Beechy, Conrod & Farrell *Intermediate Accounting* Fifth Edition, Volume 2 – Test Bank
Chapter 12 – Liabilities

1. Conceptually, liabilities constitute a present obligation as a result of a past event.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

2. Under IFRS, only legal obligations are recognized.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

3. A reasonable expectation on the part of a company's stakeholders arising from a company's past practices or behaviour may constitute a constructive obligation in certain instances.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

4. A contingency may become a provision if the likelihood of the contingent event greatly increases.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO2

5. For a small population, the best estimate for the amount of a provision that must be recognized is the expected value of the possible outcomes.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO2

6. For a large population, the best estimate for the amount of a provision that must be recognized is the most likely outcome with respect to the expected value and cumulative probabilities.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO2

7. Discounting is not required when the time value of money is immaterial or if the amount and timing of cash flows is highly uncertain.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO2

8. For a small population, the best estimate for the amount of a provision that must be recognized is the expected value of the possible outcomes.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO2

9. Contingencies must be both accrued and disclosed.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO2

10. Under proposed changes to current standards, amounts currently classified as contingencies may need to be accrued rather than simply disclosed.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO2

11. An onerous contract is one where the unavoidable costs of meeting the contract may or may not exceed the benefits derived from the contract.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO2, 3

12. A lawsuit in progress wherein the defendant will probably be found guilty would likely be accounted for as a provision.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO3

13. Warranties provisions may arise from legal or constructive obligations.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4

14. Once a company has formally decided to restructure its operations, a provision must be made for the restructuring.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO3

15. Loyalty points are provided (accrued) for and reversed once the points are redeemed.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO3

16. Self-insurance costs for expected losses must never be provided for.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO3

17. Current liabilities are usually discounted.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO3

18. The carrying value of a bond from the issuing corporation's standpoint will always move closer to its face value, regardless of whether the bond is issued at a premium or a discount.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4

19. Under the effective interest method, interest expense is calculated by multiplying the market interest rate by the carrying value of the bonds.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4

20. Assume that a company issues bonds at a discount. Under the effective interest method, the company will record progressively less interest with the passage of time.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4

21. Transaction costs are usually included in the carrying value of any financial liabilities.

    Ans: True

    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4

22. Long-term financial liabilities will usually be carried at amortized cost.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

23. Adjustments to fair value relating to FVTPL liabilities will always flow through earnings.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

24. Loan guarantees must be provided for; the amount of the provision is the probability of payout multiplied by the fair value o the loan guarantee.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

25. When the market rate exceeds the stated or nominal rate, a bond's carrying value will be less than its fair value.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4, 5

26. The stated rate of interest is the interest rate used to determine the amount of cash interest that will be paid on the principal.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4, 5

27. A short-term payable may be the current portion of a long-term liability, which arises when the next payment on such a debt will be made out of current assets.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4, 5

28. Interest may be recognized on a note even though the note does not explicitly state an interest rate.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4, 5

29. The principal amount of a debt is the cash or cash equivalent amount borrowed.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4, 5

30. A company may reclassify a current financial liability to a long-term one only if there is a contractual agreement in place by the reporting date to replace the financing.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4, 5

31. Debt issue costs may be expensed or included in the cost of the debt.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4, 5

32. An administrative fee pertaining to a successful loan application is to be immediately expensed.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4, 5

33. An administrative fee pertaining to an unsuccessful loan application is to be immediately expensed.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO4, 5

34. Capitalization of borrowing costs on qualifying assets will continue even if work on the asset has temporarily ceased.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6

35. Accounts payable should include only obligations directly related to the primary and continuing operations of an entity.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO1, 2

36. Capitalization of borrowing costs on qualifying assets is mandatory under both IFRS and ASPE.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6, 10

37. Use of the effective interest method for amortizing bond premiums and discounts is mandatory under IFRS but not under ASPE.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6, 10

38. Borrowing costs can only be capitalized on non-financial assets.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6

39. The cost of any equity financing is included when calculating the cost of generalized borrowings.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6

40. Bonds are said to be redeemable when they can be prematurely retired at the discretion of the issuing company and retractable when they can be prematurely retired at the investor's discretion.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO7

41. Under IRS, a loss contingency must be credited to a liability account only if the occurrence of the contingent event is probable and if the amount of loss can be reasonably estimated.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO1, 3, 10

42. A gain contingency will usually not be recorded in the accounts and reported in the financial statements even though its occurrence is probable.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO1, 3

43. Under ASPE, disclosure in the footnotes to the financial statements is the only way to properly report contingent losses.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO1, 3, 10

44. When the maturity date of a bond issue is within one year or the operating cycle (whichever is longer) of the current balance sheet date, the bond liability should be reclassified as a current liability (assuming the payment will be made out of current assets).

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

45. Callable bonds are callable at the option of the investor.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

46. A $1,000, 6%, 10-year bond purchased as a long-term investment at an effective rate at 7%, will pay the investor $70 cash interest each year.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

47. When bonds are sold at a discount, interest-method amortization results in a schedule of interest accruals, which increase in amount as maturity approaches.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO4

48. In-substance defeasance means that a debtor irrevocably places cash or other monetary assets in a trust fund to pay interest on an outstanding debt. In such situations, the debt is always recorded as paid when the trust fund is set up.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO7

49. Hedging is one method of minimizing foreign exchange risk.

Ans: True

Difficulty: Easy
Level of Learning: Knowledge
Topic: LO8

50. Under IFRS, a continuity schedule must be provided for both provisions and contingencies.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO9, 10

51. (Appendix) Blended payments are payments where the interest rate is fixed at the beginning of the loan term and there are regular equal payments of principal and interest made.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO11, 12

52. A brewing company operating in an Ontario city experiencing water shortages received its water bill for December 1999, on December 31, 1999. The bill ($8,000) represents the cost of water used in December to make its product. The company will not publish the 1999 financial statements until February 2000. Therefore, the adjusting entry as of December 31, 1999 includes which of the following?
A) cr. utilities payable $8,000
B) cr. cash $8,000
C) cr. utilities expense $8,000
D) no adjusting entry needed because the bill will not be paid until January 2000

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO1

53. Bonds payable (due 5 years from the balance sheet date) should be classified as follows:
A) A contingent liability.
B) An element of the owners' equity.
C) A long-term liability.
D) A current liability.

Ans: C
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO4

54. A short-term note payable may include all of the following except:
A) Trade notes payable.
B) Nontrade notes payable.
C) A current portion of a long-term liability.
D) Unearned revenue.

Ans: D
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO1, 9

55. Which of the following statements is/are correct?
    A) Under IFRS, contingencies may be accrued, but not under ASPE.
    B) Litigation for which the company will probably be found guilty would normally be accrued as a provision.
    C) Under IFRS, contingencies should be disclosed but not accrued.
    D) Both B & C are correct.

    Ans: D
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1

56. A firm sold $100,000 worth of goods during 1999. The firm extends warranty coverage on these goods. Historically, warranty costs have averaged 2% of total sales. During 1999, the firm incurred $1,000 to service goods sold in 1998 and $200 to service goods sold in 1999. What is warranty expense for 1999?
    A) $200
    B) $1,200
    C) $2,000
    D) $3,200

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO1

57. You are an investor and have just purchased a bond on July 1 which pays interest every March 1 and September 1. When you receive your first interest cheque, you will receive and have earned how many months interest?

	Received	**Earned**
1	6	6
2	6	2
3	2	2
4	4	4
5	6	4

    A) Choice 1
    B) Choice 2
    C) Choice 3
    D) Choice 4
    E) Choice 5

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO5

58. On November 7, 1999 local residents sued Brimley Corporation for excess chemical emissions that caused some of them to seek medical attention. The total lawsuit is $8,000,000. Brimley Corporation's lawyers believe that the lawsuit will be successful and that the amount to be paid to the residents will be $4,000,000. On its December 31, 1999 financial statements Brimley should:
A) Accrue a provision loss of $8,000,000 with no financial statement disclosure necessary.
B) Accrue a provision loss of $4,000,000 and note disclose.
C) Do nothing as the lawsuit has not yet ended.
D) Simply disclose the details regarding the lawsuit in a note.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO1, 3

59. AB sold its 10-year bond at a discount. In reporting the bonds and the related discount on a balance sheet shortly thereafter, the discount should be:
A) Added to the bonds.
B) Recorded as expense in the period of sale.
C) Reported as a deferred charge.
D) Deducted from the bonds payable.

Ans: D
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO4, 5

60. JMR bought 15 Z Corporation $1,000 bonds for $15,270 total, on April 1, 2000, (five years prior to maturity). The bonds pay 8% annual interest on April 1 and October 1. On December 31, 2000, the bonds had a market value of $14,950 (not a permanent decline). JMR purchased these bonds at:
A) Par.
B) Par plus accrued interest.
C) A premium.
D) A discount.
E) A discount plus accrued interest.

Ans: C
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO4, 5

61. R Company was indebted to A Inc. at January 1, 2000. The note called for a $25,000 payment to be made on December 31, 2000 and also on December 31, 2001. The note was non-interest bearing yet 10% was the prevailing rate at the time the note was issued. What is the book value of the note on R's January 1, 2000 balance sheet?
A) $47,727
B) $47,500
C) $43,389
D) $50,000
E) $38,962

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

62. $5,000 (face value) of bonds with a book value of $4,300 was retired 4 years and 9 months prior to maturity. The dollar amount (excluding interest) paid to retire the bonds was $4,700. The entry to record the retirement would include:
A) dr. bonds payable $5,000
B) cr. cash $4,300
C) dr. bonds payable $4,700
D) cr. unusual gain $400

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

63. ABC Inc has 50 pending lawsuits for which it may be found liable. The expected value (sum of the probabilities of the outcomes multiplied by their respective payouts) amounts to $100,000. However, the company's controller believes that the most likely outcome will be a payout of $120,000. Which of the following statements pertaining to the accrual of the provision is correct?

A) There is a large population of lawsuits, so a provision of $100,000 must be accrued.
B) There is a large population of lawsuits, so a provision of $120,000 must be accrued.
C) There is a small population of lawsuits, so a provision of $100,000 must be accrued.
D) There is a small population of lawsuits, so a provision of $120,000 must be accrued.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO3

64. ER issued for $2,060,000, two thousand of its 9%, $1,000 callable bonds. The bonds are dated January 1, 1999, and mature many years from now. Interest is payable semi-annually on January 1 and July 1. The bonds can be called by the issuer at 102 on any interest payment date after December 31, 2003. The unamortized bond premium was $28,000 at December 31, 2001, and the market price of the bonds was 99 on this date. In its December 31, 2001, balance sheet, at what amount should GC report the carrying value of the bonds?
A) $1,980,000
B) $2,028,000
C) $2,032,000
D) $2,040,000
E) Cannot answer; the bond term is not given

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

65. Gains or losses from the early extinguishment of debt, if material, should be:
A) recognized in income as ordinary gains and losses or as unusual items.
B) recognized as an extraordinary item in the period of extinguishment.
C) amortized over the remaining original life of the extinguished issue.
D) amortized over the life of the new issue.

Ans: A
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO4, 5

66. All of the following are true with respect to sinking funds except:
A) A sinking fund is a cash fund that is restricted for retiring the debt of a company.
B) A sinking fund may be handled by a trustee or by the individual company.
C) A sinking fund may make the investment more attractive to investors.
D) Once the sinking fund is established, the company has no more responsibility to the debt.

Ans: D
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO4, 5

67. Which one of the following items is not a liability?
    A) Accrued estimated warranty costs
    B) Dividends payable in shares
    C) Advances from customers on contracts
    D) The portion of long-term debt due within one year

    Ans: B
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1

68. Proposed changes to the IFRS definition of a liability include:
    A) The addition of the requirement that a liability relate to a past event.
    B) The removal of the requirement that a liability relate to a past event.
    C) The addition of the requirement that a liability be a present obligation.
    D) The addition of the requirement that a liability be a legal obligation.

    Ans: B
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1

69. The rate of interest specified on the face of the debt is called the:
    A) Effective interest rate.
    B) Stated interest rate.
    C) Yield interest rate.
    D) Market interest rate.

    Ans: B
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO4, 5

70. The rate of interest used to discount the future cash payments on a debt to the cash equivalent borrowed is least likely to be described by which of the following terms:
    A) Effective interest rate.
    B) Yield interest rate.
    C) Stated interest rate.
    D) Prevailing interest rate.

    Ans: C
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO4, 5

71. A company has commenced work on a non-cancellable fixed price construction contract in the amount of $6 million. Costs of $4 million have been incurred to date, and it is expected that $3.2 million in additional costs will have to be incurred to complete the contract. The company adheres to IFRS. Which of the following statements with respect to the contract are correct?
    A) There is a constructive obligation to finish the contract.
    B) The company will have recognized $3 million in profit on the contract to date.
    C) The company has a constructive obligation to accrue a loss of $1.2 million plus any previously recognized profit.
    D) This is an onerous contract, so the company must accrue a loss of $1.2 million plus any previously recognized profit.

    Ans: D
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

72. Constructive obligations may arise from:
    A) Asset retirement obligations
    B) Warranty obligations.
    C) Notes Payable
    D) Both A & B

    Ans: D
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

73. A company is being sued by a competitor for $120,000. The company's legal team estimates that there is a 20% chance that the company will be sued. Under the PROPOSED changes to current IFRS standards,
    A) No provision or note disclosure will be required.
    B) A provision of $24,000 will be required.
    C) A provision of $96,000 will be required.
    D) A provision of $120,000 will be required.

    Ans: B
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

74. Long-term obligations (i.e., debts) that is callable for early payment:
   A) Must continue to be classified as a long-term liability by the debtor, if a provision of the debt covenant has been violated.
   B) Must continue to be classified as a long-term liability in all situations.
   C) Must be reported as current liabilities by the debtor if callable on demand.
   D) Can be reported as current liabilities by the debtor only if callable because a provision of the debt covenant has been violated.

   Ans: C
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO4, 5

75. A company had sales of $1 million. Coupons in the amount of $1 per $10 in sales were given to paying customers. History has shown that 50% of all coupons are redeemed. Which of the following statements is correct?
   A) A provision for $50,000 must be recognized.
   B) A provision for $100,000 must be recognized.
   C) A provision for $1 million must be recognized.
   D) No provision is necessary.

   Ans: A
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO1, 3

76. By law, a fleet of aircraft must be subject to a major overhaul every 5 years as part of its scheduled maintenance program. Which of the following statements is correct?
   A) An accrual should be made in each of the 5 years preceding the overhaul.
   B) The costs of the overhaul should be expensed as incurred.
   C) The cost of the overhaul should be deferred and amortized.
   D) The estimated cost of the overhaul should be disclosed as part of a continuity schedule in the notes to the financial statements.

