

**Mid Term Exam
 Intermediate Financial Accounting II
 Winter 2013
 ADM3340**

(SUGGESTED SOLUTIONS)

Name: _____

ID#: _____

Required:

- Write your name and student ID number above.
- Turn off all cell phones.
- This examination “**SUGGESTED SOLUTION**” comprises **4** questions over **16** numbered pages. Answer all questions in this booklet. Booklet is **not** to be removed from the examination room. You may not separate the pages.
- Do not answer questions using a pencil or erasable pen: if you do you will forfeit the right to ask that your exam be remarked.
- Limit your answer to the space provided. Blank sheets for rough work and supporting calculations are given at the end of each question.
- This exam will be marked out of **100** marks (for convenience) and is 2½ hours long. You should budget approximately **1.5** minutes per mark. The exam is worth 40% of the overall course mark.
- Please do not ask the invigilator or the professor any questions, as they will not be answered. State reasonable assumptions, if you feel they are necessary.
- This exam paper must remain stapled: do not take this exam paper apart.
- Present value tables are provided on pages **15 and 16**.
- Language (non-electronic) dictionaries are allowed with the proctor’s permission.
- You **must** sign the Statement of Academic integrity on page 2 of this exam.

	Question		Marks
Ch 12	1: part 1	Goodwill	/3
	1: part 2	Intangibles: acquisition & amortization	/6
	1: part 3	Intangibles: impairment & reversal under ASPE	/6
	1: part 4	Intangibles: impairment & reversal under IFRS	/6
Ch 13	2: part 1	Promotion liabilities	/10
	2: part 2	Balance sheet presentation	/10
Ch 14	3: part 1	Bond liabilities: issuance	/9
	3: part 2	Bond liabilities: retirement	/12
	3: part 3	Troubled debt restructuring	/12
	3: part 4	Note payable	/7
Ch 15	4: part 1	Retained earnings	/5
	4: part 2	Dividends	/9
	4: part 3	Treasury stock	/5
	TOTAL		/100

Statement of Academic Integrity

The Telfer School of Management does not condone academic fraud, an act by a student that may result in a false academic evaluation of that student or of another student. Without limiting the generality of this definition, academic fraud occurs when a student commits any of the following offences: plagiarism or cheating of any kind, use of books, notes, mathematical tables, dictionaries or other study aid unless an explicit written note to the contrary appears on the exam, to have in his/her possession cameras, radios (radios with head sets), tape recorders, pagers, cell phones, or any other communication device which has not been previously authorized in writing.

Statement to be signed by the student:

I have read the text on academic integrity and I pledge not to have committed or attempted to commit academic fraud in this examination.

Signed: _____

Note: an examination copy or booklet without that signed statement will not be graded and will receive an exam grade of zero.

QUESTION 1 (21 marks)

Answer ALL parts to this question. Each part is independent.

PART 1: (3 marks)

Question 1

Once goodwill has been recognized in the accounts there has been much disagreement over how it should be treated in subsequent periods. Discuss briefly three alternative treatment approaches.

- a. Charge goodwill off immediately to shareholders' equity. Under this alternative goodwill is not deemed to be an asset that is separable from the business itself and therefore should not be recognized as a separate asset. In addition, immediate expensing would be consistent with the expensing of costs of internally generated goodwill. As well, there is no rational method to amortize goodwill, due to the many uncertainties involved; therefore, financial statements will be more reliable if it is expensed.
- b. Amortize goodwill over its useful life. Goodwill at the time of purchase erodes in value over time and therefore it should be charged to income over the estimated period in which it is expected to benefit the business.
- c. Retain goodwill indefinitely unless impairment occurs. Current and future expenses help to maintain existing goodwill; therefore, it can have an indefinite life. Amortization of goodwill is entirely arbitrary and leads to distortions of net income.

Question 1 (21 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 2: (6 marks)

The following transactions involving intangible assets of Vortage Corporation occurred on or near December 31, 2011. Complete the chart on the following page by writing the journal entry(ies) needed (i) at that date to record the transaction and (ii) at December 31, 2012 to record any resultant amortization. If no entry is required at a particular date, write "none needed."

1. Vortage paid Jorex Company \$200,000 for the exclusive right to market a particular product, using the Jorex name and logo in promotional material. The franchise runs for as long as Vortage is in business. Vortage decided to amortize the franchise over 25 years.
2. Vortage spent \$300,000 developing a new manufacturing process and has applied for a patent. It believes that its application will be successful and that the process will be successfully implemented and used for 10 years.
3. In January, 2012, Vortage 's application for a patent (#2 above) was granted. Legal and registration costs incurred were \$35,000. The patent runs for 17 years from the grant date. The manufacturing process will be useful to Vortage for 10 years.
4. Vortage incurred \$90,000 in successfully defending one of its patents in an infringement lawsuit. The patent expires during December, 2015.
5. Vortage incurred \$200,000 in an unsuccessful patent defence. As a result of the adverse verdict, the patent, with a remaining unamortized cost of \$99,000, is deemed worthless.

