File: Chapter 02 Consolidation of Financial Information

Multiple Choice

[QUESTION]
1. At the date of an acquisition which is not a bargain purchase, the acquisition method
A) consolidates the subsidiary's assets at fair value and the liabilities at book value.
B) consolidates all subsidiary assets and liabilities at book value.
C) consolidates all subsidiary assets and liabilities at fair value.
D) consolidates current assets and liabilities at book value, long-term assets and liabilities at fair value.
E) consolidates the subsidiary's assets at book value and the liabilities at fair value.
Answer: C
Difficulty: Easy

[QUESTION]
2. In a purchase or acquisition where control is achieved, how would the land accounts of the parent and the land accounts of the subsidiary be combined?

	Parent	Subsidiary
A)	Book Value	Book Value
B)	Book Value	Fair Value
C)	Fair Value	Fair Value
D)	Fair Value	Book Value
E)	Cost	Cost

A) Entry A.
B) Entry B.
C) Entry C.
D) Entry D.
E) Entry E.
Answer: B
Difficulty: Medium

[QUESTION]
3. Lisa Co. paid cash for all of the voting common stock of Victoria Corp. Victoria will continue to exist as a separate corporation. Entries for the consolidation of Lisa and Victoria would be recorded in
A) a worksheet.
B) Lisa's general journal.
C) Victoria's general journal.
D) Victoria's secret consolidation journal.
E) the general journals of both companies.
Answer: A
Difficulty: Easy

[QUESTION]
4. Using the purchase method, goodwill is generally defined as:
A) Cost of the investment less the subsidiary's book value at the beginning of the year.
B) Cost of the investment less the subsidiary's book value at the acquisition date.

C) Cost of the investment less the subsidiary's Fair Value at the beginning of the year.
D) Cost of the investment less the subsidiary's Fair Value at acquisition date.
E) is no longer allowed under federal law.
Answer: D
Difficulty: Medium

[QUESTION]
5. Direct combination costs and stock issuance costs are often incurred in the process of making a controlling investment in another company. How should those costs be accounted for in a Purchase transaction?

	Direct Combination Costs	Stock Issuance Costs
A)	Increase Investment	Decrease Investment
B)	Increase Investment	Decrease Paid-In Capital
C)	Increase Investment	Increase Expenses
D)	Decrease Paid-In Capital	Increase Investment
E)	Increase Expenses	Decrease Investment

A) Entry A.
B) Entry B.
C) Entry C.
D) Entry D.
E) Entry E.
Answer: B
Difficulty: Medium

[QUESTION]
6. Direct combination costs and stock issuance costs are often incurred in the process of making a controlling investment in another company. How should those costs be accounted for in an Acquisition transaction?

	Direct Combination Costs	Stock Issuance Costs
A)	Increase Investment	Decrease Investment
B)	Increase Investment	Decrease Paid-In Capital
C)	Increase Investment	Increase Expenses
D)	Decrease Paid-In Capital	Increase Investment
E)	Increase Expenses	Decrease Investment

Commented [ILP1]: I can't edit picture. Need to change item D so first text box is "Increase Expenses" and second text box is "Decrease Paid-In Capital"

A) Entry A.
B) Entry B.
C) Entry C.
D) Entry D.
E) Entry E.
Answer: D
Difficulty: Medium

[QUESTION]
7. What is the *primary* accounting difference between accounting for when the subsidiary is dissolved and when the subsidiary retains its incorporation?
A) If the subsidiary is dissolved, it will not be operated as a separate division.
B) If the subsidiary is dissolved, assets and liabilities are consolidated at their book values.
C) If the subsidiary retains its incorporation, there will be no goodwill associated with the acquisition.

D) If the subsidiary retains its incorporation, assets and liabilities are consolidated at their book values.
E) If the subsidiary retains its incorporation, the consolidation is not formally recorded in the accounting records of the acquiring company.
Answer: E
Difficulty: Medium

[QUESTION]
8. According to SFAS No. 141, the pooling of interest method for business combinations
A) Is preferred to the purchase method.
B) Is allowed for all new acquisitions.
C) Is no longer allowed for business combinations after June 30, 2001.
D) Is no longer allowed for business combinations after December 31, 2001.
E) Is only allowed for large corporate mergers like Exxon and Mobil.
Answer: C
Difficulty: Easy

[QUESTION]
9. In a pooling of interests,
A) revenues and expenses are consolidated for the entire fiscal year, even if the combination occurred late in the year.
B) goodwill may be recognized.
C) consolidation is accomplished using the fair values of both companies.
D) the transactions may involve the exchange of preferred stock or debt securities as well as common stock.
E) the transaction is properly regarded as an acquisition of one company by another.
Answer: A
Difficulty: Easy

[QUESTION]
10. A company is not required to consolidate a subsidiary in which it holds more than 50% of the voting stock when
A) the subsidiary is located in a foreign country.
B) the subsidiary in question is a finance subsidiary.
C) the company holds more than 50% but less than 60% of the subsidiary's voting stock.
D) the company holds less than 75% of the subsidiary's voting stock.
E) the subsidiary is in bankruptcy.
Answer: E
Difficulty: Medium

[QUESTION]
11. Which one of the following is a characteristic of a business combination that should be accounted for as an *acquisition*?
A) The combination must involve the exchange of equity securities only.
B) The transaction establishes an acquisition fair value basis for the company being acquired.
C) The two companies may be about the same size, and it is difficult to determine the acquired company and the acquiring company.
D) The transaction may be considered to be the uniting of the ownership interests of the companies involved.
E) The acquired subsidiary must be smaller in size than the acquiring parent.
Answer: B

Difficulty: Easy

[QUESTION]
12. Which one of the following is a characteristic of a business combination that should be accounted for as a *purchase*?
A) The combination must involve the exchange of equity securities only.
B) The transaction clearly establishes an acquisition price for the company being acquired.
C) The two companies may be about the same size, and it is difficult to determine the acquired company and the acquiring company.
D) The transaction may be considered to be the uniting of the ownership interests of the companies involved.
E) The acquired subsidiary must be smaller in size than the acquiring parent.
Answer: B
Difficulty: Easy

[QUESTION]
13. A *statutory merger* is a(n)
A) business combination in which only one of the two companies continues to exist as a legal corporation.
B) business combination in which both companies continues to exist.
C) acquisition of a competitor.
D) acquisition of a supplier or a customer.
E) legal proposal to acquire outstanding shares of the target's stock.
Answer: A
Difficulty: Medium

[QUESTION]
14. How are *stock issuance costs* and *direct combination costs* treated in a business combination which is accounted for as an acquisition when the subsidiary will retain its incorporation?
A) Stock issuance costs are a part of the acquisition costs, and the direct combination costs are expensed.
B) Direct combination costs are a part of the acquisition costs, and the stock issuance costs are a reduction to additional paid-in capital.
C) Direct combination costs are expensed and stock issuance costs are a reduction to additional paid-in capital.
D) Both are treated as part of the acquisition price.
E) Both are treated as a reduction to additional paid-in capital.
Answer: C
Difficulty: Medium

REFERENCE: Ref. 02_01
Bullen Inc. assumed 100% control over Vicker Inc. on January 1, 20X1. The book value and fair value of Vicker's accounts on that date (prior to creating the combination) follow, along with the book value of Bullen's accounts:

	Bullen Book Value	Vicker Book Value	Vicker Fair Value
Retained earnings, 1/1/X1	$160,000	$240,000	

