

ACCO. 320- SUMMER, 2015

MID-TERM REVIEW

- 1) Multiple choice questions, varied, ch. 13, 14, 16**
- 2) Auburn Limited- bond retirement, ch. 14**
- 3) Dilemma Inc.- restructure debt, ch. 14**
- 4) Shankman Corporation- bond conversion, ch. 16**
- 5) Niagara Co. convertible bonds with warrants, exercise of warrants, ch. 14, 16**

Question 1 (this section contains 5 multiple choice questions)

1) When a deposit on returnable containers is forfeited, the company holding the deposit will experience:

- a) An increase in expenses.
- b) An increase in revenues.**
- c) An increase in accounts receivable.
- d) An increase in current liabilities.

Cash X → liab dep X
liab dep X rev PP&E X

2) On February 5, 2013, an employee filed a \$2 million lawsuit against Steel Co. for damages suffered when one of Steel's plants exploded on December 29, 2012. Steel Co. uses IFRS. Steel's legal counsel expects the company will lose the lawsuit and estimates the loss to be between \$500,000 and \$1,000,000 with no point in the range being more likely than any other. The employee has offered to settle the lawsuit out of court for \$900,000 but Steel will not agree to the settlement. In its December 31, 2012 balance sheet how should Steel Co. account for this event?

IFRS
probable > 50% (more likely than not)
estimable?
range 500k - 1000k
expected value 750k

- a) ignore since the action was only taken after year end;
- b) accrue \$900,000 and note disclose information re the lawsuit including amount of action;
- c) accrue \$750,000 and note disclose information re the lawsuit including amount of action;**
- d) accrue \$500,000 and note disclose information re the lawsuit including amount of action;
- e) accrue \$1,000,000.

3) Kearney Corporation issued call options on 20,000 shares of Royal Bank Inc. on October 31, 2013. These options give the holder the right to buy Royal Bank shares at \$33 per share until April 30, 2014 and Kearney Corporation received \$30,000 by selling these options and records this revenue on the straight line basis over the option term. At its' fiscal year end of December 31, 2013, the Royal Bank shares traded on the Montreal Exchange for \$35.50 each. On April 30, 2014 Royal Bank's share price was \$37 and option holders exercised their options.

For the year ended December 31, 2013 what was Kearney Corporations gain or loss relating to these options?

- a) loss of \$50,000;
- b) loss of \$35,000;
- c) gain of \$30,000;
- d) loss of \$40,000**
- e) none of the above.

K
writer 20000 #
exp 33

	6 months	expires
33		apr 30
oct 31		
	Dec 31/13	
	35.50	
	33	
	<u>2.50</u>	
	× 20,000	
	\$ 50k	

X Loss derivative call 50
Liab derivative 50
Not the answer
since 2/6 months
Liab call 10k
Revenue 10k

	Gross	80k	Remit
QPP		$1260 \times 2 =$	2,520
EI		$910 \times 2.4 =$	2,184
I/T		$(25,000) \rightarrow$	25,000
Invest		$(1,200)$	<u>29,704</u>

Multiple choice questions (continued)

- 4) Tippo Co., recorded gross salaries for the month amounting to \$80,000. QPP deductions were \$1,260, EI deductions were \$910. Income tax withheld was \$25,000 and \$1,200 was withheld for investment in company stock per agreement with certain employees. What would be the total amount to remit to the government given that Tippo must remit income tax deducted, QPP and EI deducted as well as employer portion of QPP (match deduction from employee) and EI of 1.4 times deduction from employees?
- a. \$30,904
 - b. \$29,704**
 - c. \$25,000
 - d. \$29,584
 - e. none of the above, but \$ _____.

- 5) Luger Machinery Ltd. Has made a total of \$46,500 in instalments for corporate income tax for 2011, which have been debited to Current Income Tax expense. At year end, December 31, 2011, the accountant has calculated that the corporation's actual tax liability is only \$43,000. What is the correct adjusting entry to reflect this fact?
- a) Dr- Current income tax expense \$3,500; cr-Income taxes payable \$3,500.
 - b) Dr-Income taxes payable \$3,500; cr- Current income tax expense \$3,500.
 - c) Dr-Income taxes receivable \$3,500; cr- current income tax expense \$3,500.**
 - d) Dr-Current income tax expense \$43,000; cr- income taxes payable \$43,000.

I/T expense 46,500
 Cash 46,500

 I/T receivable 3,500
 I/T expense 3,500

Question 2)

E14 16 (Entries for Retirement and Issuance of Bonds—Straight-Line) On June 30, 2004, Auburn Limited issued 12% bonds with a par value of \$800,000 due in 20 years. They were issued at 98 and were callable at 104 at any date after June 30, 2011.

Because of lower interest rates and a significant change in the company's credit rating, it was decided to call the entire issue on June 30, 2011, and to issue new bonds. New 10% bonds were sold in the amount of \$1 million at 102; they mature in 20 years. The company follows private enterprise GAAP and uses straight-line amortization. The interest payment dates are December 31 and June 30 of each year.

Instructions

- Prepare journal entries to record the retirement of the old issue and the sale of the new issue on June 30, 2011.
- Prepare the entry required on December 31, 2011, to record the payment of the first six months of interest and the amortization of the bond premium.