On Date of Transaction

1. Franchise (asset) ..	200,000	
Cash		200,000
2. Deferred		
Devel. Costs (asset)	300,000	
Cash.....		300,000
3. Patents (asset).....	35,000	
Cash.....		35,000
4. Patents (asset).....	90,000	
Cash.....		90,000
5. Legal Fees Expense	200,000	
Cash.....		200,000
Loss on Impairment of		
Patent.....	99,000	
Acc impairment losses		99,000
(or Patent)		

On December 31, 2011

1. Franchise Amort. Exp.	8,000	
Acc Amortization Franchise		8,000
2. Devel. Cost		
Amortization Expense		30,000
Deferred		
Devel. Costs		30,000
3. Patent Amortization		
Expense	3,500	
Acc Amortization Patents		3,500
4. Patent Amortization		
Expense	22,500	
Acc Amortization Patents		22,500
5. "None needed."		

Question 1 (21 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 2: (6 marks) (continued)

	On Date of Transaction	On December 31, 2012
1		
2		
3		
4		
5		

Question 1 (21 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 3: (6 marks)

	Limited-life intangibles	Indefinite-life intangibles (excluding goodwill)	Goodwill [the values below pertain to the Reporting Unit/Cash-Generating-Unit, including its Goodwill].
Has management observed events & circumstances indicating that there might be an impairment?	Yes	No	Yes
Carrying amount	\$8,000,000	\$8,000,000	\$32,000,000
Fair value	\$7,000,000	\$7,000,000	\$30,000,000
Costs to sell	\$40,000	\$40,000	\$500,000
Undiscounted future cash flows from use and eventual sale	\$9,000,000	\$7,600,000	\$40,000,000
Present value of the future cash flows from use and eventual sale	\$6,000,000	\$7,200,000	\$33,000,000

Required

Using the above data complete the following grid, applying ASPE. [Input the above data into www.impairmentlonglivednonfinancialassets.com](http://www.impairmentlonglivednonfinancialassets.com) for the suggested solution.

		Under ASPE		
		Limited-Life Intangible Assets.	Indefinite-Life Intangible Assets.	Goodwill.
1	Should the asset be tested for impairment? You must explain your answer.			
2	Ignore your answer to 1 above. Is the asset impaired? You must show supporting calculations.			
3	If the asset is deemed to be impaired, what is the amount of the impairment loss to be recognized in the income statement? You must show supporting calculations.			
4	Can an impairment loss reversal be recognized in a subsequent period, and if so, is there a limit to the reversal? Assume the company uses the cost model (i.e., not the revaluation model) subsequent to acquisition. You must explain your answer.			

Question 1 (21 marks) (continued)

Answer ALL parts to this question. Each part is independent.

Part 4: (6 marks)

	Limited-life intangibles	Indefinite-life intangibles (excluding goodwill)	Goodwill [the values below pertain to the Reporting Unit/Cash-Generating-Unit, including its Goodwill].
Has management observed events & circumstances indicating that there might be an impairment?	Yes	No	Yes
Carrying amount	\$8,000,000	\$8,000,000	\$32,000,000
Fair value	\$7,000,000	\$7,000,000	\$30,000,000
Costs to sell	\$40,000	\$40,000	\$500,000
Undiscounted future cash flows from use and eventual sale	\$9,000,000	\$7,600,000	\$40,000,000
Present value of the future cash flows from use and eventual sale	\$6,000,000	\$7,200,000	\$33,000,000

Required: Using the above data complete the following grid, applying IFRS. [Input the above data into www.impairmentlonglivednonfinancialassets.com](http://www.impairmentlonglivednonfinancialassets.com) for the suggested solution.

		Under IFRS		
		Limited-Life Intangible Assets.	Indefinite-Life Intangible Assets.	Goodwill.
1	Should the asset be tested for impairment? You must explain your answer.			
2	Ignore your answer to 1 above. Is the asset impaired? Show supporting calculations.			
3	If the asset is deemed to be impaired, what is the amount of the impairment loss to be recognized in the income statement? Show supporting calculations.			
4	Can an impairment loss reversal be recognized in a subsequent period, and if so, is there a limit to the reversal? Assume the company uses the cost model (i.e., not the revaluation model) subsequent to acquisition. You must explain your answer.			

QUESTION 2 (20 marks)

Answer ALL parts to this question. Each part is independent.

PART 1: (10 marks)

Rover Corp. commenced business in 2011 and includes one coupon in each bag of dog food it sells. In return for three coupons, customers receive a dog toy that the company purchases for \$1.20 each. Rover's experience indicates that 60% of the coupons will be redeemed. During 2011, 100,000 bags of dog food were sold, 22,000 toys were purchased, and 45,000 coupons were redeemed. During 2012, 120,000 bags of dog food were sold, 26,000 toys were purchased, and 60,000 coupons were redeemed.

Required

Determine the premium (promotion) expense to be reported in the income statement and the estimated liability for premiums on the year-end balance sheets for 2011 and 2012. Show all supporting calculations.