Cash receivables	170,000	70,000	$70,000
Inventory	230,000	170,000	210,000
Land	280,000	220,000	240,000
Buildings (net)	480,000	240,000	270,000
Equipment (net)	120,000	90,000	90,000
Liabilities	650,000	430,000	420,000
Common stock	360,000	80,000	
Additional paid-in capital	20,000	40,000	

[QUESTION]
REFER TO: Ref. 02_01
15. Assume that Bullen issued 12,000 shares of common stock with a $5 par value and a $47 fair value to obtain all of Vicker's outstanding stock. In this transaction (which is not a pooling of interests), how much goodwill should be recognized?
A) $144,000.
B) $104,000.
C) $64,000.
D) $60,000.
E) $0.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_01
16. Assume that Bullen issued 12,000 shares of common stock with a $5 par value and a $42 fair value for all of the outstanding stock of Vicker. What is the consolidated Land as a result of this transaction (which is not a pooling of interests)?
A) $460,000.
B) $510,000.
C) $500,000.
D) $520,000.
E) $490,000.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_01
17. Assume that Bullen issued 12,000 shares of common stock with a $5 par value and a $42 fair value for all of the outstanding shares of Vicker. What will be the consolidated Additional Paid-In Capital and Retained Earnings (January 1, 20X1 balances) as a result of this transaction (which is not a pooling of interests)?
A) $20,000 and $160,000.
B) $20,000 and $260,000.
C) $380,000 and $160,000.
D) $464,000 and $160,000.
E) $380,000 and $260,000.
Answer: D
Difficulty: Hard

[QUESTION]
REFER TO: Ref. 02_01
18. Assume that Bullen issued preferred stock with a par value of $240,000 and a fair value of $500,000 for all of the outstanding shares of Vicker in a business combination (which is not a pooling of interests). What will be the balance in the consolidated Inventory and Land accounts?
A) $440,000, $496,000.
B) $440,000, $520,000.
C) $425,000, $505,000.
D) $402,000, $520,000.
E) $427,000, $510,000.
Answer: B
Difficulty: Hard

[QUESTION]
REFER TO: Ref. 02_01
19. Assume that Bullen paid a total of $480,000 in cash for all of the shares of Vicker. In addition, Bullen paid $35,000 to a group of attorneys for their work in arranging the combination to be accounted for as a purchase. What will be the balance in consolidated goodwill?
A) $0.
B) $20,000.
C) $35,000.
D) $55,000.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_01
20. Assume that Bullen paid a total of $480,000 in cash for all of the shares of Vicker. In addition, Bullen paid $35,000 to a group of attorneys for their work in arranging the combination to be accounted for as an acquisition. What will be the balance in consolidated goodwill?
A) $0.
B) $20,000.
C) $35,000.
D) $55,000.
Answer: B
Difficulty: Medium

REFERENCE: Ref. 02_02
Prior to being united in a business combination, Botkins Inc. and Volkerson Corp. had the following stockholders' equity figures:

	Botkins	Volkerson
Common stock ($1 par value)	$ 220,000	$ 54,000
Additional paid-in capital	110,000	25,000
Retained earnings	360,000	130,000

Botkins issued 56,000 new shares of its common stock valued at $3.25 per share for all of the outstanding stock of Volkerson.

[QUESTION]

REFER TO: Ref. 02_02
21. Assume that Botkins acquired Volkerson as a purchase combination. Immediately afterwards, what are consolidated Additional Paid-In Capital and Retained Earnings, respectively?
A) $133,000 and $360,000.
B) $236,000 and $360,000.
C) $130,000 and $360,000.
D) $236,000 and $490,000.
E) $133,000 and $490,000.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_02
22. Assume that Botkins and Volkerson were being joined in a pooling of interests and this occurred on January 1, 2000, using the same values given . Immediately afterwards, what is consolidated Additional Paid-In Capital?
A) $138,000.
B) $266,000.
C) $130,000.
D) $236,000.
E) $133,000.
Answer: E
Difficulty: Hard

[QUESTION]
23. Chapel Hill Company had common stock of $350,000 and retained earnings of $490,000. Blue Town Inc. had common stock of $700,000 and retained earnings of $980,000. On January 1, 2009, Blue Town issued 34,000 shares of common stock with a $12 par value and a $35 fair value for all of Chapel Hill Company's outstanding common stock. This combination was accounted for as an acquisition. Immediately after the combination, what was the consolidated net assets?
A) $2,520,000.
B) $1,190,000.
C) $1,680,000.
D) $2,870,000.
E) $2,030,000.
Answer: D
Difficulty: Medium

[QUESTION]
24. Which of the following is a *not* a reason for a business combination to take place?
A) Cost savings through elimination of duplicate facilities.
B) Quick entry for new and existing products into domestic and foreign markets.
C) Diversification of business risk.
D) Vertical integration.
E) Cost synergies throughout the organizations.
Answer: E
Difficulty: Easy

[QUESTION]

25. Which of the following statements is true regarding a statutory merger?
A) The original companies dissolve while remaining as separate divisions of a newly created company.
B) Both companies remain in existence as legal corporations with one corporation now a subsidiary of the acquiring company.
C) The acquired company dissolves as a separate corporation and becomes a division of the acquiring company.
D) The acquiring company acquires the stock of the acquired company as an investment.
E) A statutory merger is no longer a legal option.
Answer: C
Difficulty: Medium

[QUESTION]
26. Which of the following statements is true regarding a statutory consolidation?
A) The original companies dissolve while remaining as separate divisions of a newly created company.
B) Both companies remain in existence as legal corporations with one corporation now a subsidiary of the acquiring company.
C) The acquired company dissolves as a separate corporation and becomes a division of the acquiring company.
D) The acquiring company acquires the stock of the acquired company as an investment.
E) A statutory consolidation is no longer a legal option..
Answer: A
Difficulty: Medium

[QUESTION]
27. In a transaction accounted for using the *purchase* method where cost exceeds book value, which statement is true for the acquiring company with regard to its investment?
A) Net assets of the acquired company are revalued to their fair values and any excess of cost over fair value is allocated to goodwill.
B) Net assets of the acquired company are maintained at book value and any excess of cost over book value is allocated to goodwill.
C) Assets are revalued to their fair values. Liabilities are maintained at book values. Any excess is allocated to goodwill.
D) Long-term assets are revalued to their fair values. Any excess is allocated to goodwill.
Answer: A
Difficulty: Medium

[QUESTION]
28. In a transaction accounted for using the *purchase* method where cost is less than fair value, which statement is true?
A) Negative goodwill is recorded.
B) A deferred credit is recorded.
C) Long-term assets of the acquired company are reduced in proportion to their fair values. Any excess is recorded as a deferred credit.
D) Long-term assets of the acquired company are reduced in proportion to their fair values. Any excess is recorded as an extraordinary gain.
E) Long-term assets and liabilities of the acquired company are reduced in proportion to their fair values. Any excess is recorded as an extraordinary gain.
Answer: D
Difficulty: Hard

[QUESTION]
29. Which of the following statements is true regarding the pooling of interests method of accounting for a business combination?
A) Net assets of the acquired company are reported at their book values.
B) Net assets of the acquired company are reported at their fair values.
C) Any goodwill associated with the acquisition has an indefinite life.
D) Subsequent amounts of cost in excess of fair value of net assets are amortized over their useful lives.
E) Indirect costs reduce additional paid-in capital.
Answer: A
Difficulty: Medium