   Ans: C
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO1, 3

77. Which of the following statements is/are correct?
    A) For companies that are self-insured, a provision must be established for events taking place prior to the reporting period but not for loss events that have happened during the year but are not yet known.
    B) For companies that are self-insured, a provision must be established for events taking place prior to the reporting period and for loss events that have happened during the year but are not yet known.
    C) Contingent assets are only recorded when it is virtually certain that the benefits relating to the contingent assets will be received.
    D) Both A & C are correct.
    E) Both B & C are correct.

    Ans: E
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

78. Information obtained prior to the issuance of the current period's financial statements of KG Company indicates that it is probable that, at the date of the financial statements, a liability will be incurred for obligations related to product warranties on products sold during the current period. During the past three years, product warranty costs have been approximately 1 1/2 percent of annual sales revenue. An estimated loss contingency should be:
    A) Neither accrued nor disclosed in the financial statements.
    B) Recognized as an appropriation of retained earnings.
    C) Accrued in the accounts and reported in the financial statements.
    D) Disclosed in the financial statements but not accrued.

    Ans: C
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

79. Contingent liabilities will or will not become actual liabilities depending on:
    A) Whether they are probable and estimable
    B) The degree of uncertainty
    C) The present condition suggesting a liability
    D) The outcome of a future event

    Ans: D
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

80. Under IFRS, which of the following will only require only a note disclosure as a contingency?
    A) Cash discounts given for early payment by customers; almost always taken
    B) Remote chance of loss from a lawsuit in process
    C) Probable claim for an income tax refund
    D) Loss from an investment in equity securities that is certain

    Ans: B

    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

81. (Appendix) A Bank requires a client to maintain a certain debt-to-equity ratio, or else the client's loan will become immediately repayable. This is an example of a(an):
    A) Debt covenant.
    B) Indenture.
    C) Contingency.
    D) Retraction.

    Ans: A
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO13

82. Which of the following contingencies should be accrued in the accounts and reported in the financial statements?
    A) The estimated expenses of a one-year product warranty
    B) The company is forcefully contesting a personal injury suit and a loss is possible and reasonably estimable
    C) An accommodation endorsement involving a remote loss
    D) It is probable that the company will receive $50,000 in settlement of a lawsuit

    Ans: A
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

83. KR Corporation was involved in a lawsuit with the Government alleging inadequate air pollution control facilities at its Glowworm plant site during 1999. At December 31, 2002, it appeared probable the Government would settle for approximately $150,000. This event should be recorded (i.e., recognized) in 2002 as a(n):
    A) Loss on the lawsuit (operating expense).
    B) Unusual gain.
    C) Prior period adjustment.
    D) Unusual loss.
    E) Disclosure of contingency loss only in a note.

    Ans: A

    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO1, 3

84. Under IFRS, interest paid should be recorded on the Statement of Cash Flows as a(an):
    A) Operating activity.
    B) Financing Activity.
    C) Investing Activity
    D) A or B

    Ans: D
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO4, 5

85. On January 1, 2000, DWW borrowed $400,000 cash and signed a one-year, 12 percent interest-bearing note payable. Assuming a 40 percent average income tax rate for DWW Corporation, the net effective interest rate on this note was:
    A) 4.8 percent.
    B) 6.0 percent.
    C) 7.2 percent.
    D) 12.0 percent.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4, 5

86. XYZ borrowed $60,000 for one year and signed an 18 percent, interest-bearing note payable. Assuming XYZ has an income tax rate of 45 percent, the net effective rate was:
A) 8.1 percent.
B) 9.9 percent.
C) 11.7 percent.
D) 18 percent.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

87. On September 1, 1999, Company B signed a $7,392, two-year non-interest-bearing note payable in full on August 31, 2001. Company B received $6,000 cash. What was the yield or effective rate of interest?
A) 11 percent
B) 14 percent
C) 18 percent
D) 23 percent

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

88. VCR Company owed a $73,311 debt due on January 1, 2000. An agreement was reached to pay it off in three equal annual payments of $30,000 each, starting on December 31, 2002. The interest rate was 11 percent. The balance in the liability account of VCR Company on January 1, 2002 is:
A) $27,027
B) $51,875
C) $73,321
D) $90,000

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

89. XY Company owed a $45,489 due on January 1, 2000. An agreement was reached to pay it off in five equal annual payments, starting on December 31, 2000. The interest rate was 10 percent. The total amount of interest paid under the terms of the agreement was (round annual payment to nearest $1):
A) $25,000
B) $22,745
C) $14,511
D) $ 6,000

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

90. A firm sells products covered by a three-year warranty. From the past experience of the other firms in the industry, the firm expects to incur warranty costs equal to 1% of sales. Firm sales were $40,000 and $50,000 in 1999 and 2000 respectively. In 2000, the firm spent $200 to repair goods sold in 1999, and $300 to repair goods sold in 2000. The firm received no warranty servicing demands from customers in 1999, the firm's first year of operations. What is the balance in the warranty liability account on January 1, 2001?
A) $400
B) $500
C) $300
D) $0

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO1, 3

91. On January 1, 2000, JG purchased a machine and gave a $30,000 three-year, 8% note. The market or "going" interest rate was 12%. The annual interest payments are to be paid on each December 31. On January 1, 2000, JG should record the net liability amount determined as follows:
A) Compute the present value of its face amount and the three $2,400 interest amounts by using a discount rate of 8%.
B) Compute the present value of its face amount and the three $2,400 interest amounts by using a discount rate of 12%.
C) Use its face amount, $30,000 plus the $7,200 interest.
D) Use its face amount, $30,000 minus $7,200 interest.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

92. KR issued bonds payable with a face amount of $200,000 and a maturity date ten years from date of issuance. If the bonds were issued at a premium, this indicated that:
    A) The effective and stated rates were the same.
    B) The stated rate of interest exceeded the effective rate.
    C) The stated rate and the market rate were the same.
    D) No necessary relationship exists between the two rates.
    E) The effective rate of interest exceeded the stated (nominal) rate.

    Ans: B
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO4, 5

93. In theory (disregarding any other marketplace variables) the proceeds from the sale of a bond will be equal to:
    A) The face amount of the bond plus the present value of the interest payments made during the life of the bond discounted at the prevailing market rate of interest.
    B) The sum of the face amount of the bond and the periodic interest payments.
    C) The present value of the principal amount due at the end of the life of the bond plus the present value of the interest payments made during the life of the bond, each discounted at the stated rate of interest.
    D) The present value of the principal amount due at the end of the life of the bond plus the present value of the interest payments made during the life of the bond, each discounted at the prevailing market rate of interest.

    Ans: D
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4, 5

94. AB Company sold and issued a $100,000, 10%, bond at 99. Therefore, the bond:
    A) was sold at a premium because the stated interest rate was higher than the yield rate.
    B) sold at a discount because the stated interest rate was lower than the market interest rate.
    C) sold at a premium because the $1,000 accrued interest is added to the $100,000 face amount.
    D) was sold for $100,000 less $1,000 of accrued interest.

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4, 5

95. For bonds payable, the cash interest paid in each interest period is:
    A) The same amount regardless of whether the bond was sold at par, a discount, or a premium.
    B) Different depending upon the date of sale.
    C) Not the same amount when the stated and yield interest rates are different.
    D) Dependent on the initial amount of accrued interest.

    Ans: A
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4, 5

96. Straight-line amortization of bond premium or discount:
    A) Can be used as an optional method of amortization in all situations.
    B) Provides the same amounts of interest expense and interest revenue each interest period as the effective interest method.
    C) Provides the same total amount of interest expense and interest revenue as the effective interest method over the life of the bonds.
    D) is appropriate when the bond term is especially long.
    E) is appropriate for deep discount bonds.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4, 5

97. If a bond was sold at 108, the stated rate of interest was:
    A) Equal to market rate.
    B) Not related to market rate.
    C) Higher than market rate.
    D) Lower than market rate.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4, 5

98. Bond A and Bond B both have a maturity value of $1,000 and pay annual interest of 9%. The market rate of interest is also 9%. Bond A matures in 4 years and Bond B matures in 5 years. Which of the following is correct?
A) Both bonds sell for more than $1,000.
B) Bond A will sell for more than Bond B.
C) Both bonds sell for the same amount, $1,000.
D) Bond B will sell for more than Bond A.
E) There is not sufficient information to answer the question.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

99. Bonds payable should be reported as a long-term liability in the balance sheet of the issuer at:
A) Current market price.
B) lower-of-cost-or-market.
C) Issue price, excluding any accrued interest at purchase date.
D) Issue price less any unamortized bond premium or plus any unamortized discount.
E) Issue price plus any unamortized bond premium or less any unamortized discount.

Ans: E
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

100. When the interest payment dates of a bond are May 31 and November 30, and a bond issue is sold on July 1, the amount of cash received by the issuer will be:
A) Decreased by accrued interest from July 1 to November 30.
B) Decreased by accrued interest from May 31 to July 1.
C) Increased by accrued interest from May 31 to July 1.
D) Increased by accrued interest from July 1 to November 30.
E) Unaffected by accrued interest.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

101. When the interest payment dates of a bond are May 31 and November 30, and a bond issue is sold on July 1, the price of the bond will be:
   A) Decreased by accrued interest from July 1 to November 30.
   B) Decreased by accrued interest from May 31 to July 1.
   C) Increased by accrued interest from May 31 to July 1.
   D) Increased by accrued interest from July 1 to November 30.
   E) Unaffected by accrued interest.

   Ans: E
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO4, 5

102. A firm retired a long-term note by in-substance defeasance. This me
   A) the creditors have been paid
   B) the debtor has been released of its legal responsibility for all remaining debt payments
   C) there is only a remote chance that the debtor will be required to make further payments on the liability
   D) the debt is shown as an offset against the assets used to retire the debt, in the debtor's balance sheet
   E) the debtor will continue to recognize interest expense on the debt but will make no more payments

   Ans: C
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO 5

103. There are two methods for amortizing premiums and discounts on the sale of bonds. The differences between the two methods are:
   A) Both methods charge a constant amount of interest to the financial statements each year; however, the effective interest method charges a larger total amount of interest expense over the life of the bond.
   B) The effective interest method charges a different interest expense each year while the straight-line method results in a different amount of annual interest expense as a percentage of beginning book value each year.
   C) There are no differences between the two
   D) None of these answers is correct

   Ans: B
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO4

104. In-substance defeasance is sometimes used as a method of bond retirement. Choose the correct statement about this practice.
    A) The bonds are legally retired as a result
    B) The firm may invest in any investment-grade debt security to retire the bonds as long as the investment securities are transferred irrevocably to a trustee
    C) Neither the assets used to effect the defeasance, nor the bonds themselves, are reported in the balance sheet, even though the bonds remain outstanding
    D) The process may require the company which issued the bonds to make substantial payments in addition to the investments purchased for the defeasance

    Ans: C
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO5

105. Which of the following is not one of the conditions that must be met to qualify as extinguishment of debt by in-substance defeasance?
    A) Trust must own monetary assets that are essentially risk free.
    B) Cash inflows into the trust must approximately coincide with required cash outflows.
    C) There is a reasonable possibility that the debtor will be called on to make additional payments on the debt.
    D) The qualifying assets must not be used for trustee fees.

    Ans: C
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO5

106. The result of an effective interest rate that is higher than the stated rate on a debt security is the:
    A) Carrying value of the debt will decrease each interest period.
    B) Security will sell at a premium.
    C) Cash interest paid on each interest date will be changed.
    D) Dollar amount of interest expense reported on the income statement, assuming the interest method is used, will increase each interest period.

    Ans: D
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO4, 5

107. Which of the following statements is true?
   A) If a bond is sold "at a discount," the effective interest rate on the bond is lower than the stated interest rate.
   B) If a bond is sold between interest dates, it is necessary to record the interest accrued since the last payment date before sale.
   C) If a bond is sold "at a premium," the effective interest rate on the bond is higher than the stated interest rate.
   D) Bond price of 98 means that the yield rate is 98% of the stated rate.

   Ans: B
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO4, 5

108. If bonds are issued initially at a discount and the straight-line method of amortization is used for the discount, interest expense in the earlier years will be:
   A) less than if the interest method is used.
   B) less than the amount of the interest payments.
   C) more than if the interest method is used.
   D) The same as if the interest method is used.

   Ans: C
   Difficulty: Medium
   Level of Learning: Knowledge
   Topic: LO4, 5

109. VB owes a $200,000, 8%, five-year note payable dated January 1, 2000. It is the end of year 2000, and instead of making the interest payment now due, VB has made arrangements to pay the debt and the 2000 interest payment in four equal instalments based on the same interest rate. The first payment is to be made on January 1, 2001. The amount of the equal annual payments is (rounded to the nearest dollar):
   A) $54,000
   B) $60,384
   C) $55,912
   D) $65,214

   Ans: B
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO4, 5

110. On January 1, 2000, ER signed a $120,000, 10%, three-year, note payable. The proceeds are to be used to purchase a computer and related software for the company. The lending institution advanced proceeds of $115,800 and took a mortgage on the computer. The note is payable in three equal annual instalments starting on December 31, 2000. The effective interest rate to use for this debt is (rounded to the nearest percent; do not interpolate):
A) 10%.
B) 11%.
C) 12%.
D) 13%.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

111. On November 1, 1999, WC purchased CX, 10-year, 7%, bonds with a face value of $100,000 for $96,000. The bonds are intended to be held to maturity. An additional $2,333 was paid for the accrued interest. Interest is payable semi-annually on January 1 and July 1. The bonds mature on July 1, 2006. WC uses the straight-line method of amortization. Ignoring income taxes, the amount of interest revenue reported in WC's 1999 income statement (year-end December 31) as a result of WC's long-term bond investment in CX was:
A) $1,267
B) $1,167
C) $1,120
D) $1,067

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

112. On March 1, 2000, WC issued 10% stated interest rate, 10 year debentures dated January 1, 2000, in the face amount of $1,000,000, with interest payable on January 1 and July 1. The debentures were sold to yield 12% plus accrued interest. How much should WC debit to cash on March 1, 2000?
A) $ 901,963
B) $ 903,003
C) $1,016,667
D) $1,033,333
E) $ 902,336

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

113. On September 1, 2000, ER issued 11%, 10 year bonds dated June 1, 2000, in the face amount of $140,000, with interest payable July 1 and December 31. The bonds were sold for $140,000. How much should ER debit to cash on September 1, 2000?
A) $140,000
B) $142,567
C) $147,700
D) Cannot be determined from the information given

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO4, 5

114. Which of the following is true with respect to bond retirement?
A) If interest rates increase, the issuer can retire bonds at a gain by buying them on the open market.
B) Gains and losses on bond retirements may be classified as ordinary gains and losses or unusual gains and losses.
C) On debt retirement all related accounts should be update.
D) All of these answers are correct.