	<u>2011</u>	<u>2012</u>
Premium (promotion) expense	\$24,000 (1)	\$28,800 (3)
Estimated liability for premiums	6,000 (2)	10,800 (4)

- (1) $100,000 \times .6 = 60,000$; $60,000 \div 3 = 20,000$; $20,000 \times \$1.20 = \$24,000$.
 (2) $45,000 \div 3 = 15,000$; $20,000 - 15,000 = 5,000$; $5,000 \times \$1.20 = \$6,000$.
 (3) $120,000 \times .6 = 72,000$; $72,000 \div 3 = 24,000$; $24,000 \times \$1.20 = \$28,800$.
 (4) $60,000 \div 3 = 20,000$; $5,000 + 24,000 - 20,000 = 9,000$; $9,000 \times \$1.20 = \$10,800$.

PART 2: (10 marks)

At their last year end, December 31, 2012, the liabilities outstanding of Sapphire Corp included the following:

- Cash dividends on common shares, \$100,000, payable on January 15, 2013.
- Note payable to Vanier Bank, \$850,000, due January 20, 2013.
- Serial bonds, \$2,000,000, of which \$500,000 matures during 2013.
- Note payable to Rathmines Bank, \$200,000, due January 27, 2013.

The following transactions occurred early in 2013:

- January 15: The cash dividends were paid.
 January 20: The note payable to Vanier Bank was paid.
 January 25: Sapphire entered into a financing agreement with Terenure Bank, enabling it to borrow up to \$1,000,000 at any time through the end of 2015. Amounts borrowed under the agreement would bear interest at 1% above the bank's prime rate and would mature 3 years from the date of the loan. The corporation immediately borrowed \$800,000 to replace the cash used in paying its January 20 note to Vanier Bank.
 January 26: 40,000 common shares were issued for \$300,000. \$200,000 of the proceeds was used to pay off the note payable to Rathmines Bank.
 February 1: The financial statements for 2012 were issued.

Required

Prepare a partial balance sheet in good form for Sapphire Corp, showing the manner in which the above liabilities should be presented at December 31, 2012. Any appropriate note disclosure should be included. Sapphire Corp. uses ASPE.

Current liabilities:

Dividends payable on common shares	\$ 100,000	
Notes payable—Vanier Bank - Note 1	850,000	<small>[\$800k could be classified as long-term debt – see note 1]</small>
Note payable—Rathmines Bank - Note 2	200,000	<small>[could be classified as long-term debt – see note 2]</small>
Currently maturing portion of serial bonds	<u>500,000</u>	
Total current liabilities		\$1,650,000

Long-term debt:

Serial bonds not maturing currently	<u>1,500,000</u>	
Total long-term debt		<u>1,500,000</u>
Total liabilities		<u>\$3,150,000</u>

- Note 1: On January 25, 2013, the corporation borrowed \$800,000, payable on January 25, 2016, and used the proceeds to replace cash that had been used to repay a note payable on January 20, 2013.
- Note 2: On January 26, 2013, the corporation issued 40,000 common shares and received proceeds totalling \$300,000, of which \$200,000 was used to liquidate a note payable that matured on January 27, 2013.
[see ASPE 1510.13 or the second paragraph on page 841 of Kieso et al (9th ed): Under ASPE, currently maturing debt can be classified as long-term if there is irrefutable evidence at time of issuing financial statements that debt **has been or will be** replaced by or converted to long-term debt or the company's own share capital.]

QUESTION 3 (40 marks)

Answer ALL parts to this question. Each part is independent.

PART 1: (9 marks)

On April 1, 2012 BondBeagle Inc. issues \$2,500,000 face value bonds. The bond date is February 1, 2012, and the bonds carry a coupon rate of 6% per year, payable semi-annually on January 31 and July 31. The bonds' maturity date is January 31, 2022. The bonds are sold to provide an annual yield of 4%.

BondBeagle Inc. uses the effective interest rate method to amortize any bond premium or discount. BondBeagle Inc.'s accounting year-end is September 30.

Required

Present the journal entry to record the issuance of the bonds: show all supporting calculations.

Intro	INPUT	Text	Date_Tables	Issuance_Calc	Issuance	I1	I2	I3	I4	I5	Retiremer
	B	C	D	E							
2	April 01, 2012	Date of issuance	Dr	Cr							
3											
4											
5	Cash		2,928,174.67								
6		Interest payable		25,000.00							
7		Bonds payable		2,500,000.00							
8		Bond premium		403,174.67							
9											
<p>To record the issuance of 10.00-year bonds, face value \$2,500,000, stated interest rate 6.0000% per annum. The bond date is February 01, 2012 with interest paid semi-annually. There are 118 months (including 20 interest payments) between the bond's issuance and maturity dates. For details of how this journal entry's amounts are determined, please refer to the ISSUANCE_CALC sheet.</p>											

The following table is not required in your solution:

		If the bonds were issued on:	
		January 31, 2012	July 31, 2012
20			
21			
22			
23	Present value of the bond's 20.00 semi-annual interest payments of \$75,000 (= \$2,500,000 x 6.0000%/2) at 2.0000% effective interest rate [$\$1,226,357 = 16.35143 \times \$75,000$]	1,226,357.25	
24	Present value of the maturity value of \$2,500,000 at the end of 20.00 periods at 2.0000% effective interest rate [$\$1,682,425 = 0.67297 \times \$2,500,000$]	1,682,425.00	
25	Present value of the bond's 19.00 semi-annual interest payments of \$75,000 (= \$2,500,000 x 6.0000%/2) at 2.0000% effective interest rate [$\$1,175,885 = 15.67846 \times \$75,000$]		1,175,884.50
26	Present value of the maturity value of \$2,500,000 at the end of 19.00 periods at 2.0000% effective interest rate [$\$1,716,075 = 0.68643 \times \$2,500,000$]		1,716,075.00
27	Total	2,908,782.25	2,891,959.50
28	Bond proceeds, excluding any accrued interest and issuance cost, on April 01, 2012 (which lies between January 31, 2012 and July 31, 2012). $\$2,903,175 = \$2,908,782 + \{[(\$2,891,960 - \$2,908,782)/6\text{months}] \times 2\text{months}\}$	2,903,174.67	

Question 3 (40 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 2: (12 marks)

On February 1, 2013 BondBeagle Inc. issues \$2,000,000 face value bonds. The bond date is February 1, 2013, and the bonds carry a coupon rate of 4% per year, payable semi-annually on January 31 and July 31. The bonds' maturity date is January 31, 2033. Proceeds upon issuance were \$1,537,705, and the bonds provide an annual yield of 6%.

BondBeagle Inc. uses the effective interest rate method to amortize any bond premium or discount. On September 30, 2028 BondBeagle Inc. retires 30% of the bonds at 102.50%, excluding accrued interest. BondBeagle Inc.'s accounting year-end is August 31.

Required

Present all necessary journal entries for the retired bonds on September 30, 2028.

To answer this question you must first determine the amortized cost (carrying value) of the bond at July 31, 2028 (shown as \$1,844,278 below).

2013	11	February 1, 2013 to July 31, 2028: 31 interest pymt periods: 9 remaining periods to maturity. $\$40,000 \times 7.786108922 = \$311,444$ $\$2,000,000 \times 0.766416732 = 1,532,833$ Amortized cost at July 31, 2028 = $\$1,844,278$ (rounded)
2014-2027	168 (14yrs x 12)	
2028	<u>7</u>	
	<u>186</u> months	
186/6 = 31 periods		

Intro	INPUT	Text	Date_Tables	Issuance_Calc	Issuance	I1	I2	I3	I4	I5	Retirement	R1	R2	R3	R4	R5	Maturity	Amort_T
	B		C		D	E					F							
2																		
3			Date of retirement															
4		September 30, 2028			Dr	Cr												
5		Interest expense			2,766.42													
6		Bond discount				766.42												
7		Interest payable				2,000.00												
8																		
9																		
10																		
11																		
12		Loss on retirement			60,183.49													
13		Interest payable			4,000.00													
14		Bond payable			600,000.00													
15		Bond discount				45,183.49												
16																		
17		Cash				619,000.00												
18																		
19																		

Question 3 (40 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 3: (12 marks)

On 1/1/2012 Hobbit Inc. issued a 4 year 10% \$1,000,000 bond payable to Middle-Earth Bank. Interest payment dates are June 30 and December 31 and the bonds were issued to provide a semi-annual yield of **5%**. By December 2013 Hobbit Inc. is in financial difficulties and is about to miss the 31/12/2013 interest payment. Hobbit Inc. negotiates an agreement with Middle-Earth Bank whereby the bank agrees to waive the 31/12/2013 interest payment and to replace, effective 31/12/2013, the above bond with an 8 year \$700,000 bond bearing 14% annual interest, payable semi-annually. Due to Hobbit Inc.'s precarious situation, lenders would normally seek an 8% semi-annual return on this 'bail-out' financing.

Required

- (a) Is this troubled debt restructuring a *settlement* or a *modification*? Your answer must show all supporting calculations.
- (b) Answer either i or ii:
 - i If in part (a) you deem this restructuring to be a *settlement* provide any journal entries on Hobbit Inc's books that may be necessary on 31/12/2013.
 - ii If in part (a) you deem this restructuring to be a *modification*, what is the total of the interest expense that will be recognized by Hobbit Inc. during the 8 year life of the \$700,000 bond.