Question 3)

Dilemma Inc. owes Stauskas Bank a \$250,000, 10-year, 15% note. The note is due today, December 31, 2011. Because Dilemma Inc. is in financial trouble, Stauskas agrees to accept 60,000 shares of Dilemma's common shares, which are currently selling for \$1.40; to reduce the note's face amount to \$150,000; to extend the maturity date to December 31, 2015; and to reduce the interest rate to 6%. Interest will continue to be due on December 31 of each year. (Interest is still outstanding as at December 31, 2011.)

- Prepare all the necessary journal entries on the books of Dilemma Inc. from the time of the restructuring through 2012.
- Prepare all the necessary journal entries on the books of Stauskas Bank from the time of the restructuring through 2012.

a) Test $\geq 10\%$

	Old	New
price	250k	150k
term	10yr	
i	15%	6%
due	31/12/11 (now)	31/12/15 4 years
C/s	—	84k
Int. due (15%)(250k)	37.5k	0

(A) given

$$C/s \rightarrow 60,000 \times 1.40 \$ \underline{84k}$$

$$.06 \times 150k \times PVF \overset{\text{Annuity factor}}{A \over 15\% \over 4} + 150k \times PVF \overset{.15\% \over 4}{.5715}$$

$$2.85498$$

$$\underline{111458}$$

$$\underline{195458}$$

$$\underline{287500}$$

$$\leq 10\%$$



Review Questions

Question 2

	30/6/04	Face	800K	disc	(16K)	BV	784K
↓ 7 years		(20yr)	$\frac{6K}{2} = 800 \times 7$	$\frac{56K}{10.41K}$		<u>5.6K</u>	789.6K
	30/6/11	new cash	semi-dec 31 st	June 30 th	Cash		
		b/p	new				1020K

100,000

b/p dd 789.6K

Cash

832K (800 x 1.04)

loss on red

42.4K

Hope the audio helps his writing was a mess

b)

$$A = 20 \times 2 = 40 \left. \begin{array}{l} \$20 \\ \end{array} \right\} \underline{\$500}$$

dec 31/11

b/p

500

Cash

$$\frac{1}{2} \times 10\% \times 1mm = 50K$$

b) deprec
 1) 31/12/11
 dep old 250k
 int pay 37.5k
 dep new 11158
 c/s 2412
 gain 22,042

31/12/12
 int. expense (.15 x 111458) 16719
 (cash (150 x 6%)) 9k
 dep new 7719

Question 4)

Shankman Corporation

8% convertible bond issue in the face amount of \$8 million. Interest payment dates of the bond issue are June 30 and December 31. The conversion clause in the bond indenture entitles the bondholders to receive 40 no par value common shares in exchange for each \$1,000 bond. The value of the equity portion of the bond issue is \$60,000. On June 30, 2011, the holders of \$1.2 million of the face value bonds exercised the conversion privilege. The market price of the bonds on that date was \$1,100 per bond and the market price of the common shares was \$35. The total unamortized bond discount at the date of conversion was \$500,000.

Instructions

Prepare in general journal form the entry to record the exercise of the conversion option, using the book value method. Assume the company follows IFRS.

Question 5)

On September 30, 2011, Niagara Co. issued a \$2 million, 8%, 10-year convertible bond maturing on September 30, 2021 with semi-annual coupon payments on March 31 and September 30. Each \$1,000 bond can be converted into 80 no par value common shares. In addition, each bond included 20 detachable common stock warrants with an exercise price of \$20 each. Immediately after issuance, the warrants traded at \$4 each on the open market. Gross proceeds on issuance were \$2.6 million. Without the warrants and conversion features the bond would be expected to yield 6% annually. Niagara's year end is December 31.

On February 22, 2014, warrant holders exercised one-half of the warrants. The shares of Niagara traded at \$44 each on this day.

Required:

- a) Determine how Niagara should allocate the \$2.6 million proceeds into its components.
- b) Prepare all the journal entries for fiscal year 2011.
- c) Record the journal entry for the exercise of stock warrants on February 22, 2014.

Question 3 b) Bank side
(ignore market rate)

31/12/11

BDE or AFDA/C

92042

loan receivable

111458

C/S invest

84,000

int. ra.

37,500

loan old

250,000

31/12/12

cash

9000

loan receivable

7,719

int. receivable

16,719

Question 4

Bonds Payable convert 8% → 8mm

semi June 30 dec 31

\$1,000 → 40 C/S

cont. surp. - C 60k

30/6/11

convert! 1.2mm / 8mm

\$8mm face

(600k)

\$7.5mm BV → $\frac{1.2}{8} = 1125k$

cont. surplus 60k → $\frac{1.2}{8} = 9k$

Common shares

1134k

Question 5

a) convertible bond \$2 mm semi } \$ mm x PVIF $\overline{207.03}$ + 2mm x $\overline{04}$ x PVIF $\overline{207.03}$
 1,000\$ → 30 c/s 8% coupon } ^{coupon} _{annuity}

1,000\$ → 20w expc \$20 @ \$4/w * 2,000 = \$160,000 #

Allocate the surplus
 229 755 8
 0 → 142,442
 160K
 2 600 000
 b/p
 cont. surpl - C
 cont. surpl - W

b) 30/9/11
 Cash 2600k
 cont. surplus - W 160k
 cont. surplus - C 142442
 b pay 2297558

31/12/11
 int exp (2297558 * 3%) 34463
 b/p 5537
~~int. payable~~ 40k
 (2mm x 4% x .5)

c) Feb 22/14

40 000 W * \$4 * .5 = 80 000

Cont. sup - W

800 00

C/S

480, 000

Cash (40,000 * 20)

400 000

* .5