all journal entries required in 2005 assuming that HBH initially records its prepaid costs as expenses and uses reversing entries.

Question 2 (3 marks) (6 minutes)

Quayle Company acquired machinery on January 1, 2000 for \$500,000 which it depreciated under the Diminishing Balance method at 20% with an estimated useful life of 10 years and no residual value. On January 1, 2003, Quayle decided to change to straight-line method of depreciation.

Required

Determine the cumulative effect of this accounting change on January 1st, 2003 Retained Earnings (increase or decrease and by how much). Assume a tax rate of 30%.

Question 3 (7 marks) (14 minutes)

Stine Ltd. decided on December 31, 2011 to discontinue its division in Vancouver. In 2011, division assets with a carrying value of \$650,000 had a fair market value less costs to sell of \$590,000. The profit generated by the division from January 1 to December 31, 2011 amounted to \$80,000. On December 31, 2012, the division hasn't been sold but the company is still committed to sell it. The fair market value less costs to sell was revaluated to \$610,000. In 2012, the division held for sale has generated sales of \$200,000 and expenses of \$340,000.

Required

Calculate the amount of gain/loss from discontinued operations to be reported on Stine's Statement of Comprehensive Income for the years ended December 31, 2011 and December 31, 2012. Assume a tax rate of 30%.

Question 4 (8 marks) (16 minutes)

Keffer Construction Corporation contracted to construct a building for \$2,500,000. Construction began in 2006 and was completed in 2008. Keffer used the percentage-of-completion method as the basis for income recognition. Data relating to the contract are summarized below:

	Year ended December 31,		
	<u>2006</u>	<u>2007</u>	<u>2008</u>
Costs incurred during the year	\$500,000	\$660,000	600,000
Estimated costs to complete	1,500,000	540,000	-----
Progress billings to date	700,000	1,500,000	2,500,000
Cash collected during the year	550,000	900,000	1,050,000

Required

- 1) Prepare the journal entries for Keffer in **2007**. Calculate percentages to two decimal places and round amounts to the nearest dollar.
- 2) Determine the balance of the 'Construction In Progress' account **net of Billings** in **December 31, 2007**.

Question 5 (20 marks) (40 minutes)

Yates Corporation is a public company which started business in 2006. You have been recently hired by the company as accountant and were provided with the following information taken from the company's combined Statement of Income and Retained Earnings for the year ended December 31, 2012:

**Yates Corporation
Combined Statement of Income and Retained Earnings
For the year ended December 31, 2012**

Net Income Before Taxes	\$3,500,000
Income tax (30%)	(1,050,000)
Net income	<u>2,450,000</u>
Retained Earnings, January 1 st	1,800,000
Preferred dividend	(200,000)
Common dividend	(350,000)
Retained Earnings, December 31 st	<u>\$3,700,000</u>

You have also collected the following information:

- 1) A piece of equipment acquired on January 1, 2010 for \$400,000 was depreciated based on the straight-line method. Useful life was estimated to 10 years and residual value to \$30,000. On January 1, 2012, the useful life of the equipment was revised to 6 years and the residual value to \$40,000. You are informed that the 2012 depreciation has not been recorded.
- 2) On October 1, 2012, the company decided to discontinue its plastic making division. The assets related to the discontinued business had a carrying value of \$800,000 as of December 31, 2012. Annual depreciation of \$35,000 was taken in 2012. An appraiser determined the Fair value less costs to sell the assets to be \$700,000 on October 1, 2012. No impairment loss or gain has been recorded. A total profit of \$300,000 (before tax) generated by the plastic making division was included in the Net Income before Taxes of \$3,500,000.
- 3) In 2011, the company received Rent advances of \$24,000 for the period of November 1, 2011 to March 31, 2012. The total amount has been recorded as "Rent revenue" in 2011 and the former accountant forgot to adjust the revenue account at the end of 2011. You discovered the error in December 2012.
- 4) The total number of outstanding common shares as of December 31, 2011 was 700,000. A stock split 2:1 was made in August 31, 2012.
- 5) There were 20,000 outstanding preferred shares, \$10, non-cumulative as of December 31, 2012.

Required:

- a) Prepare a revised Statement of Income and retained Earnings for Yates Corporation for the year ended December 31, 2012.
- b) Calculate basic EPS for the year ended December 31, 2012.