	A	B	C	D	E	F	G	H	I	J
3	Step 1									
4	PV of the 4 year bond at 31/12/2013, using the old bond's historic 5% semi-annual yield:									
5	PVA, 4 periods, 5%, \$50,000	\$ 50,000	5.00%	4	3.545950504		\$177,298			
6	PV, 4 periods, 5%, \$1,000,000	\$ 1,000,000	5.00%	4	0.822702475		822,702			
7							1,000,000			
8	31/12/2013 interest payment						50,000			
9	PV of old debt owed at 31/12/2013, using the old bond's historic 5% semi-annual yield:						\$1,050,000			
10										
11	PV of the new 8 year bond at 31/12/2013, using the old bond's historic 5% semi-annual yield:									
12	PVA, 16 periods, 5%, \$49,000	\$ 49,000	5.00%	16	10.837769560		\$531,051			
13	PV, 16 periods, 5%, \$700,000	\$ 700,000	5.00%	16	0.458111522		320,678			
14	PV of new debt at 31/12/2013, using the old bond's historic 5% semi-annual yield:						\$851,729			
15										
16	Step 2									
17	Difference (\$1,050,000 - \$851,729).						\$198,271			
18	Difference as a percentage of \$1,050,000						18.88%			
19	Greater than 10% and thus this is a 'settlement' and the old bond is derecognized.									
20										
21	Step 3									
22	As this is a 'settlement' calculate the PV of the new bond using the prevailing 8% required semi-annual rate of return for bonds with similar risk and maturity.									
23										
24	PV of the new 8 year bond at 31/12/2013, using the prevailing rate of return for bonds with similar risk and maturity:									
25	PVA, 16 periods, 8%, \$49,000	\$ 49,000	8.00%	16	8.851369155		\$433,717			
26	PV, 16 periods, 8%, \$700,000	\$ 700,000	8.00%	16	0.291890468		204,323			
27	PV of new debt at 31/12/2013, using the prevailing 8% required semi-annual rate of return for bonds with similar risk and maturity.						\$638,040			
28	Face value of the new 8 year bond:						700,000			
29	Therefore, bond discount is:						\$61,960			
30										
31	31/12/2013 J/E to record the bond restructuring									
32	(Old) Bond payable			1,000,000						
33	(Old) Bond discount									[\$0 = \$1,000,000 - \$1,000,000 (PV of the 4 year bond at 31/12/2013, using the old bond's historic 5% semi-annual yield)].
34	Interest payable				50,000					
35	(New) Bond discount				61,960					
36	(New) Bond payable						700,000			
37	Gain on bond restructuring						411,960			
38										
39										
40	This amortization table (assumes semi-annual interest payments) is not required:									
41	Beginning of period	Face value	Bond discount	Beginning of period amortized cost	7% interest paid per 6 months	8% interest expense per 6 months	Bond discount amortization	End of period amortized cost	End of period	
42	31-Dec-13	700,000	61,960	638,040	49,000	51,043	2,043	640,084	30-Jun-14	1
43	30-Jun-14	700,000	59,916	640,084	49,000	51,207	2,207	642,290	31-Dec-14	2
44	31-Dec-14	700,000	57,710	642,290	49,000	51,383	2,383	644,674	30-Jun-15	3
45	30-Jun-15	700,000	55,326	644,674	49,000	51,574	2,574	647,247	31-Dec-15	4
46	31-Dec-15	700,000	52,753	647,247	49,000	51,780	2,780	650,027	30-Jun-16	5
47	30-Jun-16	700,000	49,973	650,027	49,000	52,002	3,002	653,029	31-Dec-16	6
48	31-Dec-16	700,000	46,971	653,029	49,000	52,242	3,242	656,272	30-Jun-17	7
49	30-Jun-17	700,000	43,728	656,272	49,000	52,502	3,502	659,774	31-Dec-17	8
50	31-Dec-17	700,000	40,226	659,774	49,000	52,782	3,782	663,555	30-Jun-18	9
51	30-Jun-18	700,000	36,445	663,555	49,000	53,084	4,084	667,640	31-Dec-18	10
52	31-Dec-18	700,000	32,360	667,640	49,000	53,411	4,411	672,051	30-Jun-19	11
53	30-Jun-19	700,000	27,949	672,051	49,000	53,764	4,764	676,815	31-Dec-19	12
54	31-Dec-19	700,000	23,185	676,815	49,000	54,145	5,145	681,960	30-Jun-20	13
55	30-Jun-20	700,000	18,040	681,960	49,000	54,557	5,557	687,517	31-Dec-20	14
56	31-Dec-20	700,000	12,483	687,517	49,000	55,001	6,001	693,519	30-Jun-21	15
57	30-Jun-21	700,000	6,481	693,519	49,000	55,481	6,481	700,000	31-Dec-21	16
58				Totals	784,000	845,960	61,960			
59										
60										
61										
62	If this restructuring were deemed a <i>modification</i> then the total of the interest expense that will be recognized by Hobbit Inc. during the 8 year life of the \$700,000 bond is \$434,000.									
63	Total interest expense if the restructuring were deemed a <i>settlement</i> (as above)						845,960			
64	Gain on <i>settlement</i>						411,960			
65	Total interest expense if the restructuring were (incorrectly) deemed a <i>modification</i>						434,000			

Or: \$434,000 = interest paid of \$784,000 [\$700,000 x 14% x 8 years] less \$350,000 amortization [\$1,050,000 - \$700,000]

Question 3 (40 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 4: (7 marks)

Rebecca Land Corp. issued a 5-year, zero-interest-bearing note with a \$1,000,000 face value to Lindsay Inc. for \$1,000,000 cash. Rebecca also gave Lindsay the right to use a parcel of land for equipment storage for 5 years. Interest rates for notes of this type were 8% at the time of issue.

Required

Prepare the journal entries to record the issuance of the note by (1) Rebecca and (2) Lindsay.