Ans: D
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 5

115. Ryan Company borrow $45,000 US when the exchange rate for US $1.00 is Cdn. $1.46. When the debt was repaid the exchange rate changes to US $1.00 = Cdn. $1.38. Ryan Company records the amount on the date of exchange as:
A) A foreign exchange loss of $3,600
B) A foreign exchange gain of $3,600
C) A foreign exchange gain of $62,100
D) A foreign exchange loss of $62,100

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO8

116. ASPE and IFRS differ in their treatment of long-term Bonds Payable in that:
    A) Under IFRS, exchange gains and losses on short-term debt are recorded in the income statement immediately.
    B) The straight-line method may be used under ASPE but not under IFRS..
    C) ASPE ignores foreign exchanges gains and losses.
    D) IFRS does not account for foreign exchange gains and losses on Bonds Payable.

Ans: B
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO4, 10

117. Which of the following is not a required disclosure for Bonds Payable under IFRS?
    A) Interest rate risk.
    B) Credit risk.
    C) Transaction risk.
    D) Liquidity risk.

Ans: C
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO9

118. On January 1, 1999, a company borrowed $20,000 on a 10% interest-bearing note, due on December 31, 2001. The interest is payable each December 31.

(a) The principal amount of the note is	$__________
(b) The face amount of the note is	$__________
(c) The maturity amount of the note is	$__________
(d) Total cash interest expense for the three years is	$__________
(e) The balance in the note payable account on January 1, 1999 is	$__________
(f) The balance in the note payable account on December 31, 19x2 is	$__________

Ans: (a) $20,000, (b) $20,000, (c) $20,000, (d) $6,000, (e) $20,000, (f) $20,000
Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

119. A company has been sued for damages as a result of illness caused to local residents due to the emission of highly toxic chemicals from its plant. The company's legal firm advises that it is probable that the company will lose the suit and that it probably will result in a judgment of $2 million to $10 million in damages. However, the legal firm believes that the most probable amount of the loss will be $6 million, and that the suit will be terminated about three years hence. The company has no other lawsuits pending.

(a) Should the company disclose this event in the year the suit was filed? (check one)_____ No; _____ Note only; _____ A loss in the income statement.
(b) If a loss should be reported, give the journal entry required:

Ans: (a) a loss in the income statement.,

(b) Loss-pollution (lawsuit pending)	6,000,000	
Estimated liability pollution lawsuit		6,000,000

Difficulty: Hard
Level of Learning: Application
Topic: LO3

120. A firm issued a 16%, $1,000 bond issued and dated Jan. 1/2000 maturing Jan. 1, 2011 paying interest each June 30 and December 31, and yielding 14%. One bond is used for simplicity.
Required:
(a)Determine the price of the bond
(b)All Year 2000 entries and balance sheet presentations for the bond after each interest date in Year A. Show the interest method and straight-line methods in parallel fashion.
Ans:

(a)Price = $1,000(PV1,7%,20)(.25842) + $80(PVA,7%,20)(10.59401)
= $1,105.94

(b)		Interest	SL
Jan. 1/00	Cash	1,105.94	
	(both methods)	Bond premium	105.94
		Bonds payable	1,000.00

Balance sheet disclosure Jan. 1/00 (both methods)

Bonds payable	$1,000.00	
Bond premium	105.94	
Book value of bonds		$1,105.94

		Interest	SL
June 30/00	Interest expense	77.42	74.70
	Bond premium	2.58	5.30
	Cash	80.00	80.00

77.42 = $1,105.94(.07) 5.30 = $105.94/20

Balance sheet disclosure June 30/00

Bonds payable	$1,000.00	$1,000.00
Premium	103.36	100.64
Book value of bonds	$1,103.36	$1,100.64

Dec. 31/00 Interest expense	77.24	74.70	
	Bond premium	2.76	5.30
	Cash	80.00	80.00

77.24 = $1,103.36(.07) 5.30 = $105.94/20

Balance sheet disclosure Dec. 31/00

Bonds payable	$1,000.00	$1,000.00
Premium	100.60	95.34
Book value of bonds	$1,100.60	$1,095.34

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

121. JV issued $10,000, 10% bonds payable (interest payable annually), which mature at the end of six years from issue date. The effective rate of interest at issue date was 12%. The sale price of the bonds was: $_________________.

Ans:

$10,000 x PV1, 12%, 6 (.50663)	=	$5,066
$1,000 x PVA, 12%, 6 (4.11141)	=	4,111
		9,177

Difficulty: Hard

Level of Learning: Application

Topic: LO4, 5

122. Match the "Characteristic" with the "Designation" by entering appropriate letters to the left.

Characteristic

A. Bonds supported by a lien (mortgage) on specific assets.

B. The entire bond issue matures at a single date.

C. The investor has the option to turn in the bonds and receive in exchange other specified securities.

D. Issuer has the option to retire them at a stated price before the obligatory maturity date.

Designation

___ 1. Ordinary bonds

___ 2. Convertible bonds

___ 3. Callable bonds

___ 4. Secured bonds

Ans: 1:B, 2:C, 3:D, 4:A

Difficulty: Hard

Level of Learning: Application

Topic: LO4, 5

123. RX issued $1,000,000, 10% bonds payable (interest payable annually), which mature at the end of five years from issue date. The effective rate of interest at issuance was 8%. The sale price of the bonds was: $_________________.

Ans:

$1,000,000 x PV1, 8%, 5 (.68058)=	$ 680,580
$100,000 x PVA, 8%, 5 (3.99271)=	399,271
Total	$ 1,079,851
	=========

Difficulty: Hard

Level of Learning: Application

Topic: LO4, 5

124. A retail store has completed certain transactions that management believes may have caused current liabilities. Indicate by check mark whether the following items should be classified as current liabilities. Assume a December 31 year-end.

	Classified as a Current Liability		
Items	**Yes**	**No**	**Unknown**
(a) Dividend issuable in stock of the company.	___	___	___
(b) Interest for January through March, which is not payable until July 1 next year.	___	___	___
(c) Amounts withheld in January for income tax from employee pay cheques; amount not yet remitted.	___	___	___
(d) Bonds maturing in 11 months from the financial statement date for which inadequate sinking fund exists.	___	___	___
(e) Obligation to service warranted (one year) products sold with store's private label.	___	___	___
(f) Obligation on gift certificates redeemable during the upcoming year.	___	___	___
(g) Shipping cost for goods sold, in transit, shipped f.o.b. point of shipment.	___	___	___

Ans: (a) No, (b) Yes, (c) Yes, (d) No, (e) Yes, (f) Yes, (g) No
Difficulty: Hard
Level of Learning: Application
Topic: LO1

125. At the end of the current reporting period, a company which adheres to ASPE is involved in a number of contingencies. The company seeks your advice as to how each contingency should be recorded and reported. Below are listed four "Requirements for Recording and Reporting" and six "Contingencies." Match each situation with one appropriate requirement code.
Requirements for Recording and Reporting:
Code
A = Record with entry
B = Disclosure note required
C = Disclosure note permitted
D = Disclosure not recommended
Contingencies:
___ 1. The company has substantial assets in a foreign country and their expropriation is reasonably possible; the amount of the loss can be estimated reliably.
___ 2. The company is the defendant in a lawsuit wherein the plaintiff seeks damages; a loss is remote, however, if it does occur its amount can be estimated reliably.
___ 3. The company is the plaintiff in a lawsuit seeking damages; a gain is remote and the amount of the gain, should it occur, cannot be estimated reliably.
___ 4. The company is the defendant in a lawsuit wherein the plaintiff seeks damages; a loss is likely but the amount of it cannot be estimated reliably.
___ 5. The company gives a two-year warranty on all goods sold; the warranty cost can be estimated reliably.
___ 6. The company is the plaintiff in a lawsuit seeking damages; a gain is likely and the amount can be estimated reliably.

Ans: 1: B, 2: C, 3: D, 4: B, 5: A, 6: B
Difficulty: Hard
Level of Learning: Application
Topic: LO2, 3

126. Indicate the correct financial statement treatment of each of the three situations listed below by entering the identifying letter in the space provided.
Financial Statement
A. Report as a current or long-term liability.
B. Must report as a note to the financial statements.
C. May report in a note to the financial statements.
Situations
___ 1. Short term obligation estimated amount.
___ 2. Probable obligation estimated amount.
___ 3. Short term obligation known amount.
___ 4. Probable obligation known amount.
___ 5. Reasonably possible obligation known amount.
___ 6. Reasonably possible obligation unknown amount.
___ 7. Remote obligation unknown amount.
___ 8. Remote obligation known amount.

Ans: 1:A, 2:A, 3:A, 4:A, 5:B, 6:B, 7:C, 8:C

Difficulty: Hard
Level of Learning: Application
Topic: LO2 3

127. Use the identifying letters which appear below to classify the items listed.

Classification

A. Contingent liability
B. Current liability
C. Long-term liability
D. Owners' equity
E. None of these.

Items

___ 1. Premium on bonds payable.
___ 2. Dividends payable in stock of the company.
___ 3. Accounts receivable assigned.
___ 4. Income tax withheld from employees' salaries.
___ 5. Revenue collected in advance.
___ 6. Estimated premium claims payable (in connection with sales promotion offer involving redemption of proof of purchase premiums).
___ 7. Estimated income tax payable.

Ans: 1:C, 2:D, 3:E, 4:B, 5:B, 6:B, 7:B
Difficulty: Hard
Level of Learning: Application
Topic: LO1-8

128. Match each of the following items with its appropriate financial statement classification by entering letters in the spaces provided.

Classification

A. Current liability
B. Long-term liability
C. Contingent liability
D. Owners' equity
E. None of these.

Items

___ 1. Sales taxes collected.
___ 2. Deferred repairs.
___ 3. Cash dividends payable.
___ 4. Appropriated retained earnings for bond sinking fund.
___ 5. Accrued wages.
___ 6. Bonds payable.
___ 7. Stock dividends issuable.
___ 8. Unearned rent revenue.
___ 9. Notes Payable (due in 6 months) discounted.
___ 10. Premium on bonds payable.

Ans: 1:A, 2:A, 3:A, 4:D, 5:A, 6:B, 7:D, 8:A, 9:A, 10:B
Difficulty: Hard
Level of Learning: Application
Topic: LO1-8

129. Classify each of the items listed below by entering the appropriate letter. Assume that IFRS is adhered t.

Classification

A. Contingent liability
B. Current liability
C. Long-term liability
D. Owners' equity
E. Provision

Items

___ 1. Unearned rent revenue.
___ 2. Deferred interest revenue.
___ 3. Accrued wages.
___ 4. Cash dividends payable.
___ 5. Bonds payable (due in five years).
___ 6. Accommodation endorsement (probable and estimable).
___ 7. Stock dividend issuable.
___ 8. Estimated taxes payable.

Ans: 1:B, 2:B, 3:B, 4:B, 5:C, 6:E, 7:D, 8:B
Difficulty: Hard
Level of Learning: Application
Topic: LO1-8

130. On January 1, 2000, a company purchased a machine that had a list price of $23,500. The purchase terms agreed upon were: cash down payment $12,000 plus a 15% note payable of $9,132 (its present value). The note is payable in three equal annual instalments (interest plus principal) on each December 31. Round to the nearest dollar.
Required:
(a)Give the entry to record the acquisition of the machine.
(b)Give the adjusting entry required on September 30, 20x2, for interest assuming this is the end of the accounting period.
Ans:

(a) Machine	21,132	
Cash		12,000
Note payable		9,132
(b) Interest expense	731	
Interest payable (975 x 9/12)		731

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

131. On January 1, 2000, a corporation purchased a machine (10 year estimated useful life; no residual value; straight-line method) by paying cash $1,500 and signing a note payable with a face amount of $4,500, 8% interest payable each December 31. The maturity date is December 31, 2002. The going market rate of interest was 10%. Give all required entry (entries) at each of the following dates:
January 1, 2000:
December 31, 2000:
Ans: January 1, 2000:

Machine ($1,500 + $4,276)	5,776
Cash (given)	1,500
Note payable (net)*	4,276

* principal $4,500 x (PV1, 10%, 3) (.75131)	3,381
* Interest $ 360 x (PVA, 10%, 3) (2.48685)	895
	4,276
	=====

December 31, 2000:

Depreciation expense ($5,776 ÷ 10 years)	578	
Accumulated depreciation		578
Interest expense ($4,276 x .10)	428	
Cash ($4,500 x .08)		360
Note payable ($428 - 360)		68

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

132. On January 1, 1999, a company incurred a debt of $11,663, which is payable in four equal annual instalments of $3,600, starting on December 31, 1999.
(a)The implicit interest rate is _______% (rounded to the nearest percent).
(b)Give the journal entry to record the second annual payment (on December 31, 2000).
Ans: (a) Implicit interest rate: 9%
$11,663 ÷ $3,600 = 3.23972, PVA for n = 4 shows 9%
(b) December 31, 2000

Liability	2,780	
Interest expense	820	
Cash		3,600

Date	Cash	Interest Expense	Principal Reduction	Principal Balance
Jan. 1/99	$11,663			
Dec.31/99	$ 3,600	$ 11,663 x.09 = $ 1,050	$3,600 - 1,050 = $ 2,550	9,113
Dec.31/00	3,600	9,113 x.09 = 820	3,600 – 820 = 2,780	6,333

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

133. X owed a debt dated January 1, 2000, amounting to $91,330. Arrangements were made to pay the debt in three equal annual instalments, starting on December 31, 2000. The interest is 15% per annum.
(a)Compute the amount of the annual cash payment to be made on each December 31.
Payment $______________.
(b)Prepare the related debt amortization schedule for the term of the debt.
Ans:
(a)$91,330 ÷ (PVA, 15%, 3) (2.28323)= $40,000
======

(b)

Date	Cash –	Interest Expense (15%)	=	Principal Reduction	Principal Balance
Jan. 1/00					$91,330
Dec.31/00	40,000	13,700		26,300	65,030
Dec.31/01	40,000	9,755		30,245	34,785
Dec.31/02	40,000	5,218		34,782*	

*$3 difference due to rounding
Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

134. On September 1, 2000, a company signed a $19,800, one-year, non-interest-bearing note payable and received $18,000 cash.
(a)What was the yield rate of interest?_________
(b)Give the entry required at September 1, 2000, in the accounts of the company (use the net method).
(c)Give the adjusting entry required at the end of the accounting year for the company (December 31, 2000).
(d)Give the entry required on the due date, August 31, 2001, assuming no reversing entries were made.