[QUESTION]
30. Which of the following statements is true?
A) Pooling of interests is acceptable provided the twelve criteria required by the APB are met.
B) Pooling of interests is no longer acceptable for new combinations as stated in *SFAS No. 141*, “Business Combinations.”
C) Companies that used pooling of interests method in the past must make a retrospective accounting change in accounting principle.
D) Companies that used pooling of interests method in the past must make a cumulative effect accounting change in accounting principle.
E) Companies that used pooling of interests in the past must make a prospective change in accounting principle.
Answer: B

REFERENCE: Ref. 02_03
The financial statements for Goodwin, Inc., and Corr Company for the year ended December 31, 20X1, prior to Goodwin’s business combination transaction regarding Corr, follow (in thousands):

	Goodwin	Corr
Revenues	$2,700	$600
Expenses	1,980	400
Net income	$ 720	$200
Retained earnings 1/1	$2,400	$400
Net income	720	200
Dividends	(270)	(0)
Retained earnings, 12/31	$2,850	$600
Cash	$ 240	$ 220
Receivables and inventory	1,200	340
Buildings (net)	2,700	600
Equipment (net)	2,100	1,200
Total assets	$6,240	$2,360
Liabilities	$1,500	$ 820
Common stock	1,080	400
Additional paid-in capital	810	540
Retained earnings	2,850	600
Total liabilities & stockholders' equity	$6,240	$2,360

On December 31, 20X1, Goodwin issued $600 in debt and 30 shares of its $10 par value common stock to the owners of Corr to purchase all of the outstanding shares of that company. Goodwin shares had a fair value of $40 per share.
Goodwin paid $25 to a broker for arranging the transaction. Goodwin paid $35 in stock issuance costs. Corr's equipment was actually worth $1,400 but its buildings were only valued at $560.

[QUESTION]
REFER TO: Ref. 02_03
31. If the combination is accounted for as a purchase, at what amount is the investment recorded on Goodwin's books?
A) $1,540.
B) $1,800.
C) $1,860.
D) $1,825.
E) $1,625.
Answer: D
Difficulty: Medium

[QUESTION]
32. If the combination is accounted for as an acquisition, at what amount is the investment recorded on Goodwin's books?
A) $1,540.
B) $1,800.
C) $1,860.
D) $1,825.
E) $1,625.
Answer: B

Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_03
33. Compute the consolidated revenues for 20X1.
A) $2,700.
B) $720.
C) $920.
D) $3,300.
E) $1,540.
Answer: A
Difficulty: Easy

[QUESTION]
REFER TO: 02_03
34. Assuming the combination is accounted for as a purchase, compute the consolidated expenses for 20X1.
A) $1,980.
B) $2,380.
C) $2,040.
D) $2,015.
E) $2,005.
Answer: A
Difficulty: Easy

[QUESTION]
REFER TO: 02_03
35. Assuming the combination is accounted for as an acquisition, compute the consolidated expenses for 20X1.
A) $1,980.
B) $2,380.
C) $2,040.
D) $2,015.
E) $2,005.
Answer: E
Difficulty: Easy

[QUESTION]
REFER TO: 02_03
36. Compute the consolidated cash account at December 31, 20X1.
A) $460.
B) $425.
C) $400.
D) $435.
E) $240.
Answer: C
Difficulty: Medium

[QUESTION]

REFER TO: 02_03
37. Compute the consolidated buildings (net) account at December 31, 20X1.
A) $2,700.
B) $3,370.
C) $3,300.
D) $3,260.
E) $3,340.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
38. Compute the consolidated equipment (net) account at December 31, 20X1.
A) $2,100.
B) $3,500.
C) $3,300.
D) $3,000.
E) $3,200.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
39. Assuming the combination is accounted for as a purchase, compute the consolidated goodwill account at December 31, 20X1.
A) $0.
B) $100.
C) $125.
D) $160.
E) $45.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
40. Assuming the combination is accounted for as an acquisition, compute the consolidated goodwill account at December 31, 20X1.
A) $0.
B) $100.
C) $125.
D) $160.
E) $45.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
41. Compute the consolidated common stock account at December 31, 20X1.
A) $1,080.
B) $1,480.

C) $1,380.
D) $2,280.
E) $2,680.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
42. Compute the consolidated additional paid-in capital at December 31, 20X1.
A) $810.
B) $1,350.
C) $1,675.
D) $1,910.
E) $1,875.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
43. Assumiing the combination is accounted for as a purchase, compute the consolidated retained earnings at December 31, 20X1.
A) $2,850.
B) $3,450.
C) $2,400.
D) $2,800.
E) $2,810.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: 02_03
44. Assuming the combination is accounted for as an acquisition, compute the consolidated retained earnings at December 31, 20X1.
A) $2,800.
B) $2,825.
C) $2,850.
D) $3,425.
E) $3,450.
Answer: B
Difficulty: Medium

REFERENCE: Ref. 02_04
On January 1, 20X1, the Moody company entered into a transaction for 100% of the outstanding common stock of Osorio Company. To acquire these shares, Moody issued $400 in long-term liabilities and 40 shares of common stock having a par value of $1 per share but a fair value of $10 per share. Moody paid $20 to lawyers, accountants, and brokers for assistance in bringing about this purchase. Another $15 was paid in connection with stock issuance costs. Prior to these transactions, the balance sheets for the two companies were as follows:

	Moody	Osorio
Cash	$ 180	$ 40
Receivables	810	180
Inventories	1,080	280
Land	600	360
Buildings (net)	1,260	440
Equipment (net)	480	100
Accounts payable	(450)	(80)
Long-term liabilities	(1,290)	(400)
Common stock ($1 par)	(330)	
Common stock ($20 par)		(240)
Additional paid-in capital	(1,080)	(340)
Retained earnings	(1,260)	(340)

Note: Parentheses indicate a credit balance.

In Moody's appraisal of Osorio, three assets were deemed to be undervalued on the subsidiary's books: Inventory by $10, Land by $40, and Buildings by $60.

[QUESTION]
REFER TO: 02_04
45. If the transaction is accounted for as a purchase, what amount was recorded as the investment in Osorio?
A) $930.
B) $820.
C) $800.
D) $835.
E) $815.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: 02_04
46. If the transaction is accounted for as an acquisition, what amount was recorded as the investment in Osorio?
A) $930.
B) $820.
C) $800.
D) $835.
E) $815.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: 02_04
47. Compute the amount of consolidated inventories at date of combination.
A) $1,080.
B) $1,350.
C) $1,360.

D) $1,370.
E) $290.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: 02_04
48. Compute the amount of consolidated buildings (net) at date of combination.
A) $1,700.
B) $1,760.
C) $1,655.
D) $1,550.
E) $1,660.
Answer: C
Difficulty: Hard

[QUESTION]
REFER TO: 02_04
49. Compute the amount of consolidated land at date of combination.
A) $1,000.
B) $816.
C) $940.
D) $916.
E) $920.
Answer: D
Difficulty: Hard

[QUESTION]
REFER TO: 02_04
50. Compute the amount of consolidated equipment at date of combination.
A) $580.
B) $480.
C) $559.
D) $570.
E) $560.
Answer: C
Difficulty: Hard

[QUESTION]
REFER TO: 02_04
51. Compute the amount of consolidated common stock at date of acquisition.
A) $370.
B) $570.
C) $610.
D) $330.
E) $530.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: 02_04

52. Compute the amount of consolidated additional paid-in capital at date of combination.
A) $1,080.
B) $1,420.
C) $1,065.
D) $1,425.
E) $1,440.
Answer: D
Difficulty: Hard

[QUESTION]
REFER TO: 02_04
53. Compute the amount of consolidated cash after recording the transaction.
A) $220.
B) $185.
C) $200.
D) $205.
E) $215.
Answer: B
Difficulty: Medium

REFERENCE: Ref. 02_05
Carnes has the following account balances as of May 1, 2000 before a pooling of interests transaction takes place.