Rebecca

Cash	1,000,000	
Notes Payable.....		* 680,500
Unearned Revenue (Rent).....		319,420

Lindsay

Notes Receivable	* 680,500	
Prepaid Rent.....	319,420	
Cash.....		1,000,000

\$680,580 is the present value of \$1,000,000 at 8% for 5 years

QUESTION 4 (19 marks)

Answer ALL parts to this question. Each part is independent.

PART 1: (5 marks)

What are the items that increase retained earnings?

Items that increase retained earnings are:

- net income,
- prior period adjustments (error corrections),
- financial reorganization, and
- certain changes in accounting principle.

What are the items that decrease retained earnings?

Items that decrease retained earnings are:

- net loss,
- cash, property and most stock dividends,
- some treasury shares transactions,
- prior period adjustments (error corrections), and
- certain changes in accounting principle.

PART 2: (9 marks)

In each of the following independent cases, it is assumed that the corporation has outstanding 20,000, \$0.80, preferred shares, with a carrying value of \$200,000, and 80,000 common shares, with a carrying value of \$800,000. No dividends have been declared for 2010 or 2011.

- (a) At December 31, 2012, the board of directors wants to distribute \$125,000 in dividends. How much will the preferred shareholders receive if their shares are cumulative and nonparticipating? Show all supporting calculations.
- (b) At December 31, 2012, the board of directors wants to distribute \$210,000 in dividends. How much will the preferred shareholders receive if their shares are cumulative and participating up to a 15% return in total? Show all supporting calculations.
- (c) On December 31, 2012, the preferred shareholders received an \$80,000 dividend on their shares, which are cumulative and fully participating. How much money was distributed in total for dividends to the preferred and common shares? Show all supporting calculations.

(a) Preferred: \$48,000. $[(\$0.80 \times 20,000) \times 2 \text{ yrs arrearages}] + [(\$0.80 \times 20,000) \text{ for 2012}]$.
Common: \$77,000 = \$125,000 - \$48,000. Not Asked.

(b) Preferred: \$62,000 = $[(\$0.80 \times 20,000) \times 2 \text{ yrs arrearages}] + (\$200,000 \times 15\%)$.
Common: \$148,000 = \$210,000 - \$62,000. [\$148,000 is an 18.5% return on \$800,000]. Not Asked.

(c) \$272,000 (\$192,000 to common and \$80,000 to preferred: Not Asked).

- $\$80,000 - [(\$0.80 \times 20,000) \times 2 \text{ yrs arrearages}] = \$48,000$;
- $\$48,000 / \$200,000 = 24\%$.
- $24\% \times (\$200,000 + \$800,000) = \$240,000$;
- Total dividend declared = $\$240,000 + [(\$0.80 \times 20,000) \times 2 \text{ yrs arrearages}] = \$272,000$.

Question No. 4 (19 marks) (continued)

Answer ALL parts to this question. Each part is independent.

PART 3: (5 marks)

Sasquatch Corporation's last year-end balance sheet reported the following in its shareholders equity section:

Common shares, no par, outstanding 5,000 shares	\$115,000
Retained earnings	200,000

The following transactions occurred this year:

- (a) Purchased 70 common shares at \$30 per share, to be held as treasury shares.
- (b) Sold 60 treasury shares at \$32 per share.
- (c) Retired the remaining treasury shares.

Required

Prepare the journal entries for these transactions.

(a) Treasury Shares (70 x \$30)	2,100	
Cash		2,100
(b) Cash (60 x \$32)	1,920	
Treasury Shares (60 x \$30)		1,800
Contributed Surplus		120
(c) Common Shares 10 x (\$115,000/5,000)	230	
Contributed Surplus	70	
Treasury Shares (10 x \$30)		300