Ans: (a) $19,800 - $18,000 = $1,800 ÷ $18,000 = 10%

(b)September 1, 2000		
Cash	18,000	
Note payable		18,000
(c)December 31, 2000:		
Interest expense ($1,800 x 4/12)	600	
Note payable		600
(d)August 31, 2001:		
Note payable	18,600	
Interest expense ($1,800 x 8/12)	1,200	
Cash		19,800

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

135. On September 1, 2000, a company purchased a machine and paid for it by signing a two-year noninterest-bearing note, face $4,000. The note is payable August 31, 2002. The going rate of interest was 18% per year. The accounting period ends December 31.
(a) Compute the cost of the machine.
(b) Give all appropriate entries throughout the term of the note.
Use the net method.

Ans: (a) $4,000 x (PV1, 18%, 2) (.71818) = $2,873
(b) September 1, 2000

Machine	2,873	
Note payable		2,873
December 31, 2000		
Interest expense ($2,873 x .18 x 4/12)	172	
Note payable		172
December 31, 2001		
Interest expense	548*	
Note payable		548
August 31, 2002		
Note payable ($2,873 + $172 + $548)	3,593	
Interest expense ($4,000 - $3,593)	407	
Cash		4,000
*$2,873 x .18 = $517 x 8/12	=	$345
or ($2,873 + $172) x .18	=	$548
		====
($2,873 + $517) x .18 = $610 x 4/12	=	203
$548		

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

136. On September 1, 2000, a company signed a $6,540, one-year, non-interest-bearing note payable and received $6,000 cash.
(a)What was the imputed rate of interest?______________ % .
(b)Give the entry required at September 1, 2000, to record the receipt of the cash (record on net basis).
(c)Give the adjusting entry required at the end of the accounting year, December 31, 2000.
(d)Give the entry required on the due date, August 31, 2001, assuming no reversing entries were made.

Ans: (a) $6,540 - $6,000 = $540 ÷ $6,000 = 9%

(b) September 1, 2000		
Cash	6,000	
Note payable		6,000
(c) December 31, 2000		
Interest expense ($540 x 4/12)	180	
Note payable		180
(d) Note payable ($6,000 + $180)	6,180	
Interest expense ($540 x 8/12)		360
Cash		6,540

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

137. Quality 9000 International Inc., which began operations in 1996, sells 20,000 units of its product each year under the following warranty: defective units will be fixed free of charge during the calendar year of purchase and the next two calendar years. (This means it is best to buy from this company early in the year.) Only 1% of units sold have required warranty service in the past. The average cost has been $200 per unit for servicing. Units require service only once and the likelihood of a unit requiring service is the same during each year in the warranty period. What is the balance in the warranty liability account at December 31, 1999?

Ans: As of Dec. 31/99, the warranty for 1996, 1997 units is expired;
Dec. 31/99 liability =

For 1998 sales: 1/3(20,000)($200)(.01)	=	$13,333
For 1999 sales: 2/3(20,000)($200)(.01)	=	26,667
Total liability at Dec. 31/99		$40,000
		======

Difficulty: Hard
Level of Learning: Application
Topic: LO2

138. A firm sells a remarkable product, which serves many household purposes. The firm is confident about its product and is so anxious to sell a large number of units that it grants a 3-year warranty. The warranty agreement specifies that any malfunction or other problem will be fixed at no cost to the customer, unless the customer has abused the product. Based on experience with other household products it has sold in the past, 3% of total units sold will require service over the warranty period at an average cost of $200 per unit. The following information relates to the first two years of the product's life:

	Year 1	**Year 2**
Unit sales	20,000	5,000
Actual warranty costs incurred	$ 35,000	$ 80,000

What is the balance of the warranty liability account at January 1, Year 3? Assume that the company did not revise its estimate of future warranty claims frequency.

Ans: January 1, 20x3 warranty liability balance =
(20,000 + 25,000).03($200) - $35,000 - $80,000 = $155,000

Difficulty: Hard
Level of Learning: Application
Topic: LO3

139. At December 31, 1999 ABC Company has the following three separate lawsuits pending against it: Suit A-Plaintiffs seek damages of $40,000; Suit B-Plaintiff seeks damages of $200,000; and Suit C-Plaintiff seeks damages of $20,000.
ABC management and legal counsel have made the assessments indicated below. For each suit, taking into account the assessment, you are to (a) give the accrual entry if it is required (if not, state why) and (b) indicate whether a disclosure note is required and explain the reason.

CASE A-Remote that ABC will lose the suit.
(a) Accrual entry:
(b) Disclosure note: _______ Yes ______ No. Explanation:

CASE B-Reasonably possible that ABC will lose; reasonable estimate of damages $4,000.
(a) Accrual entry:
(b) Disclosure note: ______ Yes _______ No. Explanation:

CASE C-Probable that ABC will lose; reasonable estimate of damages $10,000.
(a) Accrual entry:
(b) Disclosure note: ______ Yes ______ No. Explanation:

Ans: **CASE A**
(a) None permitted for remote loss contingencies
(b) No (permissible but not required)

CASE B
(a) None
(b) Yes (required for reasonably possible loss contingencies)

CASE C

(a) Estimated loss-Damages from lawsuit	20,000	
Estimated liability-Damages from lawsuit		20,000

(b) Yes or no (Disclosure often required in addition to the journal entry) for full disclosure.

Difficulty: Hard
Level of Learning: Application
Topic: LO3

140. BRIEFLY explain how the treatment of contingencies differs under IFRS and ASPE.

Ans: Contingencies may or may not be accrued under ASPE but are never accrued under IFRS. Both IFRS and ASPE require the disclosure of contingencies.
Difficulty: Hard
Level of Learning: Application
Topic: LO3, 10

141. Match the following bond classifications with the appropriate statement by entering the appropriate letters in the spaces provided:

Bond Classifications

A. Government bonds
B. Corporate bonds
C. Serial bonds
D. Redeemable bonds
E. Convertible bonds
F. Callable bonds
G. Income bonds
H. Registered bonds
I. Coupon bonds

Statements

___ 1. Bonds that may be turned in to issuer in exchange for other securities.
___ 2. Issued by private companies.
___ 3. Interest is paid only to owners of record as reflected in the accounts of the issuer.
___ 4. Interest is paid only in years in which the issuer earns a profit.
___ 5. Investor has the option of turning in the bond for retirement before maturity date.
___ 6. Interest is paid only to investors who return a coupon.
___ 7. Issued by public entities.
___ 8. Principal paid off in steps (instalments).
___ 9. Issuer has the option to pay off the bonds before maturity date.

Ans: 1:E, 2:B, 3:H, 4:G, 5:D, 6:I, 7:A, 8:C, 9:F
Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

142. For each of the following, indicate the appropriate balance sheet classification by entering the applicable classification letter.

Classification

A. Current liability
B. Long-term liability
C. Contingent liability
D. Owners' equity
E. None of these

Item

___ 1. Premium on bonds payable
___ 2. Sales taxes collected
___ 3. Repairs expense payable
___ 4. Cash dividends payable
___ 5. Bond sinking fund
___ 6. Accrued wages payable
___ 7. Bonds payable
___ 8. Stock dividends declared
___ 9. Rent received in advance

Ans: 1:B, 2:A, 3:A, 4:A, 5:E, 6:A, 7:B, 8:D, 9:A
Difficulty: Hard
Level of Learning: Application
Topic: LO1-8

143. On September 1, 2000, XYZ borrowed $100,000 on a 9%, two-year, note payable. Simple interest is payable on August 31, 2001 and 2002. XYZ's reporting year ends December 31 and the company does not use reversing entries for interest. The required entry on August 31, 2001, is:

Ans:

Interest Expense	6,000	
Interest Payable	3,000	
Cash		9,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

144. A company wishes to finance a long-term construction project and in doing so, capitalize the related interest expense. The company requires $2 million in financing.

The company currently has the following debt and equity items on its December 31st, 2009 Balance Sheet:

Bonds Payable (8%, Issue at Par)	$1,000,000
Unsecured Line of Credit (6%)	$3,000,000
Common Shares (Par Value $100)	$1,000,000

There are 10,000 common shares outstanding which pay an annual dividend of $ 5 per share. The company can borrow a maximum of $5 million on its unsecured line of credit.

The company's bank has indicated its willingness to extend an additional credit facility in the amount of $1.5 million at an annual rate of 5% as of March 31st, Year 6. These amounts remained outstanding throughout Year 6.

On March 1st, Year 6 the company borrowed $600,000. On April 1st, Year 6, and additional $1.4 million was wired to the company's account, drawn on its new credit facility.

Determine the amount of interest that the company would be able to capitalize as per IFRS for Year 6.

Ans: The company requires $2 Million. $500,000 was drawn from the company's unsecured line of credit – a generalized borrowing. The remainder was drawn on the purpose-specific credit facility.

It is necessary to calculate the company's weighted average cost of capital for its general borrowings:

8%*$1 million + 6%*3 million =$260,000/ ($1 million + $3 million) = 6.5%.

The amount of interest to be capitalized would be adulated as follows:

Category	**Portion of Year**	**Weighted Avg Borrowings**	**Capitalized Interest**
General	10/12	$600,000*10/12=$500,000*6.5%	$32,500
Specific	9/12	$1.4 million*9/12=$1,050,000*5%	$52,500
Total			**$85,000**

Thus, $85,000 of interest would be capitalized.

The journal entry to reflect the capitalization of interest would be as follows:

Interest Expense	$85,000	
Construction-in-process		$85,000

Difficulty: Hard
Level of Learning: Application
Topic: LO6

145. On July 1, 2000, RC sold two of its $10,000, 9%, bonds payable at an effective interest rate of 8%. Interest is paid each June 30 and the bond matures in six years on June 30, 2006. Round all amounts to the nearest dollar.
(a)What was the amount of the premium $_____________ or discount $_______________________?
(b)The income statement for the accounting year ended December 31, 2000, should report interest expense of, assuming:
(1) Straight-line amortization, $_____________________.
(2) Interest-method amortization, $___________________.
Ans:

(a) $20,000 x PV1, 8%, 6 (.63017)	$2,60
$1,800 x PVA, 8%, 6 (4.62288)	8,321
Cost	20,924
Par	20,000
Premium	$924
	======

(b) Straight-line amortization: $823, interest expense
====
1,800 - ($924 ÷ 6 years = $154) = $1,646 x 6/12 = $823
(2) Interest-method amortization: $837, interest expense
====
$20,924 x 8% x 6/12 = $837
Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

146. It is often necessary to compute the book value of a bond issue several years into its term. Rather than compute an amortization schedule for the entire term, it is possible to directly compute the net bond liability at any interest date under either the interest method or straight-line method. Assume that $100,000 of 8% bonds were issued to yield 10% on January 1, 2000, the bond date. The bonds pay interest each December 31 and are scheduled to mature in ten years. Answer the following questions without producing an amortization schedule.
(a) What is the book value of the bonds on January 1, 2006 if the firm uses the straight-line method.
(b) What is the book value of the bonds on January 1, 2006 if the firm uses the interest (effective interest) method.
Ans: (a) Original issue price = $100,000(PV1,.10,10)(.38554) + $8,000(PVA,.10,10)(6.14457) = $87,711. Original discount = $12,289. At Jan. 1/06, 4 years of term are left so BV = $100,000 -.4($12,289) = $95,084.
(b) BV = 100,000(PV1,.10,4)(.68301) + $8,000(PVA,.10,4)(3.16987) = $93,660.
Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

147. A firm has two bonds outstanding today, each with: (1) $1,000 face value, (2) a term of 5 years at issuance, (3) 3 years remaining to maturity, and (4) 10% yield rate at issuance. Bond A is a zero coupon bond; bond B pays 10% annually and just paid interest yesterday. The yield rate today on both bonds is 12%. Which bond has experienced the greatest percentage change in value since issuance?

Ans: Bond A sold for 62: $1,000(PV1, .10, 5) (.62092).
Bond B sold for 100 as coupon and market rate were the same at issuance.
Market value of Bond A today = 71 = $1,000(PV1, .12, 3)(.71178).
Market value of Bond B today = 95 = $1,000(PV1, .12, 3) (.71178) + $100(PVA,.12,3)(2.40183)
Bond A has increased 15% = (71 - 62)/62
Bond B has decreased 5% = (100 - 95)/100 (generally the price of zeros is more volatile with interest rate changes)

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

148. On September 1, 2000, RC sold $10,000, 6% (payable semi-annually each March 1 and September 1), 10-year bonds dated September 1, 2000, to yield 8%. RC uses straight-line amortization. The accounting period ends December 31.

(a) The sale price of the bond was $________________.
(b) Interest expense for 2000, was $________________.

Ans: (a)

$10,000 x PV1, 4%, 20 (.45639)	=	$4,564
$300 x PVA, 4%, 20 (13.59033)	=	4,077
Sale price	=	$8,641
		======

(b)

$10,000 x 3% x 4/6	=	$200
$1,359 x 4/120	=	45
Interest expense	=	245
		====

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

149. (Appendix) Discuss some of the sources of short-term financing.

Ans: The answer should include the ability to use promissory notes as financing. These notes can be interest or non-interest bearing. Companies can approach the banks for an operating line of credit. Large companies can issue commercial paper. Companies can also sell their receivables to a finance company.

Difficulty: Hard
Level of Learning: Application
Topic: LO11

150. On January 1, 2000, a company purchased a machine (an operational asset) with a list price of $4,000. $2,000 was paid in cash and a three-year, noninterest-bearing note was signed. The note was for $3,000 and required payment of equal amounts of $1,000 each December 31, 2000, 2001, and 2002. The going rate of interest was 12%. Using this information, complete the following requirements.
(a) Give the entry on January 1, 2000, to record the purchase of the machine (show computations and round to the nearest dollar):
(b) Prepare the related debt amortization schedule.
(c) Give any adjusting entry related to the note payable required for 2001, assuming the accounting period ends March 31. If none is required, state the reason.
(d) Assuming that the accounting period ends March 31 and there were no reversing entries, give the entry to record the annual payment made on December 31, 2001.