Inventory	$100,000
Land	400,000
Buildings (net)	500,000
Common stock ($10 par)	600,000
Retained earnings	200,000
Revenues	450,000
Expenses	250,000

The fair value of Carnes' Land and Buildings are $650,000 and $550,000, respectively. On May 1, 2000, Riley Company issues 30,000 shares of its $10 par value ($25 fair value) common stock in exchange for all of the shares of Carnes' common stock.

[QUESTION]
REFER TO: 02_05
54. On May 1, 2000, what value is assigned to the investment account?
A) $300,000.
B) $750,000.
C) $800,000.
D) $1,100,000.
E) $1,300,000.
Answer: B
Difficulty: Medium

[QUESTION]

REFER TO: 02_05
55. At the date of pooling, by how much does Riley's retained earnings increase or decrease?
A) $200,000 increase.
B) $200,000 decrease.
C) $700,000 increase.
D) $300,000 increase.
E) $300,000 decrease.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: 02_05
56. Assume Riley issues 70,000 shares instead of 30,000 at date of acquisition. Riley currently has $40,000 of additional paid-in capital on its books. By how much will Riley's retained earnings increase or decrease as a result of the combination?
A) $40,000 increase.
B) $200,000 increase.
C) $140,000 increase.
D) $160,000 increase.
E) $40,000 decrease.
Answer: C
Difficulty: Hard

[QUESTION]
REFER TO: 02_05
57. Assume Riley issues 70,000 shares instead of 30,000 at date of pooling. Assume Riley has no additional paid-in capital on its books. By how much will Riley's retained earnings increase or decrease as a result of the combination?
A) $100,000 increase.
B) $200,000 increase.
C) $100,000 decrease.
D) $200,000 decrease.
E) No change.
Answer: A
Difficulty: Hard.

REFERENCE: Ref. 02_06
The financial balances for the Atwood Company and the Franz Company as of December 31, 20X1, are presented below. Also included are the fair values for Franz Company's net assets.

	Atwood	Franz Co.	
	(all numbers are in thousands)		
	Book Value December 31, 20X1	Book Value December 31, 20X1	Fair Value December 31, 20X1
Cash	$ 870	$ 240	$ 240
Receivables	660	600	600
Inventory	1,230	420	580
Land	1,800	260	250

Buildings (net)	1,800	540	650
Equipment (net)	660	380	400
Accounts payable	(570)	(240)	(240)
Accrued expenses	(270)	(60)	(60)
Long-term liabilities	(2,700)	(1,020)	(1,120)
Common stock ($20 par)	(1,980)		
Common stock ($5 par)		(420)	
Additional paid-in capital	(210)	(180)	
Retained earnings	(1,170)	(480)	
Revenues	(2,880)	(660)	
Expenses	2,760	620	

Note: Parenthesis indicate a credit balance

Assume a business combination took place at December 31, 20X1. Atwood issued 50 shares of its common stock with a fair value of $35 per share for all of the outstanding common shares of Franz. Stock issuance costs of $15 (in thousands) and direct costs of $10 (in thousands) were paid.

[QUESTION]
REFER TO: Ref. 02_06
58. Assuming Atwood accounts for the combination as a purchase, compute the investment to be recorded at date of acquisition.
A) $1,760.
B) $1,750.
C) $1,775.
D) $1,765.
E) $1,120.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
59. Assuming Atwood accounts for the combination as an acquisition, compute the investment to be recorded at date of acquisition.
A) $1,760.
B) $1,750.
C) $1,775.
D) $1,765.
E) $1,120.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
60. Compute consolidated inventory at the date of the business combination.
A) $1,650.
B) $1,810.
C) $1,230.
D) $580.
E) $1,830.

Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
61. Compute consolidated land at the date of the business combination.
A) $2,060.
B) $1,800.
C) $260.
D) $2,050.
E) $2,070.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
62. Compute consolidated buildings (net) at the date of the business combination.
A) $2,450.
B) $2,340.
C) $1,800.
D) $650.
E) $1,690.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
63. Assuming Atwood accounts for the combination as a purchase, compute consolidated goodwill at the date of the combination.
A) $360.
B) $450.
C) $460.
D) $440.
E) $475.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
64. Assuming Atwood accounts for the combination as an acquisition, compute consolidated goodwill at the date of the combination.
A) $360.
B) $450.
C) $460.
D) $440.
E) $475.
Answer: B
Difficulty: Medium

[QUESTION]

REFER TO: Ref. 02_06
65. Compute consolidated equipment (net) at the date of the combination.
A) $400.
B) $660.
C) $1,060.
D) $1,040.
E) $1,050.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
66. Assuming the combination is accounted for as a purchase, compute consolidated retained earnings at the date of the combination.
A) $1,170.
B) $1,650.
C) $1,290.
D) $1,810.
E) $3,870.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
67. Assuming the combination is accounted for as an acquisition, compute consolidated retained earnings at the date of the combination.
A) $1,160.
B) $1,170.
C) $1,280.
D) $1,290.
E) $1,640.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
68. Compute consolidated revenues at the date of the combination.
A) $3,540.
B) $2,880.
C) $1,170.
D) $1,650.
E) $4,050.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
69. Assuming the combination is accounted for as a purchase, compute consolidated expenses at the date of the combination.
A) $2,760.
B) $3,380.

C) $2,770.
D) $2,735.
E) $2,785.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_06
70. Assuming the combination is accounted for as an acquisition, compute consolidated expenses at the date of the combination.
A) $2,760.
B) $2,770.
C) $2,785.
D) $3,380.
E) $3,390.
Answer: B
Difficulty: Medium

REFERENCE: Ref. 02_07
Presented below are the financial balances for the Atwood Company and the Franz Company as of December 31, 2009, immediately before Atwood acquired Franz. Also included are the fair values for Franz Company's net assets at that date.

	Atwood	Franz Co.	Franz Co.
	(all amounts in thousands)		
	Book Value December 31, 2008	Book Value December 31, 2008	Fair Value December 31, 2008
Cash	$ 870	$ 240	$ 240
Receivables	660	600	600
Inventory	1,230	420	580
Land	1,800	260	250
Buildings (net)	1,800	540	650
Equipment (net)	660	380	400
Accounts payable	(570)	(240)	(240)
Accrued expenses	(270)	(60)	(60)
Long-term liabilities	(2,700)	(1,020)	(1,120)
Common stock ($20 par)	(1,980)		
Common stock ($5 par)		(420)	
Additional paid-in capital	(210)	(180)	
Retained earnings	(1,170)	(480)	
Revenues	(2,880)	(660)	
Expenses	2,760	620	

Note: Parenthesis indicate a credit balance

Assume a business combination took place at December 31, 2009. Atwood issued 50 shares of its common stock with a fair value of $35 per share for all of the outstanding common shares of Franz. Stock issuance costs of $15 (in thousands) and direct costs of $10 (in thousands) were paid. Atwood is applying the **acquisition method** in accounting for Franz. To settle a difference of opinion regarding Franz's fair value, Atwood promises to pay an additional $5.2 (in thousands) to the former owners if Franz's earnings exceed a certain sum during the next year. Given the probability of the required contingency payment and utilizing a 4% discount rate, the expected present value of the contingency is $5 (in thousands).