Financial Tables

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

Period/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
7	0.9327181	0.8705602	0.8130915	0.7599178	0.7106813	0.6650571	0.6227497	0.5834904	0.5470342	0.5131581	0.4816584	0.4523492
8	0.9234832	0.8534904	0.7894092	0.7306902	0.6768394	0.6274124	0.5820091	0.5402689	0.5018663	0.4665074	0.4339265	0.4038832
9	0.9143398	0.8367553	0.7664167	0.7025867	0.6446089	0.5918985	0.5439337	0.5002490	0.4604278	0.4240976	0.3909248	0.3606100
10	0.9052870	0.8203483	0.7440939	0.6755642	0.6139133	0.5583948	0.5083493	0.4631935	0.4224108	0.3855433	0.3521845	0.3219732
11	0.8963237	0.8042630	0.7224213	0.6495809	0.5846793	0.5267875	0.4750928	0.4288829	0.3875329	0.3504939	0.3172833	0.2874761
12	0.8874492	0.7884932	0.7013799	0.6245970	0.5568374	0.4969694	0.4440120	0.3971138	0.3555347	0.3186308	0.2858408	0.2566751
13	0.8786626	0.7730325	0.6809513	0.6005741	0.5303214	0.4688390	0.4149644	0.3676979	0.3261786	0.2896644	0.2575143	0.2291742
14	0.8699630	0.7578750	0.6611178	0.5774751	0.5050680	0.4423010	0.3878172	0.3404610	0.2992465	0.2633313	0.2319948	0.2046198
15	0.8613495	0.7430147	0.6418619	0.5552645	0.4810171	0.4172651	0.3624460	0.3152417	0.2745380	0.2393920	0.2090043	0.1826963
16	0.8528213	0.7284458	0.6231669	0.5339082	0.4581115	0.3936463	0.3387346	0.2918905	0.2518698	0.2176291	0.1882922	0.1631217
17	0.8443775	0.7141626	0.6050164	0.5133732	0.4362967	0.3713644	0.3165744	0.2702690	0.2310732	0.1978447	0.1696326	0.1456443
18	0.8360173	0.7001594	0.5873946	0.4936281	0.4155207	0.3503438	0.2958639	0.2502490	0.2119937	0.1798588	0.1528222	0.1300396
19	0.8277399	0.6864308	0.5702860	0.4746424	0.3957340	0.3305130	0.2765083	0.2317121	0.1944897	0.1635080	0.1376776	0.1161068
20	0.8195445	0.6729713	0.5536758	0.4563869	0.3768895	0.3118047	0.2584190	0.2145482	0.1784309	0.1486436	0.1240339	0.1036668
21	0.8114302	0.6597758	0.5375493	0.4388336	0.3589424	0.2941554	0.2415131	0.1986557	0.1636981	0.1351306	0.1117423	0.0925596
22	0.8033962	0.6468390	0.5218925	0.4219554	0.3418499	0.2775051	0.2257132	0.1839405	0.1501817	0.1228460	0.1006687	0.0826425
23	0.7954418	0.6341559	0.5066917	0.4057263	0.3255713	0.2617973	0.2109469	0.1703153	0.1377814	0.1116782	0.0906925	0.0737880
24	0.7875661	0.6217215	0.4919337	0.3901215	0.3100679	0.2469785	0.1971466	0.1576993	0.1264049	0.1015256	0.0817050	0.0658821
25	0.7797684	0.6095309	0.4776056	0.3751168	0.2953028	0.2329986	0.1842492	0.1460179	0.1159678	0.0922960	0.0736081	0.0588233
26	0.7720480	0.5975793	0.4636947	0.3606892	0.2812407	0.2198100	0.1721955	0.1352018	0.1063925	0.0839055	0.0663136	0.0525208
27	0.7644039	0.5858620	0.4501891	0.3468166	0.2678483	0.2073680	0.1609304	0.1251868	0.0976078	0.0762777	0.0597420	0.0468936
28	0.7568356	0.5743746	0.4370768	0.3334775	0.2550936	0.1956301	0.1504022	0.1159137	0.0895484	0.0693433	0.0538216	0.0418693
29	0.7493421	0.5631123	0.4243464	0.3206514	0.2429463	0.1845567	0.1405628	0.1073275	0.0821545	0.0630394	0.0484879	0.0373833
30	0.7419229	0.5520709	0.4119868	0.3083187	0.2313774	0.1741101	0.1313671	0.0993773	0.0753711	0.0573086	0.0436828	0.0333779
31	0.7345771	0.5412460	0.3999871	0.2964603	0.2203595	0.1642548	0.1227730	0.0920160	0.0691478	0.0520987	0.0393539	0.0298017
32	0.7273041	0.5306333	0.3883370	0.2850579	0.2098662	0.1549574	0.1147411	0.0852000	0.0634384	0.0473624	0.0354540	0.0266087
33	0.7201031	0.5202287	0.3770262	0.2740942	0.1998725	0.1461862	0.1072347	0.0788889	0.0582003	0.0430568	0.0319405	0.0237577
34	0.7129733	0.5100282	0.3660449	0.2635521	0.1903548	0.1379115	0.1002193	0.0730453	0.0533948	0.0391425	0.0287752	0.0212123
35	0.7059142	0.5000276	0.3553834	0.2534155	0.1812903	0.1301052	0.0936629	0.0676345	0.0489861	0.0355841	0.0259236	0.0189395
36	0.6989249	0.4902232	0.3450324	0.2436687	0.1726574	0.1227408	0.0875355	0.0626246	0.0449413	0.0323492	0.0233546	0.0169103
37	0.6920049	0.4806109	0.3349829	0.2342968	0.1644356	0.1157932	0.0818088	0.0579857	0.0412306	0.0294093	0.0210402	0.0150985
38	0.6851534	0.4711872	0.3252262	0.2252854	0.1566054	0.1092389	0.0764569	0.0536905	0.0378262	0.0267349	0.0189551	0.0134808
39	0.6783697	0.4619482	0.3157535	0.2166206	0.1491480	0.1030555	0.0714550	0.0497134	0.0347030	0.0243044	0.0170767	0.0120364
40	0.6716531	0.4528904	0.3065568	0.2082890	0.1420457	0.0972222	0.0667804	0.0460309	0.0318376	0.0220949	0.0153844	0.0107468