Ans: (a)

January 1, 2000:

Machinery	4,402	
Cash		
Note payable		

______
*$1,000 x (PVA, 12%, 3) (2.40183) = 2,402

(b)

Date	Cash	Interest Expense	Principal Reduction	Principal Balance
Jan. 1/00			$ 2,402	
Dec.31/00	$ 1,000	288	712	1,690
Dec.31/01	1,000	203	797	893
Dec.31/02	1,000	107	893	-0-

(c) March 31, 2001

Interest expense ($203 x 3/12)	51	
Interest payable		51
(d) Interest expense ($203 x 9/12)	152	
Interest payable	51	
Note payable	797	
Cash		1,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

151. AB owes a $100,000, 8%, five-year note payable dated January 1, 2000. It is the end of year 2000, and instead of making the interest payment now due, AB has made arrangements to pay the debt and the 2000 interest payment, in four equal instalments based on the same interest rate. The first payment is to be made on January 1, 2001. The amount of the equal annual payments, rounded to the nearest dollar, is:
Ans: $100,000 + ($100,000 x .08) = $108,000 ÷ 3.57710 (PVAD, 8%, 4) =$30,192
Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

152. The management of PT authorized an issue of $120,000 bonds payable, 6% (annual interest rate), dated January 1, 2000. The bonds mature on December 31, 2005 (5 years). Interest is payable each June 30 and December 31. The bonds were sold on May 1, 2000, at an effective (yield) rate of 8%.
(a) The bonds were sold at a____________ premium; ____________discount (check one).
(b) Give the entry for PT to record the sale of the bonds on May 1, 2000. Show computations for the issue price.
Ans: (a) Discount, because the effective interest rate is higher than the stated rate.

(b)Cash ($110,807* + $2,400)	113,207	
Discount on bonds payable ($120,000 - $110,807)	9,193	
Interest expense ($120,000 x 3% x 4/6)		2,400
Bonds payable		120,000

* To compute issue price on May 1:
January 1, 2000:

Principal: $120,000 x PV1, 4%, 10 (.67556)	=	$81,067
Interest: $3,600 x PVA, 4%, 10 (8.11090)	=	29,199
Total	=	$110,266
		========

June 30, 2000:

Principal: $120,000 x PV1, 4%, 9 (.70259)	=	$ 84,311
Interest: $3,600 x PVA, 4%, 9 (7.43533)	=	26,767
Total	=	$111,078
		========

Interpolation:
($111,078 $110,266 = $812) x 2/6 =$271.00
($111,078 $271) =$10,807

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

153. On April 1, 2000, the DEF sold a $2,000,000 bond issue dated January 1, 2000, to yield 9% per annum to maturity. The bonds were to be outstanding for twenty years from January 1, 2000, and the stated rate of interest was 8%. Interest is paid each January 1.
(a) Give the entry to record the purchase of one-fourth of these bonds as a long-term investment by NOP. Assume effective interest amortization and contra/adjunct accounts.
(b) Give the December 31, 2000, adjusting and closing entries for NOP.
Ans:

(a) Investment in bonds ($2,000,000 x 1/4)	500,000	
Interest revenue ($500,000 x 8% x 3/12)	10,000	
Discount on bond investment		45,420
Cash (See computation below.)		464,580
(b) Interest receivable ($500,000 x 8%)	40,000	
Discount on bond investment (892 - 223)	669	
Interest revenue		40,669
Interest revenue ($40,669 - $10,000)	30,669	
Income summary		30,669

PV @ n=20; i=9:
Prin. (500,000 x .17843 = 89,215) + Int. (40,000 x 9.12855 = 365,142) = 454,357

PV @ n=19; i=9:
Prin. (500,000 x .19449 = 97,245) + Int. (40,000 x 8.95011 = 358,004) = 455,249
Difference 892
======

PV @ Apr. 1/00: $454,357 + (892 x 1/4 = 223) = 454,580

plus accrued interest	10,000
Total Cash Paid	464,580
	======

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

Use the following to answer questions 154-155:

In August 2005, Cummings Corporation, a calendar-year corporation that records adjusting entries only once per year, issued bonds with the following characteristic:

a. $50,000 total face value
b. 12% nominal rate
c. 16% yield rate
c. Interest dates are 1 February, 1 May, 1 August, and 1 November
e. Bond date is 31 October 2004
f. Maturity date is 1 November 2009 $1,000 of bond issue costs were incurred.

154. Provide the entries required on 1 August 2007 under the effective interest method of amortization.

Ans: 1 August 2007 - interest payment date

Interest expense	1,103	
Discount on bonds payable		203
Cash		900
Bond issue expense	35	
Bond issue cost		35

$1,103 = $27,567 x 4%
$900 = $30,000 x 3%
$35 = (60% of issue remaining) x ($1,000 / 17)

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

155. Provide the entries required on 1 August 2007 under the straight line method of amortization.

Ans:

Interest expense	1,115	
Discount on bonds payable		215
Cash		900
Bond issue expense	35	
Bond issue cost		35

$215 = $358 x 60%

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

Use the following to answer questions 156-162:

Four year term loan, U.S. $500,000
Funds borrowed 1 January 20X6; due 31 December 20X9
Exchange rates:

1 January	20X6	U.S. $1 = Cdn. $1.35
31 December	20X6	U.S. $1 = Cdn. $1.40
31 December	20X7	U.S. $1 = Cdn. $1.42
31 December	20X8	U.S. $1 = Cdn. $1.36
31 December	20X9	U.S. $1 = Cdn. $1.39

156. Based on the above information prepare entries to record receipt of loan proceeds for January 20X6.

Ans: Cash ($500,000 x 1.35)	$675,000	
Long term debt		$675,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

157. Based on the above information prepare entries to record the adjustment to spot rate for December 20X6.

Ans: Exchange loss	$25,000	
Long term debt 500,000($1.35 - $1.40)		$25,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

158. Based on the above information prepare entries to record adjustment to spot rate December 20X7

Ans: Exchange loss	$10,000	
Long term debt 500,000($1.40 - $1.42)		$10,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

159. Based on the above information prepare entries to record adjustment to spot rate December 20X8

Ans: Long term debt 500,000($1.42 - $1.36)	$30,000	
Exchange gain		$30,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

160. Based on the above information prepare entries to record adjustment to spot rate December 20X9

Ans: Exchange loss	$15,000	
Long term debt 500,000($1.36 - $1.39)		$15,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

161. Based on the above information prepare entries to record repayment of loan December 20X9

Ans: Long term debt 500,000($1.40 - $1.42)	$695,000	
Cash		$695,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

162. Based on the above information calculate the total accounting recognition of loss.

Ans: 20X6	$ 25,000 dr.
20X7	10,000 dr.
20X8	30,000 cr.
20X9	15,000 dr.
Total	$ 20,000 dr.

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5

163. ABC Inc issued $10,000,000 worth of bonds on January 1st, 2008. The bonds mature on December 31st, 2017 and carry a coupon rate of 6% payable semi-annually on June 30th and December 31st of each year. A market interest rate of 8% was effective throughout 2008.

Required:

1) Were the bonds issued at a premium or a discount?
2) Prepare all journal entries required during 2008.
3) Assume that on January 1st 2009, ABC decided to retire half of the bonds for $4,800,000 in cash. Prepare the required journal entry.

Ans:

1) The bonds were issued at a discount – market rate exceeds nominal (coupon) rate.

2) January 1st, 2008:

Cash	$8,640,999	
Bond Discount	$1,359,001	
Bonds Payable		$10,000,000

June 30th, 20X8

Interest Expense	$345,640	
Bond Discount		$ 45,640
Cash		$300,000

Dec 31st, 20X8

Interest Expense	$359,466	
Bond Discount		$ 59,466
Cash		$300,000

3)

Bonds Payable	$5,000,000	
Loss on Bond Disposal	$ 428,448	
Bond Discount		$ 628,448
Cash		$4,800,000

Difficulty: Hard
Level of Learning: Application
Topic: LO4, 5, 6

164. GHI Inc issued $5,000,000 worth of bonds on January 1st, 2008. The bonds mature on December 31st, 2017 and carry a coupon rate of 4% payable semi-annually on June 30th and December 31st of each year. A market interest rate of 6% was effective throughout 2008.

Required:

1) Were the bonds issued at a premium or a discount?
2) Prepare all journal entries required during 2008.
3) Assume that on January 1st 2009, ABC decided to retire ALL of the bonds for $5,500,000 in cash. Prepare the required journal entry.

Ans:

1) The bonds were issued at a premium – market rate is less than nominal (coupon) rate.

2) January 1st, 2008:

Cash	$5,743,894	
Bond Premium		$ 743,894
Bonds Payable		$5,000,000

June 30th, 20X8

Interest Expense	$172,317	
Bond Premium	$ 27,683	
Cash		$200,000

Dec 31st, 20X8

Interest Expense	$170,509	
Bond Premium	$ 29,491	
Cash		$200,000

3)	Bonds Payable	$5,000,000	
	Gain on Bond Disposal		$ 186,720
	Bond Premium	$ 686,720	
	Cash		$5,500,000

Difficulty: Hard

Level of Learning: Application

Topic: LO4, 5, 6

1. Businesses engage in many transactions that are unaffected by the form of the business: proprietorship, partnership, or corporation.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

2. The primary sources of owners' equity must be separately identified in the accounts.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

3. Preferred shareholders normally have the same voting rights as common shareholders.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

4. Shareholders in a corporation usually have limited liability.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

5. The contributed capital accounts should be classified by source.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

6. Retained Earnings restrictions are usually imposed on a company by a third party.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 5

7. Before a company can issue a property dividend in shares of another company, it must ensure that the shares are recorded at market value. The dividend is then paid out of the company's contributed capital accounts rather than its retained earnings.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO21

8. Under IFRS, companies are required to disclose the components of their shareholders' equity along with an explanation of any shareholder equity transactions during the year.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1, 9

9. Preferred shares generally have fewer voting rights than common shareholders but receive preferential treatment (relative to the common shareholders in the event of the company's liquidation.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

10. All unrealized gains and losses, regardless of origin, flow through Other Comprehensive Income.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 1, 9

11. Retained earnings, if not designated otherwise, represents the unappropriated portion of retained earnings.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 1

12. Total retained earnings include both appropriated and unappropriated retained earnings.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 5

13. Property dividends are dividends that the corporation distributes in the form of noncash assets.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 6

14. All Contributed Capital accounts may carry either a debit or a credit balance, depending on the transactions from which the account balance originated.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 3

15. When a corporation declares a small stock dividend, it should capitalize the par value of the shares.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 7

16. A large stock split should be accounted for by capitalizing the current market value of the stock.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 7

17. A stock dividend and a stock split are identical in all respects for the corporation issuing the dividend or splitting the stock.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6, 7

18. When stock rights are issued to current shareholders, it may require more than one such right to later acquire one additional share of the stock covered by the rights.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6, 7

19. Liquidating dividends are similar to stock dividends because neither one reduces total stockholders' equity.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO61

20. Dividends are paid when declared.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO61

21. Par value is typically set at a low amount so that the corporation can pay a minimum amount in dividends to the preferred shareholders.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 6

22. Only certain unrealized gains flow through Other Comprehensive Income – any realized gains flow through retained earnings.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO9

23. The shareholders of a corporation usually cannot be held legally liable for the debts of the corporation except to the extent that legal capital is impaired.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 2

24. Legal capital is related directly to the total number of shares issued.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 2

25. Both preferred and common shares may be cumulative.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO2

26. A Statement of Changes in Shareholder Equity is mandatory under both IFRS and ASPE.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO8, 9

27. The position of common shareholders is less risky than the positions of both the creditors and preferred shareholders.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 1

28. Issuing a common stock dividend decreases common shares and increases retained earnings.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 6

29. Treasury shares held by management are considered to be issued but not outstanding.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 4

30. The Treasury Share account is debited and credited at the cost of the shares repurchased.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 4

31. Common share subscriptions receivable should always be reported as a current asset.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 2

32. "Common shares subscribed" is credited in recording a common share subscription contract because the shares are usually issued at the time the contract is signed.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO2

33. If a corporation only has one class of shares, that class must be common shares.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 1

34. A bad debt loss is recognized when a subscriber to common shares defaults.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 2

35. Cumulative preferred shares usually carry the right, upon liquidation of the corporation, to dividends in arrears to the extent the corporation has retained earnings.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 2

36. Convertible preferred shares are convertible (usually to common shares) at the option of the shareholder and not at the option of the corporation.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO2, 3

37. The purchase of treasury stock reduces the number of outstanding shares, and if the treasury stock is subsequently resold, it is again classified as outstanding.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 4

38. Treasury shares cannot be voted, nor paid dividends, pending resale.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO41

39. The conversion of preferred shares into common shares results in no change in total shareholders' equity.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO2, 3

40. When retained earnings are restricted, they must also be appropriated.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO5

41. When a company issues to its shareholders some shares of another corporation's stock that currently are held as an investment, the company is issuing a stock dividend.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 6, 7

42. Dividends in arrears on cumulative preferred shares must be paid at the end of the accounting period if cash and retained earnings are available.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6

43. Dividends in arrears on noncumulative preferred shares must be paid before dividends can be paid to the common shareholders.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO61

44. Dividends in arrears on cumulative preferred shares constitute a liability to the corporation that should be recorded (accrued).

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 6

45. The date of record for a cash dividend follows the date of payment and precedes the date of declaration.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO 6

46. In accounting for dividends, the declaration date is the most important date because dividends are paid to whomever owns the shares on that date.

    Ans: False
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO6

47. A stock split results in the reduction of the par or stated value per share and a proportional increase in the number of shares outstanding.

    Ans: True
    Difficulty: Easy
    Level of Learning: Knowledge
    Topic: LO7

48. In a stock split, only the content of contributed capital is changed, whereas in a stock dividend the amount of contributed capital is changed.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO7

49. The accounting treatment for ordinary and liquidating dividends differs. Ordinary dividends cause a debit to retained earnings and liquidating dividends cause a debit to contributed capital.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 6

50. Share issue costs may be charged to:
A) Earnings.
B) Share Capital.
C) Retained Earnings.
D) B or C.

Ans: D
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO2

51. ABC Inc. issued 1,000 common shares and 3,000 preferred shares for a lump sum of $25,000. The fair market value of each share on the date of issue was $6 per common share and $8 per preferred share. How much of the proceeds received should be allocated to the preferred shares on the date of issue?
A) $5,000
B) $20,000
C) $6,250
D) $19,750

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO2

52. The conversion from one type of share to another is accounted for at:
    A) Book Value.
    B) Fair Market Value.
    C) A or B.
    D) A discounted amount.

    Ans: A
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO 2

53. Preferred shares, which have the most restrictive features, are:
    A) Noncumulative, non-participating, nonvoting.
    B) Fully participating, nonvoting.
    C) Noncumulative, fully participating, nonvoting.
    D) Non-participating, cumulative, nonvoting.

    Ans: A
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO 2

54. Gains on sale of treasury stock should be credited to:
    A) Additional contributed capital.
    B) Other income.
    C) Share capital.
    D) Retained earnings.