[QUESTION]
REFER TO: Ref. 02_07
71. Compute the investment cost at date of acquisition.
A) $1,760.
B) $1,755.
C) $1,750.
D) $1,765.
E) $1,120.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
72. Compute consolidated inventory at date of acquisition.
A) $1,650.
B) $1,810.
C) $1,230.
D) $580.
E) $1,830.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
73. Compute consolidated land at date of acquisition.
A) $2,060.
B) $1,800.
C) $260.
D) $2,050.
E) $2,070.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
74. Compute consolidated buildings (net) at date of acquisition.
A) $2,450.
B) $2,340.
C) $1,800.
D) $650.
E) $1,690.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07

75. Compute consolidated goodwill at date of acquisition.
A) $455.
B) $460.
C) $450.
D) $440.
E) $465.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
76. Compute consolidated equipment at date of acquisition.
A) $400.
B) $660.
C) $1,060.
D) $1,040.
E) $1,050.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
77. Compute consolidated retained earnings as a result of this acquisition.
A) $1,160.
B) $1,170.
C) $1,265.
D) $1,280.
E) $1,650.
Answer: D
Difficulty: Hard

[QUESTION]
REFER TO: Ref. 02_07
78. Compute consolidated revenues at date of acquisition.
A) $3,540.
B) $2,880.
C) $1,170.
D) $1,650.
E) $4,050.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
79. Compute consolidated expenses at date of acquisition.
A) $2,760.
B) $3,380.
C) $2,770.
D) $2,735.
E) $2,785.
Answer: C

Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_07
80. Compute the consolidated cash upon completion of the acquisition.
A) $870.
B) $1,110.
C) $1,080.
D) $1,085.
E) $635.
Answer: D
Difficulty: Medium

REFERENCE: Ref. 02_08
Flynn acquires 100 percent of the outstanding voting shares of Macek Company on January 1, 20X1. To obtain these shares, Flynn pays $400 (in thousands) and issues 10,000 shares of $20 par value common stock on this date. Flynn's stock had a fair value of $36 per share on that date. Flynn also pays $15 (in thousands) to a local investment firm for arranging the transaction. An additional $10 (in thousands) was paid by Flynn in stock issuance costs.
The book values for both Flynn and Macek as of January 1, 20X1 follow. The fair value of each of Flynn and Macek accounts is also included. In addition, Macek holds a fully amortized trademark that still retains a $40 (in thousands) value. *The figures below are in thousands*. Any related question also is in thousands.

	Flynn, Inc.	Macek Company	
		Book Value	Fair Value
Cash	$ 900	$ 80	$ 80
Receivables	480	180	160
Inventory	660	260	300
Land	300	120	130
Buildings (net)	1,200	220	280
Equipment	360	100	75
Accounts payable	480	60	60
Long-term liabilities	1,140	340	300
Common stock	1,200	80	
Retained earnings	1,080	480	

[QUESTION]
REFER TO: Ref. 02_08
81. Assuming the combination is accounted for as a purchase, what amount will be reported for goodwill?
A) $35.
B) $(5).
C) $110.
D) $70.
E) $150.
Answer: D

Difficulty: Hard

[QUESTION]
REFER TO: Ref. 02_08
82. Assuming the combination is accounted for as an acquisition, what amount will be reported for goodwill?
A) $55.
B) $65.
C) $70.
D) $135.
E) $175.
Answer: A
Difficulty: Hard

[QUESTION]
REFER TO: Ref. 02_08
83. What amount will be reported for consolidated receivables?
A) $660.
B) $640.
C) $500.
D) $460.
E) $480.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
84. What amount will be reported for consolidated inventory?
A) $960.
B) $920.
C) $700.
D) $620.
E) $660.
Answer: A
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
85. What amount will be reported for consolidated buildings (net)?
A) $1,420.
B) $1,260.
C) $1,140.
D) $1,480.
E) $1,200.
Answer: D
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
86. What amount will be reported for consolidated equipment (net)?
A) $385.

B) $335.
C) $435.
D) $460.
E) $360.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
87. What amount will be reported for consolidated long-term liabilities?
A) $1,480.
B) $1,440.
C) $1,180.
D) $1,100.
E) $1,520.
Answer: B
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
88. What amount will be reported for consolidated common stock?
A) $1,200.
B) $1,280.
C) $1,400.
D) $1,480.
E) $1,390.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
89. Assuming the combination is accounted for as a purchase, what amount will be reported for consolidated retained earnings?
A) $1,830.
B) $1,350.
C) $1,080.
D) $1,560.
E) $1,535.
Answer: C
Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
90. Assuming the combination is accounted for as an acquisition, what amount will be reported for consolidated retained earnings?
A) $1,065.
B) $1,080.
C) $1,525.
D) $1,535.
E) $1,560.
Answer: A

Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_08
91. What amount will be reported for consolidated additional paid-in capital?
A) $165.
B) $150.
C) $160.
D) $175.
E) $145.
Answer: B
Difficulty: Hard

[QUESTION]
REFER TO: Ref. 02_08
92. What amount will be reported for consolidated cash after the purchase transaction?
A) $900.
B) $875.
C) $955.
D) $980.
E) $555.
Answer: E
Difficulty: Medium

Essay

[QUESTION]
93. What term is used to refer to a business combination in which only one of the original companies continues to exist?
Answer: The appropriate term is *statutory merger*.
Difficulty: Medium

[QUESTION]
94. Dutch Co. has loaned $90,000 to its subsidiary, Hans Corp., which retains separate incorporation. How would this loan be treated on a consolidated balance sheet?
Answer: The loan represents an intercompany payable and receivable, and it would be eliminated in preparing a consolidated balance sheet.
Difficulty: Medium

[QUESTION]
95. How are stock issuance costs accounted for in a business combination that is not a pooling of interests?
Answer: Stock issuance costs reduce the balance in Additional Paid-In Capital in a business combination that is not a pooling of interests.
Difficulty: Medium

[QUESTION]
96. How are direct combination costs accounted for in a purchase transaction?
Answer: In a purchase, direct combination costs are treated as part of the cost of the investment.
Difficulty: Medium

[QUESTION]
97. How are direct combination costs accounted for in an acquisition transaction?
Answer: In an acquisition, direct combination costs are expensed in the period of the acquisition.
Difficulty: Medium

[QUESTION]
98. Peterman Co. owns 55% of Samson Co. Under what circumstances would Peterman not be required to prepare consolidated financial statements?
Answer: Peterman would not be required to prepare consolidated financial statements if control of Samson is temporary or if, despite majority ownership, Peterman does not have control over Samson. A lack of control might exist if Samson is in a country that imposes restrictions on Peterman's actions.
Difficulty: Medium

[QUESTION]
99. How would you account for in-process research and development purchased in a business combination?
Answer: In-Process Research and Development is evaluated and if it has no alternative future use, then it is expensed immediately. Otherwise, it is capitalized as an asset of the combination.
Difficulty: Medium

[QUESTION]
100. How would you account for in-process research and development acquired in a business combination accounted for as an acquisition?
Answer: In-Process Research and Development is capitalized as an asset of the combination and reported as intangible assets with indefinite lives subject to impairment reviews.
Difficulty: Medium

[QUESTION]
101. Elon Corp. purchased all of the common stock of Finley Co., paying slightly less than the fair value of Finley's net assets. How should the difference between the purchase price and the fair value be treated if the transaction is treated as a purchase?
Answer: The difference between the purchase price and the fair value is used to reduce the balances in long-term assets (except for long-term investments).
Difficulty: Medium

