

Part A.

On January 1, Year 4, PARENT Corporation purchased 80% of the outstanding shares of SUBSIDIARY Company for \$720,000. At that date, the book values and fair values of SUBSIDIARY were as follows:

SUBSIDIARY COMPANY
Balance Sheet
January 1, Year 4

	Book Value	Fair Value
Cash	\$ 100,000	\$ 100,000
Accounts receivable	180,000	180,000
Inventory	220,000	260,000
Equipment	580,000	425,000
Accumulated depreciation equipment	65,000	
	\$ 1,015,000	
Accounts payable	\$ 240,000	\$ 240,000
Bond payable	135,000	114,000
Common shares	200,000	
Retained earnings	440,000	
	\$ 1,015,000	

The Year 8 financial statements of PARENT and SUBSIDIARY are as follows:

PARENT CORPORATION and SUBSIDIARY COMPANY
Balance Sheets
December 31, Year 8

	PARENT	SUBSIDIARY
Cash	\$ 500,000	\$ 140,000
Accounts receivable	780,000	200,000
Due from SUBSIDIARY	105,000	—
Inventory	970,000	300,000
Investment in SUBSIDIARY	720,000	—
Equipment — net	1,540,000	750,000
Accumulated Depreciation Equipment	375,000	150,000
	\$ 4,240,000	\$ 1,240,000
Accounts payable	\$ 720,000	\$ 150,000
Due to PARENT	—	105,000
Bond payable	700,000	205,000
Common shares	2,000,000	200,000
Retained earnings	820,000	580,000
	\$ 4,240,000	\$ 1,240,000

PARENT CORPORATION and SUBSIDIARY COMPANY
Statements of Income and Retained Earnings
Year ended December 31, Year 8

	PARENT	SUBSIDIARY
Sales	\$ 1,900,000	\$ 1,000,000
Dividend income	80,000	—
Interest revenue	10,000	—
Total revenue	1,990,000	1,000,000
Cost of goods sold	1,220,000	700,000
Gross profit	770,000	300,000
Expenses		
Selling and administrative	200,000	50,000
Depreciation	80,000	40,000
Interest and other	90,000	30,000
Total expense	370,000	120,000
Income before income taxes	400,000	180,000
Income tax expense	160,000	72,000
Net income	240,000	108,000
Retained earnings, January 1, Year 8	700,000	572,000
Dividends	(120,000)	(100,000)
Retained earnings, December 31, Year 8	\$ 820,000	\$ 580,000

Additional information

1. As of January 1, Year 4, the capital assets of Subsidiary had a remaining useful life of 8 years, and Subsidiary planned to keep the capital assets throughout their useful life.
2. The Subsidiary's bond payable was issued on January 1, Year 4 and matures on December 31, Year 10.
3. Each year, goodwill is evaluated to determine if there has been a permanent impairment. Goodwill impairment was \$80,000 in Year 5 & \$50,000 in Year 8.
4. On July 1, Year 8, Parent lent \$105,000 to Subsidiary. The loan bears a zero interest rate and principal due June 30, Year 9.
5. On December 15, Year 8, Subsidiary declared and paid \$100,000 in dividends.

Required: (35 Marks)

- a) Indicate the method of accounting Parent is using to record its investment in Subsidiary on its non-consolidated financial statements. Identify 2 factors that support your conclusion.
- b) Calculate the goodwill on purchase
- c) Prepare the acquisition differential amortization and impairment schedule.
- d) Prepare the consolidated income statement.
- e) Calculate consolidated retained earnings as of January 1, Year 8.
- f) Prepare the consolidated retained earnings as of December 31, Year 8.
- g) Calculate the non-controlling interest as of December 31, Year 8.
- h) Prepare the consolidated Balance Sheet for Parent on December 31, Year 8.

Part B. Chapter 6

Grand Inc. purchased 80% of the voting shares of Slam Inc for \$500,000 on January 1, Year 4. Assume that Grand uses the cost method to account for its investment in Slam Inc.

The Financial Statements of both companies for the Year ended December 31, Year 7 are shown below:

Income Statements	<u>Grand Inc.</u>	<u>Slam Inc.</u>
Sales	\$650,000	\$350,000
Other Revenues	100,000	40,000
Less: Expenses		
Cost of Goods Sold	\$375,000	\$220,000
Depreciation Expense	40,000	18,000
Other Expenses	67,000	25,000
Income Tax Expense	108,000	50,000
Net Income	<u>\$160,000</u>	<u>\$77,000</u>

Retained Earnings Statements	<u>Grand Inc.</u>	<u>Slam Inc.</u>
Retained Earnings, January 1, Year 7	\$190,000	\$250,000
Net Income	160,000	77,000
Less: Dividends	(25,000)	(40,000)
Retained Earnings, December 31, Year 7	<u>\$325,000</u>	<u>\$287,000</u>

Other Information:

During Year 6 Grand sold \$90,000 worth of Inventory to Slam. This inventory had a cost of \$55,000. 75% of which was sold by Slam to outsider parties during the year. This remaining 25% was sold by Slam to outsiders during Yr 7.

During Year 7, Slam sold inventory to Grand for \$110,000. This inventory had a cost of \$70,000 to Slam. 65% of this inventory was resold by Grand to outside parties in Yr 7.

The effective tax rate for both companies is 40%.

Part B required:

1. Prepare a schedule of before tax and after tax unrealized profits at the beginning and end of Year 7. State if the transaction is upstream or downstream.
2. Prepare Paris's Consolidated Income Statement for the Year ended December 31, Year 7. Show the allocation of the income between the controlling and non-controlling interests. Show all calculations for full marks.