    Ans: A
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO 4

55. Treasury shares are said to be:
    A) Issued.
    B) Outstanding.
    C) A and B.
    D) A or B.

    Ans: B
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO 4

56. Ryan Corp. has the following share capital outstanding:
Common, 10,000 shares
Preferred $1.80 noncumulative, non-participating, 10,000 shares
Dividends are two years in arrears, excluding the current year. Total dividends of $90,000 will be paid for the current year. The total amounts that will be received by the preferred shareholders and common shareholders are:

	Preferred Shareholders	**Common Shareholders**
1	$36,000	$54,000
2	$18,000	$72,000
3	$90,000	$0
4	$54,000	$36,000

A) Choice 1
B) Choice 2
C) Choice 3
D) Choice 4

Ans: B
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO6

57. The following owners' equity section of a firm's balance sheet relates to the current year (end-of-year data):

8%, $100 par cumulative preferred shares	$10,000
$5 par common shares	40,000
Contributed capital in excess of par-preferred shares	5,000
Contributed capital in excess of par-common shares	20,000
Retained earnings	60,000
Treasury stock	(10,000)
Total owners' equity	$125,000
	========

How many common shares are issued?
A) 8,000
B) 6,000
C) 7,000
D) There is insufficient information provided to answer the question.

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO 2

58. LS issued 200 common shares to BH (last share transaction was a year prior when LS sold 10 shares at $4 per share), and received a patent in full payment. The patent had a current market value of $2,000 and was carried on the books of TX at $1,500. Under ASPE, common shares should be credited for:
    A) $800
    B) $1,500
    C) $1,800
    D) $2,000
    E) This transaction has no commercial substance, therefore no entry is required.

    Ans: A
    Difficulty: Medium
    Level of Learning: Knowledge
    Topic: LO 2, 9

59. SXC reported the following data on its 1999 statement of financial position:

Common shares no par	$202,000	
Common shares subscribed		18,000
Retained earnings		175,000

    If the average price paid for all of the common shares sold and subscribed were $5.00, the total number of sold and subscribed shares was:
    A) $44,400
    B) $40,400
    C) $44,000
    D) $40,000
    E) None of these answers is correct

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

60. DWWR purchased its own common shares for $20,000 and debited the treasury stock account for the purchase price. The shares were subsequently sold for $17,000. The $3,000 difference between the cost and sale price should be recorded as a reduction of:
    A) Contributed capital from treasury stock transactions without regard as to whether or not there have been previous net "gains" from sales or retirements of the same class of shares.
    B) Contributed capital from treasury stock transactions to the extent of previous net "gains" from sales or retirements of the same class of shares; otherwise retained earnings should be reduced.
    C) The beginning balance of retained earnings.
    D) Revenues on the income statement.

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4

61. XHC had only two share transactions. Initially, XHC issued 1,000 common shares, at $15 per share. XHC later bought back 200 shares at $16 per share. Under the single-transaction method, what is the amount that should be recorded in the treasury stock account?
A) $2,000
B) $3,000
C) $3,200
D) $3,600

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO 4

62. Identify the missing component (X) in the following equation: Retained earnings, ending balance = Net income to date + prior period adjustments to date - cash and property dividends to date - X
A) Stock dividends and splits to date.
B) Stock dividends to date.
C) Stock splits to date.
D) Net unrealized gain or loss on securities available for sale.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO 6

63. Cash dividends sometimes are declared in one reporting period and are payable in the next reporting period. The dividend should be recorded on the:
A) Payment date.
B) Declaration date.
C) Record date.
D) Either the declaration, record, or payment date, as preferred by the company.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO 6

64. A property dividend causes a debit to retained earnings equal to the ___________ of the property distributed:
A) Book value
B) Fair market value
C) Original cost
D) Income tax basis

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO 6

65. CB Corporation issued a 2 for 1 stock split. Which of the following is not a true statement concerning the effect of the split?
   A) The number of shares outstanding is increased.
   B) There is a transfer of retained earnings to contributed capital.
   C) A proportionate reduction in the par value per share occurs.
   D) There is a continuation of retained earnings with no reduction in its balance.

   Ans: B
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO 7

66. On December 31, 1999, when JR Corporation's shares were selling at $44 per share, its shareholders' equity accounts were as follows:
   Common shares (no par value) 100,000

shares issued and outstanding	$2,700,000
Retained earnings (credit)	4,450,000

   A 100 percent stock dividend was declared and issued. The effect of this dividend was:
   A) Total retained earnings did not change.
   B) Common shares increased to $5,600,000.
   C) Common shares increased to $6,460,000.
   D) Total shareholders' equity decreased.

   Ans: A
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

67. Which of the following dividends does not reduce retained earnings?
   A) Scrip dividend.
   B) Stock dividend.
   C) Cash dividend.
   D) Property dividend.
   E) Liquidating dividend.

   Ans: E
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

68. For dividends, the date of record is the date:
    A) The market price of the shares drops due to the dividend.
    B) On which the list of shareholders is prepared.
    C) The dividend is actually paid.
    D) The dividend is announced.

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO6

69. Major factors contributing to the growth of the corporate form of business includes all of the following except:
    A) The facility to accumulate large amounts of resources.
    B) Limited liability of the shareholders.
    C) Easy transferability of ownership.
    D) The lack of government regulation.

    Ans: D
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

70. Total equities of a corporation usually include:
    A) Assets plus contributed capital, and plus retained earnings.
    B) Contributed capital plus retained earnings.
    C) Contributed capital plus retained earnings, and plus creditors' interest.
    D) Total owners' equity less treasury stock at cost.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

71. Owners' equity must equal the:
    A) Total contributed capital plus retained earnings less liabilities.
    B) Sum of the share capital account balances plus the total contributed capital in excess of par (or stated value).
    C) Total assets minus total liabilities.
    D) Total contributed capital plus total retained earnings.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

72. ABC Inc. engages in a non-cash exchange with a third party whereby ABC Inc. issues common shares to the third party in exchange for some highly specialized Machinery & Equipment. The value of the shares issued was $15,000 while the appraised value of the Machinery & Equipment was $12,000. At what amount would this transaction be valued on ABC's books?
A) $12,000 under IFRS and $15,000 under ASPE.
B) $15,000 under IFRS and $12,000 under ASPE.
C) $12,000 under either ASPE or IFRS.
D) $15,000 under either ASPE or IFRS.

Ans: A
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 9

73. Under IFRS, the treatment of any of a company's foreign subsidiary is dependent upon:
A) The functional currency of the subsidiary.
B) The nature and extent of the parent company's relationship with the subsidiary.
C) A or B.
D) Managerial judgement.

Ans: A
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 9

74. Which of the following is not a basic right of shareholders?
A) To inspect the books of account and to insist upon an audit in the event of dissatisfaction with results revealed by such inspection
B) To participate in the management of the corporation through taking part in and voting in shareholders' meetings
C) To participate in the profits of the corporation through dividends declared by the board of directors
D) To share in the distribution of assets of the corporation at liquidation or through liquidating dividends
E) To sell shares in the corporation at a price exceeding its cost.

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO 2

75. Ownership of shares usually entitles the holders to all of the following rights except:
    A) To elect the board of directors of the corporation.
    B) To control the day-to-day operations of the corporation.
    C) To purchase new shares when they are offered for sale.
    D) To share in the profits of the corporation.

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

76. Authorized share capital refers to the total number of shares:
    A) Outstanding.
    B) Issued.
    C) That can be issued in conformity with the corporation's charter.
    D) Issued, less all treasury shares owned.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

77. Issued share capital refers to the number of shares:
    A) Outstanding.
    B) Outstanding less all shares held as treasury shares.
    C) Outstanding plus all shares held as treasury shares.
    D) That may be issued according to the corporate charter.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

78. Share capital may be classified primarily as:
    A) Par Value, Common; or Nopar, Preferred.
    B) Nopar, Common; or Par Value, Preferred.
    C) Par Value, Common; Nopar, Common; Par Value, Preferred; or Nopar, Preferred.
    D) Par Value, Common; Stated Value Common; or Nopar, Preferred.

    Ans: C
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

79. At the date of the financial statements, common shares issued would exceed common shares outstanding as a result of the:
    A) Payment in full of subscribed shares.
    B) Declaration of a stock split.
    C) Declaration of a stock dividend.
    D) Purchase of treasury stock.

    Ans: D
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

80. Zygo sold 1,000 common shares (par $3) at $5 per share on a subscription basis. The entry to record this transaction included a credit to:
    A) Accounts receivable.
    B) Contributed capital in excess of par.
    C) Common shares.
    D) Subscriptions receivable.

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

81. When a corporation sells some of its own common shares, all on credit, there should be a debit to the account:
    A) Subscriptions receivable, common.
    B) Accounts receivable.
    C) Cash.
    D) Notes receivable, common.

    Ans: A
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

82. If preferred shares are noncumulative, then:
   A) The preferred shareholders are entitled to current dividends before common shareholders can receive dividends.
   B) Cash dividends not declared in prior years are lost permanently.
   C) The preferred shareholders are only entitled to a specific percent of the cash dividends, regardless of the amount declared.
   D) Prior years' cash dividends must be paid to the preferred shareholders before any dividends may be paid to the common shareholders.

   Ans: B
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO 2

83. If preferred shares are non-participating, then:
   A) Preferred shareholders are not entitled to vote.
   B) Preferred dividends for the year are limited to a specific rate.
   C) Preferred shareholders are not entitled to a prior year's dividend once that year has passed.
   D) Preferred shareholders may receive dividends in excess of a specific rate if common stockholders receive more than that specific rate.

   Ans: B
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO 2

84. The redemption privilege on preferred shares provides that the preferred shareholders can:
   A) Purchase treasury shares any time they become available.
   B) Purchase enough shares of any new issue, so that their percentage ownership remains the same.
   C) Turn in the preferred shares for a specified cash price.
   D) Exchange the preferred shares for common shares.

   Ans: C
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO 2

85. If preferred shares are callable, then:
   A) The corporation may, at its option, purchase the preferred shares for a specified cash price.
   B) The preferred shareholder can turn the preferred shares in for a specified cash price.
   C) The shareholders can exchange the preferred shares owned for common shares.
   D) There cannot be dividends in arrears.

   Ans: A
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO 2

86. The order in which dividends are allocated to common and preferred shares depends upon the provisions in the respective stock contracts. Choose the correct statement regarding this allocation.
    A) When noncumulative preferred shares are fully participating, the rate of dividends allocated to preferred shares is the ratio of total par of preferred shares outstanding to total par of both classes of shares outstanding
    B) When noncumulative preferred shares are not participating, the rate of dividends to common shares are limited to the ratio of total par of common shares outstanding to total par of both classes of shares outstanding
    C) When 8% cumulative preferred shares are participating to a total of 12%, any arrear dividends are ignored in the allocation since they pertain to a previous year
    D) When 8% noncumulative preferred shares are participating to a total of 12%, the preferred shares must receive all arrear dividends and 12% of total preferred shares par outstanding prior to common shares receiving any dividends

    Ans: A
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2

87. As of January 1, 2011 there are 2 years of dividends in arrears on an issue of cumulative nonconvertible preferred shares. No dividends on preferred shares were declared in 2011. Therefore, under IFRS, on the Dec. 31, 2011 financial statements, the firm issuing the preferred shares:
    A) Reports a liability equal to 3 years of dividends on preferred shares
    B) Reports a liability equal to 2 years of dividends on preferred shares
    C) Subtracts 3 years of dividends on preferred shares from earnings when computing earnings per share for 2011
    D) Discloses in a footnote to 2011's balance sheet that there are 3 years of dividends on preferred shares in arrears
    E) Discloses in a footnote to 2011's balance sheet that there are 2 years of dividends on preferred shares in arrears

    Ans: D
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO6, 9

88. The number of treasury shares held by a corporation equals:
    A) The difference between issued shares and outstanding shares.
    B) The difference between authorized shares and outstanding shares.
    C) All shares held by the treasurer of the corporation.
    D) All shares purchased by shareholders due to their pre-emptive right.

    Ans: A
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4

89. Under the single transaction method, the difference between the cost of treasury stock and a subsequent higher selling price of the treasury stock should be credited to:
    A) Retained earnings.
    B) Share capital.
    C) Gain from treasury stock transaction.
    D) Contributed capital.

    Ans: D
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4

90. How should a gain from the sale of treasury stock be reflected when using the single transaction method of recording treasury stock transactions?
    A) As an extraordinary item shown on the income statement
    B) As ordinary earnings shown on the income statement
    C) As contributed capital from treasury stock transactions
    D) As an increase in the amount shown for common stock

    Ans: C

    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4

91. Losses that a corporation suffers from dealing in its own stock may:
    A) Be recorded as a long-term loss.
    B) Be recorded in the retained earnings account.
    C) Be recorded as a loss from peripheral or incidental transactions (i.e., not from continuing operations).
    D) Never be recorded in the retained earnings account.

    Ans: B
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4

92. Which of the following is NOT a true statement? Treasury stock is:
    A) Shares that cannot receive dividends nor vote.
    B) Shares that are held by the issuing company but has not been retired.
    C) Recorded in an equity account that has a debit balance.
    D) Shares that have been issued but are no longer outstanding.
    E) Shares that are included in earnings per share calculations.

    Ans: E
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO4

93. When all of the preferred shares are purchased and formally retired by the issuing corporation for less than its original issue price, accounting for the retirement increases:
    A) Retained earnings.
    B) Contributed capital in excess of par, common stock.
    C) Net income for the period.
    D) Contributed capital from retirement of preferred shares.

    Ans: D
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 3

94. The owners' equity section of a firm's balance sheet reflects the following at the end of the current year:

$6 Preferred shares, 3,000 shares outstanding	$300,000
Common shares, 100,000 shares outstanding	500,000

    (Matching dividend, if applicable, $.30)
    The preferred shares participate up to a maximum of $8 ($2 additional participation). There were two years of dividends in arrears on the preferred shares at the beginning of the current year. If the firm declares $110,000 in dividends at the end of the current year, what portion of that amount is distributed to the common shareholders?
    A) $50,000
    B) $30,000
    C) $54,000
    D) $60,000

    Ans: A
    Difficulty: Medium
    Level of Learning: Application
    Topic: LO 2, 6

95. The increases in account balances of XYZ during 1999 are presented below:

Assets	$456,000	Common Shares	240,000
Liabilities	148,000	Other Contributed Capital	24,000

Assuming the only debit to retained earnings was for a dividend of $52,000, net income for 1999 was:
A) $8,000
B) $68,000
C) $96,000
D) $104,000

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO6

96. On December 31, 1999, TTX reported owners' equity of $150,000. During 2000, TTX declared and paid cash dividends of $30,000; reported a net loss of $15,000; issued additional common shares (nopar) for $70,000; and purchased treasury stock at a cost of $15,000 (cash), Therefore, the 2000 ending amount of shareholders' equity was:
A) $160,000
B) $170,000
C) $215,000
D) $230,000

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO 2

97. The following data is available for XAC:

Common shares, no par 10,000 shares authorized, 8,000 shares outstanding	$120,000
Common shares subscribed	?
Subscriptions receivables (40% uncollected)	12,000

Find the number of shares subscribed and the subscription price per share?