[QUESTION]
102. Elon Corp. obtained all of the common stock of Finley Co., paying slightly less than the fair value of Finley's net assets acquired. How should the difference between the consideration transferred and the fair value of the net assets be treated if the transaction is accounted for as an acquisition?
Answer: The difference between the consideration transferred and the fair value of the net assets acquired is recognized as a gain on bargain purchase.
Difficulty: Medium

[QUESTION]
103. For purchase accounting, why are assets and liabilities of the subsidiary consolidated at fair value?
Answer: A purchase is considered to be the acquisition of one company by another. The acquisition of an asset or a group of assets is generally recorded at fair value. The purchase is assumed to occur through a bargained exchange that establishes an acquisition price. Because the

assets and liabilities are being purchased, they should be recorded at fair value as of the date of the purchase.
Difficulty: Medium

[QUESTION]
104. Goodwill is often created, or purchased, during a business combination. Why doesn't Goodwill show up on the Parent company's trial balance as a separate account?
Answer: While the Goodwill does not show up on the Parent company's books, it is implied as part of the account called Investment in Subsidiary. During the consolidation process, the Investment account is broken down into its component parts. Goodwill, along with other items such as subsidiary fair value adjustments, is then shown separately as part of the consolidated financial statement balances.
Difficulty: Medium

[QUESTION]
105. What are the three departures from SFAS 141 according to SFAS 141(R) *Business Combinations*?
Answer: The acquisition method embraces a fair value concept as measured by the fair value of consideration transferred as opposed to a cost-based measure. This requires three departures: (1) Direct combination costs are expensed as incurred (and not considered a part of the investment cost); (2) Contingent consideration obligations are recognized as part of the purchase price; and (3) When a bargain purchase occurs, the acquirer measures and recognizes the fair values of each of the assets acquired and liabilities assumed at the date of the combination, and as a result no assets or liabilities are recorded at amounts below their assessed fair values as under SFAS 141. A gain on the bargain purchase is recognized at the acquisition date.
Difficulty: Medium

[QUESTION]
106. How is contingent consideration accounted for according to SFAS 141(R) *Business Combinations*?
Answer: The fair value approach of the acquisition method views contingent payments as part of the consideration transferred. Under this view, contingencies have a value to those who receive the consideration and represent measurable obligations of the acquirer. The amount of the contingent consideration is measured as the expected present value of a potential payment and increases the investment cost.
Difficulty: Medium

[QUESTION]
107. How are bargain purchases different between SFAS 141 and SFAS 141(R) *Business Combinations*?
Answer: Under SFAS 141 (the purchase method), a bargain purchase reduces long-term assets, excluding long-term investments, utilizing the relative fair value method. Those reductions may reduce those assets to a value of zero, and any remaining bargain is considered an extraordinary gain. Under SFAS 141(R), *Business Combinations* (the acquisition method), the assets and liabilities acquired are recorded at their fair values and a bargain purchase is recorded as a Gain on Bargain Purchase.
Difficulty: Medium

[QUESTION]
108. Describe the accounting for direct costs, indirect costs, and issuance costs under: (1) The pooling-of-interests method; (2) The purchase method; and (3) The acquisition method.

Answer: (1) All costs of the combination were expensed under the pooling-of-interests method. (2) Direct costs are considered an increase in the investment, indirect costs are expensed, and issuance costs reduce the otherwise fair value of the securities issued (additional paid-in capital for stock issued or debt for debt issued) under the purchase method. (3) Direct and indirect combination costs are expensed and issuance costs reduce the otherwise fair value of the consideration issued under the acquisition method.
Difficulty: Medium

[QUESTION]
109. Bale Co. acquired Silo Inc. on October 1, 20X1, in a business combination transaction. Bale's net income for the year was $1,400,000, while Silo had net income of $400,000 earned evenly during the year. There was no goodwill and there were no other allocations.
Required:
What is consolidated net income for 20X1?
Answer:

Bale's net income for 20X1	$1,400,000
Silo's net income for three months ($400,000 x ¼ year)	100,000
Consolidated net income for 20X1	$1,500,000

Difficulty: Medium

[QUESTION]
96. What is the difference in consolidated results between a business combination whereby the acquired company is dissolved, and a business combination whereby separate incorporation is maintained?
Answer: There is no difference in consolidated results.
Difficulty: Easy

[QUESTION]
111. Fine Co. issued its common stock in exchange for the common stock of Dandy Corp. in a business combination that was neither a pooling of interests nor a bargain purchase. At the date of the combination, Fine had land with a book value of $480,000 and a fair value of $620,000. Dandy had land with a book value of $170,000 and a fair value of $190,000.
Required:
If a consolidated balance sheet was prepared at the date of the combination, what was the consolidated balance for Land?
Answer:

Book value of Fine Co.'s land	$480,000
Fair value of Dandy Corp.'s land	190,000
Consolidated balance for land	$670,000

Difficulty: Medium

[QUESTION]
112. Lorne Co. issued its common stock in exchange for the common stock of Fenn Corp. in a combination accounted for as a pooling of interests. At the date of the combination, Lorne had land with a book value of $700,000 and a fair value of $980,000. Fenn had land with a book value of $280,000 and a fair value of $250,000. The purchase was not a bargain purchase.
Required:
If a consolidated balance sheet was prepared at the date of the combination, what was the

consolidated balance for Land?
Answer:

Book value of Lorne Co.'s land	$700,000
Book value of Fenn Corp.'s land	280,000
Consolidated balance for land	$980,000

Difficulty: Medium

[QUESTION]
113. Jernigan Corp. had the following account balances at 12/31/X1:

Receivables	$ 96,000
Inventory	240,000
Land	720,000
Building	600,000
Liabilities	480,000
Common stock	120,000
Additional paid-in capital	120,000
Retained earnings, 1/1/0X1	840,000
Revenues	360,000
Expenses	264,000

Several of Jernigan's accounts have fair values that differ from book value: Land — $480,000; Building — $720,000; Inventory — $336,000; and Liabilities — $396,000.
Inglewood Inc. obtained all of the outstanding common shares of Jernigan by issuing 20,000 shares of common stock having a $6 par value, but a $66 fair value. Stock issuance costs amounted to $12,000.
Required:
Prepare a fair value allocation and goodwill schedule at the date of the combination.
Answer:

Valuation basis (20,000 shares x $66)		$1,320,000
Book value		($1,176,000)
Price in excess of book value		$ 144,000
Allocations to specific accounts based on the difference between fair value and book value:		
Inventory	$ 96,000	
Land	(240,000)	
Building	120,000	
Liabilities	84,000	(60,000)
Goodwill		$ 84,000

Difficulty: Medium

REFERENCE: Ref. 02_09
Salem Co. had the following account balances as of February 1, 2008:

Inventory	$ 720,000
Land	600,000
Buildings — net (valued at $1,200,000)	1,080,000
Common stock ($10 par value)	960,000
Retained earnings, January 1, 2008	1,320,000
Revenues	720,000
Expenses	600,000

Bellington Inc. paid $1.7 million in cash and issued 12,000 shares of its $30 par value common stock (valued at $90 per share) for all of Salem's outstanding common stock. This investment is accounted for using the purchase method.