Table 4: PRESENT VALUE of Annuity of \$1.00 in arrears.												
Period/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
7	6.728195	6.471991	6.230283	6.002055	5.786373	5.582381	5.389289	5.206370	5.032953	4.868419	4.712196	4.563757
8	7.651678	7.325481	7.019692	6.732745	6.463213	6.209794	5.971299	5.746639	5.534819	5.334926	5.146123	4.967640
9	8.566018	8.162237	7.786109	7.435332	7.107822	6.801692	6.515232	6.246888	5.995247	5.759024	5.537048	5.328250
10	9.471305	8.982585	8.530203	8.110896	7.721735	7.360087	7.023582	6.710081	6.417658	6.144567	5.889232	5.650223
11	10.367628	9.786848	9.252624	8.760477	8.306414	7.886875	7.498674	7.138964	6.805191	6.495061	6.206515	5.937699
12	11.255077	10.575341	9.954004	9.385074	8.863252	8.383844	7.942686	7.536078	7.160725	6.813692	6.492356	6.194374
13	12.133740	11.348374	10.634955	9.985648	9.393573	8.852683	8.357651	7.903776	7.486904	7.103356	6.749870	6.423548
14	13.003703	12.106249	11.296073	10.563123	9.898641	9.294984	8.745468	8.244237	7.786150	7.366687	6.981865	6.628168
15	13.865053	12.849264	11.937935	11.118387	10.379658	9.712249	9.107914	8.559479	8.060688	7.606080	7.190870	6.810864
16	14.717874	13.577709	12.561102	11.652296	10.837770	10.105895	9.446649	8.851369	8.312558	7.823709	7.379162	6.973986
17	15.562251	14.291872	13.166118	12.165669	11.274066	10.477260	9.763223	9.121638	8.543631	8.021553	7.548794	7.119630
18	16.398269	14.992031	13.753513	12.659297	11.689587	10.827603	10.059087	9.371887	8.755625	8.201412	7.701617	7.249670
19	17.226008	15.678462	14.323799	13.133939	12.085321	11.158116	10.335595	9.603599	8.950115	8.364920	7.839294	7.365777
20	18.045553	16.351433	14.877475	13.590326	12.462210	11.469921	10.594014	9.818147	9.128546	8.513564	7.963328	7.469444
21	18.856983	17.011209	15.415024	14.029160	12.821153	11.764077	10.835527	10.016803	9.292244	8.648694	8.075070	7.562003
22	19.660379	17.658048	15.936917	14.451115	13.163003	12.041582	11.061240	10.200744	9.442425	8.771540	8.175739	7.644646
23	20.455821	18.292204	16.443608	14.856842	13.4889574	12.303379	11.272187	10.371059	9.580207	8.883218	8.266432	7.718434
24	21.243387	18.913926	16.935542	15.246963	13.798642	12.550358	11.469334	10.528758	9.706612	8.984744	8.348137	7.784316
25	22.023156	19.523456	17.413148	15.622080	14.093945	12.783356	11.653583	10.674776	9.822580	9.077040	8.421745	7.843139
26	22.795204	20.121036	17.876842	15.982769	14.375185	13.003166	11.825779	10.809978	9.928972	9.160945	8.488058	7.895660
27	23.559608	20.706898	18.327031	16.329586	14.643034	13.210534	11.986709	10.935165	10.026580	9.237223	8.547800	7.942554
28	24.316443	21.281272	18.764108	16.663063	14.898127	13.406164	12.137111	11.051078	10.116128	9.306567	8.601622	7.984423
29	25.065785	21.844385	19.188455	16.983715	15.141074	13.590721	12.277674	11.158406	10.198283	9.369606	8.650110	8.021806
30	25.807708	22.396456	19.600441	17.292033	15.372451	13.764831	12.409041	11.257783	10.273654	9.426914	8.693793	8.055184
31	26.542285	22.937702	20.000428	17.588494	15.592811	13.929086	12.531814	11.349799	10.342802	9.479013	8.733146	8.084986
32	27.269589	23.468335	20.388766	17.873551	15.802677	14.084043	12.646555	11.434999	10.406240	9.526376	8.768600	8.111594
33	27.989693	23.988564	20.765792	18.147646	16.002549	14.230230	12.753790	11.513888	10.464441	9.569432	8.800541	8.135352
34	28.702666	24.498592	21.131837	18.411198	16.192904	14.368141	12.854009	11.586934	10.517835	9.608575	8.829316	8.156564
35	29.408580	24.998619	21.487220	18.664613	16.374194	14.498246	12.947672	11.654568	10.566821	9.644159	8.855240	8.175504
36	30.107505	25.488842	21.832252	18.908282	16.546852	14.620987	13.035208	11.717193	10.611763	9.676508	8.878594	8.192414
37	30.799510	25.969453	22.167235	19.142579	16.711287	14.736780	13.117017	11.775179	10.652993	9.705917	8.899635	8.207513
38	31.484663	26.440641	22.492462	19.367864	16.867893	14.846019	13.193473	11.828869	10.690820	9.732651	8.918590	8.220993
39	32.163033	26.902589	22.808215	19.584485	17.017041	14.949075	13.264928	11.878582	10.725523	9.756956	8.935666	8.233030
40	32.834686	27.355479	23.114772	19.792774	17.159086	15.046297	13.331709	11.924613	10.757360	9.779051	8.951051	8.243777