	Shares Outstanding	**Average Issue Price**
1	5,000	$25.00
2	5,000	$12.00
3	1,200	$25.00
4	1,200	$12.00

A) Choice 1
B) Choice 2
C) Choice 3
D) Choice 4

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO 2

98. On January 1, 2000, DDB agreed to purchase 4,000 of CTC's common shares at $5 per share. Cash payment in full, including 10% interest, is to be paid one year later at which time the shares will be issued. The appropriate journal entry for CTC to record the transaction on January 1, 2000, would include a:
A) Debit to Cash for $20,000.
B) Credit to Common Shares Subscribed for $20,000.
C) Credit to Cash $20,000.
D) Debit to Subscriptions Receivable for $18,000.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO 2

99. During 1999, BV sold and issued the following shares for $20,000 cash:
Common shares, 600 shares (current market price per share, $23.50).
Preferred shares, 200 shares (no current market price available); original issue price, three years earlier, $22 per share.
The total issue price of $20,000 that should be apportioned to the preferred shares is:
A) $4,000
B) $4,400
C) $5,900
D) $8,000

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO 2

100. ABC had 20,000 shares of treasury common stock, which it purchased for $7 per share. Until now, this was ABC's only treasury stock transaction. The shares were originally sold and issued at $5 per share. ABC uses the single-transaction method. ABC is now selling the treasury shares for $5 per share. The entry to record the resale would include a:
A) Credit to Treasury stock for $100,000.
B) Debit to Retained earnings for $40,000.
C) Debit to common shares for $140,000.
D) Credit to common shares for $100,000.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO4

101. TTSS Corporation had 1,000 common shares issued and outstanding (sold at $40 each). It then made its first-ever purchase of treasury stock by buying 200 of its own shares for $50 per share. Assume sufficient retained earnings. The entry to record this purchase using the single-transaction method would include:
A) dr. common shares $8,000
B) dr. common shares $10,000
C) dr. contributed capital from treasury stock transactions $2,000
D) dr. treasury stock $10,000

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO4

102. When treasury stock accounted for by the single-transaction method is subsequently sold for more than its purchase price, the excess of the cash proceeds over the carrying value of the treasury stock should be recognized as:
A) an unusual gain.
B) Income from continuing operations.
C) Increase in contributed capital.
D) Increase in retained earnings.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4

103. A restriction of retained earnings is most likely to be required by the:
A) payment of last maturing series of a serial bond issue.
B) amortization of intangible assets.
C) purchase of treasury stock.
D) exhaustion of potential benefits of the investment credit.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO7

104. An appropriation of retained earnings of a significant amount:
A) Means that specific assets actually have been set aside for a specific purpose.
B) provides protection to the stockholders rather than to the creditors.
C) Can have a significant impact on the total amount of retained earnings when recorded.
D) Can be used to absorb extraordinary losses directly when of a significant amount.
E) Should be reversed when the purpose of the appropriation has been achieved.

Ans: E
Difficulty: Medium
Level of Learning: Application
Topic: LO 7

105. When noncash assets are issued as a dividend, those assets should be re-valued as of the:
A) Announcement date.
B) Recording date.
C) Declaration date.
D) Issuance date.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO 2, 6

106. Which of the following represents the interest period for a scrip dividend?
   A) Record date to payment date
   B) Declaration date to payment date
   C) Record date to ex-dividend date
   D) Declaration date to ex-dividend date

   Ans: B
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

107. X Corporation owns 15% of the outstanding shares of Z Corporation. The Z stock is distributed to the shareholders of X Corporation as a dividend at its current market value. This is an example of a:
   A) scrip dividend.
   B) cash dividend.
   C) stock dividend.
   D) property dividend.

   Ans: D
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

108. The declaration of a property dividend results in:
   A) a debit to retained earnings.
   B) a credit to retained earnings.
   C) either a debit or a credit to retained earnings.
   D) no effect on retained earnings.

   Ans: A
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

109. If a company desires to pay a cash dividend, but does not want to increase its liabilities, it can:
   A) pay the dividend only out of retained earnings.
   B) issue a scrip dividend.
   C) pay the dividend on declaration date.
   D) pay the dividend on the ex-dividend date.

   Ans: C
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

110. The declaration and payment of a cash or property dividend requires:
A) an appropriation of retained earnings.
B) the distribution of a current asset.
C) a reduction of both retained earnings and assets.
D) a decrease in retained earnings and a change in contributed (paid-in) capital.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO6

111. On January 10, 1999, ZOE Corporation declared a cash dividend when the related shares were selling for $10 per share. ZOE prepared the list of shareholders on February 10, 1999 at which time the shares were still selling for $10 per share. However, on February 11, 1999 the shares were selling for $8 per share. The dividend was paid on March 1, 1999 when the shares were selling for $9 per share. The ex-dividend date must have been:
A) January 10/99.
B) February 10/99.
C) February 11/99.
D) March 1/99.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO6

112. Cash dividends usually are declared on one date and paid on a subsequent date to shareholders of record on some intermediate date. On which of the following dates should an accrual basis shareholder recognize investment revenue?
A) Record date
B) Declaration date
C) Payment date
D) Either record date or declaration date

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

113. The declaration and issuance of a common stock dividend:
    A) Does not change the internal content of retained earnings.
    B) Does not change assets, liabilities or total owners' equity.
    C) Decreases total owners' equity and increases the related common stock account.
    D) Decreases assets and decreases total owner's equity.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

114. A common stock dividend does not:
    A) Change a shareholder's proportionate interest in the corporation.
    B) Result in the shareholder receiving additional shares.
    C) Change the proportions among the different sources of shareholders' equity.
    D) Change the total amount in the related common shares account.

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO6

115. Stock splits are often issued primarily to:
    A) Reduce the market price per share.
    B) Increase permanent capital.
    C) Decrease the liability for dividends in arrears.
    D) Give the shareholders more voting rights.

Ans: A

Difficulty: Medium
Level of Learning: Application
Topic: LO7

116. A stock dividend,
    A) If less than 20 to 25%, reduces retained earnings by the par value of shares distributed in the dividend
    B) Increases the wealth of the recipient if the market value of the shares are unchanged by the stock dividend
    C) Alters the par value of the common shares
    D) If 100%, has no effect on the market value of the shares

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

117. Choose the most correct statement regarding a 2-for-1 stock split and a 100% stock dividend.
   A) Neither affects par value
   B) Both cause the same reduction in retained earnings
   C) Both double the number of shares outstanding
   D) Both cause a significant increase in the common share account
   E) Only one affects contributed capital in excess of par on common shares

   Ans: C
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

118. A 3-for-1 common stock split,
   A) Decreases retained earnings by the par value of shares distributed in the split
   B) Will likely not affect the market value of the stock
   C) Has no effect on common share account
   D) Will cause a change in the allocation of dividends to common stock relative to preferred stock

   Ans: C
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6, 7

119. The effect of a stock dividend is to reduce:
   A) total stockholders' equity.
   B) retained earnings and the par value of each share.
   C) retained earnings and increase legal capital.
   D) total assets and reduce total stockholders' equity.

   Ans: C

   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

120. Which of the following statements concerning stock dividends is correct?
   A) The declaration of a stock dividend should not be recorded as a liability even though it has not yet been issued.
   B) The issuance of a stock dividend increases total stockholders' equity.
   C) Courts generally have held that stock dividends, once declared, are irrevocable by the board of directors; therefore, a stock dividend declared, but not yet issued is a liability.
   D) A stock dividend cannot use treasury stock.

   Ans: A
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

121. XY Company: Common shares outstanding, 10,000; average issue price, $115; current market price, $140. Shares sold on a stock subscription basis are not issued until the subscription price is collected in full. Recording a declaration of a 10 percent stock dividend in conformity with generally accepted accounting principles would change retained earnings:
A) On the basis of the market value of shares.
B) By 10 percent of its balance before the dividend.
C) On the basis of an arbitrary value of shares.
D) On the basis of the average paid-in value of shares.

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO6

122. Fractional share rights are usually issued:
A) When a corporation issues a stock split.
B) At the time a property dividend is declared.
C) At the time a cash dividend is declared.
D) At the time a stock dividend is declared.

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO6

123. When a corporation issues a dividend in excess of the balance of its retained earnings account, it is issuing a:
A) Scrip dividend.
B) Stock dividend.
C) Property dividend.
D) Liquidating dividend.

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO6

124. A dividend that constitutes a return of contributed capital rather than earnings is called a:
A) Property dividend.
B) Liability dividend.
C) Liquidating dividend.
D) Capital dividend.

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO6

125. If a corporation has dividends in arrears on preferred shares, they should also:
   A) Capitalize retained earnings for the dividends.
   B) Declare the dividends.
   C) Record a liability for the dividends.
   D) Report the dividends in arrears.

   Ans: D
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

126. If a corporation has dividends in arrears of $25,000 on its cumulative preferred shares, it must:
   A) Set aside cash for the amount of the dividends.
   B) Pay the dividends in arrears before it can pay dividends to its common shareholders.
   C) Capitalize this amount as a part of permanent capital.
   D) Appropriate retained earnings for this amount.

   Ans: B
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO6

127. XYZ reported the following on its December 31, 1999, balance sheet: common shares, nopar, $200,000; unappropriated retained earnings, $40,000; appropriation of retained earnings for bond sinking fund, $10,000; and reserve for possible future inventory losses, $5,000. Therefore, the last line on the retained earnings statement, total appropriated and unappropriated retained earnings should be:
   A) $55,000
   B) $15,000
   C) $40,000
   D) $10,000

   Ans: A
   Difficulty: Medium
   Level of Learning: Application
   Topic: LO7

128. A firm declares a property dividend to its shareholders. The assets to be distributed in the dividend have a combined book value of $40,000 and combined market value of $60,000. Before taxes, the net change in retained earnings as a result of this nonreciprocal transfer is:
A) $40,000
B) $60,000
C) $20,000
D) $0

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO6

129. You happen across the balance sheet of a firm, which discloses $40,000 of ending retained earnings, $10,000 of which is appropriated for plant expansion. This firm is not a natural resources firm. Therefore:
A) the firm has $30,000 of cash
B) the firm has $40,000 of cash
C) the maximum allowable dividend cannot exceed $30,000
D) the firm has never distributed a stock dividend

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO7

130. ABC declared a common stock dividend on March 10, at which time its shares were selling for $15 per share and 10,500 shares were outstanding. After the dividend, because only 13,650 were outstanding, some shareholders received fractional share rights. If the provisions of the dividend provided that one share was to be issued for each three shares previously owned, there must have been:
A) 1,050 fractional share rights outstanding.
B) 350 fractional share rights outstanding.
C) 117 fractional share rights outstanding.
D) Fractional shares outstanding not determinable based on the information given.

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO6

131. RST had the following shareholders and the shares owned by each on November 15:

Shareholder	Shares Owned
a	1,999
b	1,555
c	1,699
d	2,132
e	1,900
Total	9,285

On that date, RST declared a 1 for 2 common stock dividend. The stock was selling for $10 per share. RST issued fractional share rights when necessary. RST had to issue the following number of fractional share rights:

A) More than three.
B) Three.
C) Two.
D) One.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

132. The December 31, 1999, the balance sheet of TXY reflected the following:

Total assets (market value $298,000)	$252,000
	========
Total liabilities	$70,000
Preferred shares,$.10 cumulative, non-participating, liquidation preference	$ 2.20
per share, 20,000 shares outstanding	50,000
Common shares, nopar, 30,000 shares outstanding	120,000
Retained earnings (no dividends were declared or paid in 1998 - 1999)	12,000
Total	$252,000
	=======

Assume the company sold all of the assets at December 31, 1999, at market value for cash; paid off the liabilities and distributed all of the remaining cash to the shareholders. The amount of cash per share that each common shareholder would receive would be:

A) $4.47
B) $5.93
C) $6.00
D) $8.27

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO6

133. Effective April 8, 2000, the shareholders of Kim Corporation approved a 2 for 1 split of the company's common shares, and an increase in authorized common shares from 100,000 shares to 200,000 shares. Kim's shareholders' equity accounts immediately before issuance of the stock split shares were as follows:

Common shares, 100,000 shares authorized;	
50,000 shares outstanding	$2,250,000
Retained earnings	2,150,000

What should be the balances in Bennett's common shares and retained earnings accounts immediately after the stock split?

	Common Shares	**Retained Earnings**
1	$ 2,300,000	$ 1,350,000
2	$ 1,150,000	$ 200,000
3	$ 2,300,000	$ 200,000
4	$ 2,250,000	$ 2,150,000

A) Choice 1
B) Choice 2
C) Choice 3
D) Choice 4

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO6, 7

134. The dollar amount of total shareholders' equity remains the same for the:
A) Issuance of preferred shares in exchange for convertible debentures.
B) Issuance of nonconvertible bonds with detachable stock purchase warrants.
C) Declaration of a cash dividend.
D) Declaration of a stock dividend.

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO8

135. On January 1, 2000, WVC split its common shares 4 for 1 when the market value was $80 per share. Prior to the split, WVC had 50,000 common shares issued and outstanding (average issue price $12 per share). After the split, the average issue price of the shares was reduced:
A) By $3 per share.
B) To $3 per share.
C) To $4 per share.
D) To $2.40 per share.
E) No change in the par value.

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO7

136. Accounting recognition must be given to common share subscriptions on the subscription date:
A) to guarantee the receipt of dividends subsequent to the subscription date.
B) because the dollar amount is usually large.
C) because all events relating to the common share accounts must be disclosed.
D) because a legal contract is involved.

Ans: D
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO2

137. A company reacquires its own shares during the fiscal year and reports the transaction in the theoretically correct manner. What effect will this transaction have on shareholders' equity and earnings per share, respectively?
A) Increase and decrease
B) Decrease and decrease
C) Decrease and increase
D) Increase and no effect

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO4

138. XV Corporation has 1,000 shares of treasury stock (common shares). It was originally issued at $15 per share and was reacquired at $10 per share. XV Corporation has decided to formally retire these shares; the current market price is $9. The single-transaction method is used. The entry to record the retirement of the shares should include the following:
A) Contributed capital from common share retirement, credit, $5,000.
B) Gain on retirement of common shares, $5,000.
C) Unusual gain, $5,000.
D) Retained earnings credit, $5,000.