[QUESTION]
REFER TO: 02_09
114. Determine the balance for Goodwill that would be included in a February 1, 2008, consolidation.
Answer:

Purchase price (fair value):		
Cash	$ 1,700,000	
Stock issued (12,000 shares x $90)	1,080,000	$ 2,780,000
Book value of assets (no liabilities are indicated)		(2,400,000)
Cost in excess of book value		$ 380,000
Excess cost assigned to the Buildings account based on fair value		(120,000)
Goodwill		$ 260,000

Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_09
115. Assume that Bellington paid cash of $2.8 million. No stock is issued. An additional $50,000 is paid in direct combination costs.
Required:
For Goodwill, determine what balance would be included in a February 1, 2008 consolidation.
Answer:

Purchase price (includes combination costs)	$ 2,850,000
Book value of assets (no liabilities are indicated)	(2,400,000)
Cost in excess of book value	$ 450,000
Excess cost assigned to the Buildings account based on fair value	(120,000)
Goodwill	$ 330,000

Difficulty: Medium

[QUESTION]
116. On January 1, 2010, Chester Inc. acquires 100% of Festus Corp.'s outstanding common

stock by exchanging 37,500 shares of Chester's $2 par value common voting stock. On January 1, 2010, Chester's voting common stock had a fair value of $40 per share. Festus' voting common shares were selling for $6.50 per share. Festus' balances on the acquisition date, just prior to acquisition are listed below. Chester is accounting for the investment in Festus using the acquisition method.

	Book Value	Fair Value
Cash	$ 30,000	
Accounts Receivable	120,000	$ 120,000
Inventory	200,000	230,000
Land	230,000	290,000
Building (net)	450,000	600,000
Equipment (net)	175,000	160,000
Accounts Payable	(80,000)	(80,000)
Common Stock, $1 par	(500,000)	
Paid-in Capital	(350,000)	
Retained Earnings, 12/31/09	(275,000)	

Required:
Compute the value of the Goodwill account on the date of acquisition, 1/1/10.
Answer:

Fair value of consideration transferred	$ 1,500,000
Less: BV of Festus' net assets	1,125,000
Cost in excess of Book Value to be allocated	$ 375,000
Inventory	(30,000)
Land	(60,000)
Building	(150,000)
Equipment	15,000
Goodwill	$ 150,000

Difficulty: Medium

REFERENCE: Ref. 02_10
The financial statements for Jode Inc. and Lakely Corp., just prior to their combination, for the year ending December 31, 2009, follow. Lakely's buildings were undervalued on its financial records by $60,000.

	Jode Inc.	Lakely Corp.
Revenues	$ 1,300,000	$ 500,000
Expenses	(1,180,000)	(290,000)
Net income	$ 120,000	$ 210,000
Retained earnings, January 1, 2009	$ 700,000	$ 500,000
Net income (from above)	120,000	210,000
Dividends paid	(110,000)	(110,000)
Retained earnings, December 31, 2009	$ 710,000	$ 600,000
Cash	$ 160,000	$ 120,000
Receivables and inventory	240,000	240,000
Buildings (net)	700,000	350,000
Equipment (net)	700,000	600,000
Total assets	$ 1,800,000	$ 1,310,000
Liabilities	$ 250,000	$ 195,000
Common stock	750,000	430,000
Additional paid-in capital	90,000	85,000
Retained earnings, 12/31/09	710,000	600,000
Total liabilities and stockholders' equity	$ 1,800,000	$ 1,310,000

On December 31, 2009, Jode issued 54,000 new shares of its $10 par value stock to the owners of Lakely in exchange for all of the outstanding shares of that company. Jode's shares had a fair value on that date of $35 per share. Jode paid $34,000 to an investment bank for assisting in the arrangements. Jode also paid $24,000 in stock issuance costs. This combination is accounted for as an acquisition.

[QUESTION]
REFER TO: Ref. 02_10
117. Prepare the journal entries to record (1) the issuance of stock by Jode and (2) the payment of the combination costs.
Answer:
Entry One – To record the issuance of common stock by Jode to execute the purchase.

Investment in Lakely Corp.	1,890,000	
Common Stock (par value)		540,000
Paid-in Capital		1,350,000

Entry Two – To record the combination costs.

Investment in Lakely Corp. (Combination costs)	34,000	
Paid-in Capital	24,000	
Cash		58,000

Commented [ILP2]: I can't edit picture. Need to delete text in first line from "Investment…" and insert "Professional fee expense"

Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_10
118. *Required:*
Determine consolidated Net Income for at December 31, 2009.
Answer:

Consolidated Net Income	
Jode's Revenues	$ 1,300,000
Jode's Expenses	(1,180,000)
Consolidated net income	$120,000

Note: In a purchase, the subsidiary's revenues and expenses *prior to the date of acquisition are NOT consolidated.*

Difficulty: Medium

[QUESTION]
REFER TO: Ref. 02_10
119. Determine consolidated Paid-in Capital at December 31, 2009.
Answer:

Consolidated Paid-in Capital:	
Jode's Paid-in Capital prior to the date of acquisition	$ 90,000
Additional Paid-in Capital arising from the transaction (54,000 shares issued × $25 per share in excess of par value)	1,350,000
Less: Stock issuance costs	(24,000)
Consolidated Paid-in Capital	$1,416,000

Difficulty: Medium

[QUESTION]
120. The following are preliminary financial statements for Black Co. and Blue Co. for the year ending December 31, 2008.

	Black Co.	Blue Co.
Sales	$360,000	$228,000
Expenses	(240,000)	(132,000)
Net income	$120,000	$ 96,000
Retained earning, January 1, 2008	$480,000	$252,000
Net income (from above)	120,000	96,000
Dividends paid	(36,000)	-0-
Retained earnings, December 31, 2008	$564,000	$348,000
Current assets	$360,000	$120,000
Land	120,000	108,000
Building (net)	480,000	336,000
Total assets	$960,000	$564,000
Liabilities	$108,000	$132,000
Common stock	192,000	72,000
Additional paid-in capital	96,000	12,000
Retained earnings, December 31,2008	564,000	348,000
Total liabilities and stockholders' equity	$960,000	564,000

On December 31, 2008 (subsequent to the preceding statements), Black exchanged 10,000 shares of its $10 par value common stock for all of the outstanding shares of Blue. Black's stock on that

date has a fair value of $60 per share. Black was willing to issue 10,000 shares of stock because Blue's land was appraised at $204,000. Black also paid $14,000 to several attorneys and accountants who assisted in creating this combination.
Required:
Assuming that these two companies retained their separate legal identities, prepare a consolidation worksheet as of December 31, 2008 assuming the transaction is treated as a purchase combination.
Answer:
Purchase Consolidation Worksheet

For the Year Ended 12/31/2008

	Black	Blue	Consolidation Entries		Consolidated
Account	Company	Company	Dr.	Cr.	Balance
Income Statement					
Sales	(360,000)				(360,000)
Expenses	240,000				240,000
Net Income	(120,000)				(120,000)
Statement of Retained Earnings					
R/E, 1/1/08	(480,000)				(480,000)
Net Income	(120,000)				(120,000)
Dividends	36,000				36,000
R/E, 12/31/08	(564,000)				(564,000)
Balance Sheet					
Current assets	346,000	120,000			466,000
Investment in Blue Co.	614,000			(S) 432,000 (A) 182,000	0
Land	120,000	108,000	(A) 96,000		324,000
Buildings (net)	480,000	336,000			816,000
Goodwill			(A) 86,000		86,000
Total Assets	1,560,000	564,000			1,692,000
Liabilities	(108,000)	(132,000)			(240,000)
Common Stock	(292,000)	(72,000)	(S) 72,000		(292,000)
Additional Paid-in Capital	(596,000)	(12,000)	(S) 12,000		(596,000)
R/E, 12/31/08	(564,000)	(348,000)	(S) 348,000		(564,000)
Total Liabilities & Stockholders' Equity	(1,560,000)	(564,000)	614,000	614,000	(1,692,000)