Solutions

Question 1

Sept 1, 20x4	Rent expense	14,000	
	Prepaid rent		14,000
	1 mark		
Jan 1, 20x5	Rent expense	21,000	
	Cash (3,500 x 6 months)		21,000
	2 marks		
July 1, 20x5	Rent expense	24,000	
	Cash (4,000 x 6 months)		24,000
	2 marks		
August 31, 20x5	Prepaid rent	16,000	
	Rent expense (4,000 x 4 months)		16,000
	2 marks		

Question 2

NBV of assets at Dec 31, 2000: $500,000 \times (0.8)^3 = \$256,000$ / total depreciation taken = $500,000 - 256,000 = \$244,000$

NBV under the SL method at Dec 31, 2000 = $500,000 - (500,000/10 \times 3) = 350,000$ / total depreciation taken = $500,000/10 \times 3 = \$150,000$

Increase in NBV = \$94,000 or decrease in accumulated depreciation \$94,000 **2 marks**

Impact on opening R/E = $94,000 \times 70\% = \$65,800$ increase **1 mark**

Question 3

2005:

Impairment loss: $650,000 - 590,000 = \$60,000$ **1 mark**

Total gain on discontinued operations: $80,000 - 60,000 = \$20,000 \times 70\% = \$14,000$ gain **2 marks**

2006:

Impairment gain: $610,000 - 590,000 = \$20,000$ **2 marks**

Total loss on discontinued operations: $(200,000 - 340,000 + 20,000) \times 70\% = \$84,000$ loss

2 marks

Question 4

% completion in 2006 = $500 / (500+1,500) = 25\%$ **1 mark**

Gross profit in 2006 : $(2,500,000 - 2,000,000) \times 25\% = \$125,000$

% of completion in 2007 : $660+500 / (660+500+540) = 1,160/1,700 = 68.24\%$ **1 mark**

Revenue to be recognized in 2007 = $\$2,500,000 \times (68.24\% - 25\%) = \$2,500,000 \times 43.24\% = 1,081,000$ **1 mark**

Profit to be recognized in 2007 = $[(2,500,000 - 1,700,000) \times 68.24] -$ **1 mark**

$[2,500,000 - 2,000,000) \times 25\%] = \$546,000 - 125,000 = \$421,000$ (rounded)

OR

$\$1,081,000 - 660,000 = \$421,000$

Journal entries

Construction in progress	660,000	
Cash, A/P		660,000
½ mark		
A/R	800,000	
Billings		800,000
1 mark		
Cash	900,000	
A/R		900,000
½ mark		
Construction costs	660,000	
Construction in progress	421,000	
Construction Revenue		1,081,000
½ mark		

Balance in the CIP account, end of 2007: $500,000^{\text{costs 2006}} + 125,000^{\text{profit 2006}} + 660,000^{\text{costs 2007}} + 421,000^{\text{profit 2007}} = \$1,706,000$ **1 mark**

Total billings in 2007: \$1,500,000

Net CIP balance: $\$1,706,000 - \$1,500,000 = \$206,000$ **½ mark**

Question 5

a)

$$1) \text{ Revised depreciation expense for 2012} = \frac{\text{Net Book Value} - \text{Revised RV}}{\text{Remaining useful life}}$$
$$= \frac{326,000^* - 40,000}{4 \text{ years}}$$
$$= \$71,500$$

*NBV = $400,000 - (400,000 - 30,000 / 10 * 2 \text{ years})$

3 marks

2) Add back depreciation of 3 months: $35,000/12 * 3 \text{ months} = \$8,750$ **1 mark**

Revised carrying value = $800,000 + 8,750 = \$808,750$ **1 mark**

Impairment loss = $700,000 - 808,750 = \$108,750$ **1 mark**

3- as of December 31, 2011: unexpired rent = $\$24,000/5 * 3 = \$14,400$ **1 mark**

Adjustment to opening retained earnings: $\$14,400 * 0.7 = 10,080$ decrease **1 mark**

Rent revenue to be recorded in 2012 : $\$14,400$.

**Yates Corporation
Combined Statement of Income and Retained Earnings
For the year ended December 31, 2012**

Net income before taxes (3,500,000 – 71,500 ^{revised depreciation of equipment} + 8,750 ^{depreciation on assets held for sale} – 300,000 ^{profit disc.})	\$3,151,650
Operations + \$14,400 ^{rent revenue})	4 marks
Income tax (30%)	<u>(945,495)</u>
Net income from continuing operations	<u>2,206,155</u>
Gain on discontinued operations ((300,000 profit – 108,750 impairment loss) x 70%)	3 marks
	<u>133,875</u>
Net income	<u>2,340,030</u>
Retained Earnings, January 1 st (1,800,000 - 10,080)	1 mark
Preferred dividend	(200,000)
Common dividend	(350,000)
Retained Earnings, December 31 st	1 mark
	<u>\$3,579,950</u>

b)

EPS = $2,340,030 - 200,000^{\text{pref. dividend}} / 1,400,000^{\text{common shares}} = \1.5286 **3 marks**