Calculation of Goodwill:

Purchase price paid by Black Co.	614,000	
Book value of Blue Co.	(432,000)	(Entry S)
Excess of Cost over Book Value	182,000	(Entry A)
Allocations:		
Land (204,000 - 108,000)	(96,000)	(Entry A)
Excess cost not identified - Goodwill	86,000	(Entry A)

Adjustment to Book Values on Black Co's books for purchase:

			Adjusted Balances @ 12/31/08
Investment in Blue Co. (purchase price)	614,000		614,000
Common Stock - Black (10,000 x $10 Par)		100,000	292,000
Add'l Paid-in Capital - Black (10,000 x $50)		500,000	596,000
Cash (paid for direct acquisition costs)		14,000	346,000

Entry S:

Common Stock	72,000	
Additional Paid-in Capital	12,000	
Retained Earnings - 12/31/08	348,000	
Investment in Blue Co.		432,000

To eliminate Blue Co's stockholders' equity accounts and the book value of Blue Co's net assets from Black Co's investment account

Entry A:

Land	96,000	
Goodwill	86,000	
Investment in Blue Co.		182,000

To eliminate Black Co's excess payment over book value from its investment account, which should be zero, and reassign the excess to specific assets and goodwill

Difficulty: Hard

[QUESTION]
121. The following are preliminary financial statements for Black Co. and Blue Co. for the year ending December 31, 2009.

	Black Co.	Blue Co.
Sales	$360,000	$228,000
Expenses	(240,000)	(132,000)
Net income	$120,000	$ 96,000
Retained earning, January 1, 2009	$480,000	$252,000
Net income (from above)	120,000	96,000
Dividends paid	(36,000)	-0-
Retained earnings, December 31, 2009	$564,000	$348,000
Current assets	$360,000	$120,000
Land	120,000	108,000
Building (net)	480,000	336,000
Total assets	$960,000	$564,000
Liabilities	$108,000	$132,000
Common stock	192,000	72,000
Additional paid-in capital	96,000	12,000
Retained earnings, December 31,2009	564,000	348,000

Total liabilities and stockholders' equity	$960,000	564,000

On December 31, 2009 (subsequent to the preceding statements), Black exchanged 10,000 shares of its $10 par value common stock for all of the outstanding shares of Blue. Black's stock on that date has a fair value of $60 per share. Black was willing to issue 10,000 shares of stock because Blue's land was appraised at $204,000. Black also paid $14,000 to several attorneys and accountants who assisted in creating this combination.

Required:

Assuming that these two companies retained their separate legal identities, prepare a consolidation worksheet as of December 31, 2009 assuming the transaction is treated as an acquisition combination.

Answer:

Acquisition Consolidation Worksheet

For the Year Ended 12/31/2009

Account	Black Company	Blue Company	Consolidation Entries Dr.	Consolidation Entries Cr.	Consolidated Balance
Income Statement					
Sales	(360,000)				(360,000)
Expenses	254,000				254,000
Net Income	(106,000)				(106,000)
Statement of Retained Earnings					
R/E, 1/1/09	(480,000)				(480,000)
Net Income	(106,000)				(106,000)
Dividends	36,000				36,000
R/E, 12/31/09	(550,000)				(550,000)
Balance Sheet					
Current assets	346,000	120,000			466,000
Investment in Blue Co.	600,000			(S) 432,000 (A) 168,000	0
Land	120,000	108,000	(A) 96,000		324,000
Buildings (net)	480,000	336,000			816,000
Goodwill			(A) 72,000		72,000
Total Assets	1,546,000	564,000			1,678,000
Liabilities	(108,000)	(132,000)			(240,000)
Common Stock	(292,000)	(72,000)	(S) 72,000		(292,000)
Additional Paid-in Capital	(596,000)	(12,000)	(S) 12,000		(596,000)
R/E, 12/31/09	(550,000)	(348,000)	(S) 348,000		(550,000)
Total Liabilities & Stockholders' Equity	(1,546,000)	(564,000)	600,000	600,000	(1,678,000)

Calculation of Goodwill:

Consideration transferred by Black Co.	600,000	
Book value of Blue Co.	(432,000)	(Entry S)
Excess of consideration transferred over Book Value	168,000	(Entry A)
Allocations:		
Land (204,000 - 108,000)	(96,000)	(Entry A)
Excess cost not identified - Goodwill	72,000	(Entry A)

Adjustment to Book Values on Black Co's books for acquisition:

			Adjusted Balances @ 12/31/08
Professional fee expense	**14,000**		254,000
Investment in Blue Co. (purchase price)	600,000		600,000
Common Stock - Black (10,000 x $10 Par)		100,000	292,000
Add'l Paid-in Capital - Black (10,000 x $50)		500,000	596,000
Cash (paid for direct acquisition costs)		14,000	346,000

Entry S:

Common Stock	72,000	
Additional Paid-in Capital	12,000	
Retained Earnings - 12/31/09	348,000	
Investment in Blue Co.		432,000

To eliminate Blue Co's stockholders' equity accounts and the book value of Blue Co's net assets from Black Co's investment account

Entry A:

Land	96,000	
Goodwill	72,000	
Investment in Blue Co.		182,000

To eliminate Black Co's excess payment over book value from its investment account, which should be zero, and reassign the excess to specific assets and goodwill

Difficulty: Hard

[QUESTION]
122. How are direct and indirect costs accounted for when applying the acquisition method?

	Direct Costs	Indirect Costs
A.	Expensed	Expensed
B.	Increase investment account	Decrease additional paid-in capital
C.	Expensed	Decrease additional paid-in capital
D.	Increase investment account	Expensed
E.	Increase investment account	Increase investment account

Answer: A
Difficulty: Easy

[QUESTION]
123. For each of the following situations, select the best answer concerning accounting for combinations:
(A) Pooling-of-interests method only.
(B) Purchase method only.
(C) Acquisition method only.
(D) Pooling-of-interests method and purchase method, but not acquisition method.
(E) Purchase method and acquisition method, but not pooling-of-interests method.
(F) Pooling-of-interests method and acquisition method, but not purchase method.
(G) All methods (pooling-of-interests, purchase, and acquisition.)

(H) None of the methods (neither pooling-of-interests, purchase, nor acquisition.)

_____1. Direct costs are expensed.
_____2. Indirect costs are expensed.
_____3. Direct costs reduce the additional paid-in capital of the acquirer.
_____4. Both direct costs and indirect costs increase the investment account.
_____5. Direct costs increase the investment account, and stock issue costs reduce the acquirer's additional paid-in capital account.
_____6. Contingent consideration increases the investment account at date of acquisition.
_____7. Contingent consideration increases the investment account at a date subsequent to the acquisition date.
_____ 8. A bargain purchase reduces the fair value of long-term assets.
_____9. A bargain purchase is ignored or not applicable.
_____10. A bargain purchase is recorded at date of acquisition as a gain (not extraordinary).
_____11. The combination clearly defines an acquired company and an acquiring company.
_____12. Method(s) appropriate to combinations prior to June 30, 2001.
Answer: (1) F; (2) G; (3) H; (4) H; (5) B; (6) C; (7) B; (8) B; (9) A; (10) C; (11) E; (12) D
Difficulty: Medium