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO4

139. The owners' equity section of a firm's balance sheet reflects the following at the end of the current year:

$6 Preferred shares, 3,000 shares outstanding	$300,000
Common shares, 100,000 shares outstanding	500,000

(Matching dividend, if applicable, $.30)
The preferred shares participate up to a maximum of $8 ($2 additional participation). There were two years of dividends in arrears on the preferred shares at the beginning of the current year. If the firm declares $90,000 in dividends at the end of the current year, what portion of that amount is distributed to the preferred shareholders?
A) $54,000
B) $56,250
C) $60,000
D) $55,250

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

140. BX had the following shares outstanding:

Preferred shares, $6, 2,000 shares	$100,000
Common shares, 2,000 shares	$200,000

(Matching dividend, if applicable, $12)
The preferred shares are cumulative, fully participating; dividends are three years in arrears, excluding the current year; dividends declared in the current year amount to $87,000. The total amount of dividends to which common shareholders are entitled is:
A) $33,000
B) $40,000
C) $49,000
D) $52,000

Ans: A
Difficulty: Medium
Level of Learning: Application
Topic: LO6

141. DX had the following shares outstanding:

Preferred shares, $3, 2,000 shares	$100,000
Common shares, 2,000 shares	$200,000

(Matching dividend, if applicable, $6)

The preferred shares are cumulative, fully participating; dividends are three years in arrears, excluding the current year; dividends declared in the current year amount to $42,000. The total amount of dividends to which preferred shareholders are entitled is:

A) $16,000
B) $20,000
C) $24,500
D) $26,000

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO6

142. Lorella entered into a common share subscription contract for 1,000 shares at a subscription price of $20. She paid 20% of the total price as a down payment and also paid the next two 20% instalments (she paid 60% in all). Lorella then defaulted on the contract and refused to pay any more. Assuming the company must issue shares in proportion to the cash paid, the entry to record the default would include:

A) dr. common shares $12,000
B) dr. common shares subscribed $12,000
C) dr. subscriptions receivable $8,000
D) dr. common shares subscribed $20,000

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO2

143. CRC reported the following on its 1995 balance sheet:

$6 Preferred shares, no par	$62,000
Common shares, no par	320,000
Retained earnings	240,000

Given common shares outstanding, what is the average issue price per common share?

	Shares Outstanding	**Average Issue Price**
1	200,000	$1.41
2	100,000	$2.82
3	50,000	$6.40
4	40,000	$8.80
5	None of these	

A) Choice 1
B) Choice 2
C) Choice 3
D) Choice 4
E) Choice 5

Ans: C
Difficulty: Medium
Level of Learning: Application
Topic: LO2

144. YTC sold and issued 200 of its common shares, true no-par, at $12 per share. Assuming no specific legal requirements, the common share account should be credited for:
A) $200
B) $240
C) $2,000
D) $2,400

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO2

145. ABC made the following entry to record the issuance of a dividend:

Retained earnings	40,000
Common shares	40,000

ABC must have declared a:
A) stock split.
B) Property dividend.
C) Large stock dividend.
D) Small stock dividend.

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO6

146. MNO declared a stock dividend when it had 40,000 shares outstanding. After issuing the dividend, 7,200 additional shares and 4,000 fractional share rights were outstanding. If it required five fractional share rights to acquire a new share, this dividend must have been a:
A) 5 percent stock dividend.
B) 10 percent stock dividend.
C) 15 percent stock dividend.
D) 20 percent stock dividend.

Ans: D
Difficulty: Medium
Level of Learning: Application
Topic: LO6

147. BAX declared a stock dividend, which provided that each shareholder would receive one share for each ten shares currently owned. Fractional share rights were issued to each shareholder for the number of shares issuable. The rights can be bought and sold, but must be exercised within 3 months. The equity accounts had the following balances on the declaration date:
Common shares (market price $15) $ 25,000
Treasury stock, single-transaction method (400 shares) 4,000
Retained earnings 140,000
Assuming an entry is made on declaration date, BAX would properly record the declaration as follows:

1 Retained earnings	2,100	
Common stock dividend issuable		2,100
2 Retained earnings	3,150	
Common stock dividend issuable		3,150
3 Retained earnings	2,500	
Common stock dividend issuable		2,500
4 Retained earnings	3,750	
Common stock dividend issuable		3,750

A) Choice 1
B) Choice 2
C) Choice 3
D) Choice 4

Ans: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

148. Match the following terms with the appropriate definitions.
A. Contributed capital
B. Legal capital
C. Shareholders' equity
D. Total equity
___ 1. The investment made by the entrepreneurs; that is, the total amount "invested" by all parties other than creditors.
___ 2. The total equity at any given time of the legal owners of the enterprise. It is the total of the proprietorship equity including both contributed capital and subsequent accretions thereto.
___ 3. Represents the total claims of all parties in the assets of the business. It is the sum of the liabilities and owners' equity.
___ 4. hat portion of corporate capital required by statute to be retained in the business for protection of creditors.

Ans: 1: A, 2: C, 3: D, 4: B
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO1

149. XAC received a share subscription from J. Doe for 100 of its common shares, issue price $15; one-third cash down payment. Provide the entry to record the subscription and partial payment.
Ans:

Cash ($1,500 x 1/3)	500	
Subscription receivable, common ($1,500 x 2/3)	1,000	
Common shares subscribed (100 shares x $10)		1,500

Difficulty: Medium
Level of Learning: Application
Topic: LO2

150. YTC issued 200 of its preferred shares and 1,000 of its common shares, for a total cash consideration of $15,000. The current market prices for its shares were: Preferred, $25; Common, $20. The issue entry for the preferred and common shares combined would be as follows:
Ans: The total consideration paid equals the sum of the market values of the individual securities sold; therefore no allocation is necessary.

Cash (given)	15,000	
Preferred shares (20%)		3,000
Common shares (80%)		12,000

Difficulty: Medium
Level of Learning: Application
Topic: LO2

151. Indicate the principle effects of a cash dividend (declared and paid), a stock dividend issued, and a stock split issued, on the financial statements of the issuing corporation. Respond as follows: I-for increase; D-for decrease; and N-no effect. Assume no stock warrants and no reverse stock splits.
Stock

Financial Statement Item	Cash Dividend	Stock Dividend	Stock Split
(a) Contributed capital(exclusive of retained earnings)	____	____	____
(b) Par value per share outstanding	____	____	____
(c) Total amount of shares outstanding	____	____	____
(d) Retained earnings (at year-end)	____	____	____
(e) Number of shares outstanding	____	____	____
(f) Net income (for the year of issuance)	____	____	____
(g) Earnings per share (for the year of issuance)	____	____	____
(h) Total assets (at year-end)	____	____	____
(i) Total liabilities (at year end)	____	____	____
(j) Total shareholders' equity(at year-end)	____	____	____

Ans:

	Cash Dividend	Stock Dividend	Stock Split
a)	N	I	N
b)	N	N	D
c)	N	I	N
d)	D	D	N
e)	N	I	I
f)	N	N	N
g)	N	D	D
h)	D	N	N
i)	N	N	N
j)	D	N	N

Difficulty: Medium
Level of Learning: Application
Topic: LO5, 6, 7

152. On July 1, 1999, NTC had outstanding 10,000 common shares, (originally sold at $12); the quoted market price currently is $16. The company declared and issued a 10% common stock dividend. Give the entry.
Ans:

Retained earnings (1,000 sh. x $16)	16,000	
Common shares		16,000

Difficulty: Medium
Level of Learning: Application
Topic: LO6

153. Match the following terms and definitions by entering the appropriate letters to the left.

Terms

A. Stock dividend
B. Liability dividend
C. Property dividend
D. Cash dividend
E. None of these.

Definitions

___ 1. Issuance of additional shares to each shareholder at no cost.
___ 2. Issuance of a dividend that decreases both retained earnings and noncash assets.
___ 3. Issuance of a stock split.
___ 4. A dividend that does not change total assets, liabilities, or shareholders' equity.
___ 5. A dividend that decreases cash and shareholders' equity when declared and paid.
___ 6. A dividend that decreases retained earnings and increases contributed capital.

Ans: 1: A, 2: C, 3: E, 4: A, 5: D, 6: A
Difficulty: Medium
Level of Learning: Application
Topic: LO5, 6, 7

154. Several types of dividends and other items are identified below by letter. Match the type of dividends with its characteristic by entering letters in the spaces provided.

Type of Item

A. Cash dividend
B. Liquidating dividend
C. Property dividend
D. Stock dividend
E. Stock split
F. Stock dividend and stock split
G. None of these

Characteristic

___ 1. Increases the number of shares outstanding by decreasing the book value per share proportionately.
___ 2. Creates a current liability and decreases retained earnings when declared (no gain or loss recorded).
___ 3. Decreases retained earnings and increases contributed capital accounts.
___ 4. Decreases retained earnings and noncash assets.
___ 5. Results in no change to assets, debt, or total shareholders' equity.
___ 6. Represents a return of capital rather than a distribution of earnings.

Ans: 1: E, 2: A, 3: D, 4: C, 5: F, 6: B
Difficulty: Medium
Level of Learning: Application
Topic: LO6

155. Several years ago, a corporation set up a reserve for storm losses in the amount of $300,000 as an appropriation of retained earnings. During the current year, the company suffered a $85,000 hurricane loss that was not covered by insurance. The firm reduces appropriations when their purpose has been fulfilled. Give the entry(s) to record the loss and provide any appropriate explanation.

Ans:

Casualty loss	85,000	
Plant		85,000
Retained earnings, appropriated	85,000	
Retained earnings		85,000

Difficulty: Medium
Level of Learning: Application
Topic: LO7

156. Propertee, Inc. declared a dividend on May 1 payable in shares of Milly, Inc. (original cost: $4 per share, acquired at the beginning of the current year) to Propertee shareholders of record on June 1. The payment date is July 1. The dividend requires 20,000 shares of Milly to be distributed. Market prices of Milly/share were: May 1: $6; June 1: $8; July 1: $9. Provide the entry at declaration of the dividend.

Ans:

Retained earnings	120,000	$6(20,000)	
Investment	40,000	($6-$4)(20,000)	
Property dividend payable			120,000
Gain on investment			40,000

Difficulty: Medium
Level of Learning: Application
Topic: LO6

157. On October 1, 1999, XBC declared a dividend to its common shareholders by issuing one share of YTC, preferred share, \$.60 nopar (held as a long-term investment) for each of the 15,000 common shares of XBC. On declaration date, the YTC shares were selling at \$7 per share. The YTC shares originally were purchased by XBC at \$9 per share; they were transferred to the XBC shareholders on January 30, 2000, when their quoted market price was \$7.50 per share. Give the following entries for XBC:

(a) At date of declaration:

(b) At date of payment:

Ans: (a)At date of declaration:

Retained earnings (15,000 sh. x \$7)	105,000	
Loss on disp. of investment	30,000	
Investment in YTC preferred shares		30,000
Prop. dividend payable		105,000

(b)At date of payment:

Prop. div. payable	105,000	
Investment in YTC preferred shares		105,000

Difficulty: Medium

Level of Learning: Application

Topic: LO6

158. ATC's balance sheet on December 31, 20x1, showed the following:

Cash	$30,000	Current liabilities	$90,000
Other current assets.	70,000	Long-term liabilities	170,000
Operational assets (net)	200,000	Common shares, 5000	
Other assets	100,000	shares outstanding	100,000
		Retained earnings	40,000
	$400,000		$400,000
	========		========

Using this information, answer the following questions:

(a) What is the absolute maximum amount of cash dividends that can be paid immediately?____.
(b) What is the book value per common share? $_________________.
(c) Assuming a $10,000 cash dividend is declared, what entries would be made on each of the following dates:
(1) Declaration date:
(2) Date of record:
(3) Date of payment:
Ans: (a) $30,000 (cash balance).

(b) $140,000 ÷ 5,000 = $28

(c)

(1)Retained earnings	10,000	
Dividends payable		10,000

(2) None

(3) Dividends payable	10,000	
Cash		10,000

Difficulty: Medium
Level of Learning: Application
Topic: LO6

159. On July 1, 1999, NDC had outstanding 20,000 common shares, (originally sold at $5 per share); the current quoted market price is $7 per share. The company declared and issued a 10% common stock dividend; however, stock rights for 100 fractional shares were issued (10 shares). The rights currently had a quoted market price of $.80 each. Give the entry to record the dividend.
Ans:

Retained Earnings (2,000 sh. x $7)	14,000	
Common shares (1,990 sh. x $7)		13,930
Common stock warrants outstanding (100 ÷ 10) x $7		70

Difficulty: Medium
Level of Learning: Application
Topic: LO3

160. On July 1, 1999, the Board of Directors of BXC declared a stock dividend that required the issuance of 5,000 common shares. The common shares had a market value at this date of $18 per share. Retained earnings amounted to $900,000. Give the entry to record the stock dividend (the shares were issued), assuming:
The 5,000 shares represented 10% of the previously outstanding shares.
Ans:

Retained earnings	90,000	
Common shares (5,000 x $18 par value)		90,000

Difficulty: Medium
Level of Learning: Application
Topic: LO3

161. During December 1999, BRC declared and issued a 1 for 5 stock dividend on its 100,000 outstanding common shares. The per share amounts were: original average issue price $16; current market price (end 1999) $13; and the average market price for 1999, $15. Give the required journal entry to record the simultaneous declaration and issuance of the stock dividend.
Ans: Small stock dividend-Use market value:

Retained earnings (100,000 sh. ÷ 5) x $13	260,000	
Common shares		260,000

Difficulty: Medium
Level of Learning: Application
Topic: LO3

162. Match the following terms with the appropriate definitions.

Terms

A. Common shares
B. Preferred shares
C. Preferred shares, non-participating
D. Par value shares
E. Preferred shares, cumulative
F. No-par shares
G. No-par, stated value shares
H. Shares purchased on credit

Definitions

___ 1 The basic issue of shares.
___ 2. Shares on which dividends in arrears must be paid before current dividends can be paid.
___ 3. No-par shares with an assigned "value," but not usually specified in the charter.
___ 4. Shares with specified differences from the basic shares.
___ 5. Shares with a minimum "value" always specified in the charter.
___ 6. Subscribed shares.
___ 7. Shares that are limited to a specified dividend rate per year.
___ 8. Shares that have no minimum amount that must be paid in at first sale.

Ans: 1:A, 2:E, 3:G, 4:B, 5:D, 6:H, 7:C, 8:F

Difficulty: Medium
Level of Learning: Application
Topic: LO1

163. Match the following terms with the appropriate definitions.

Terms
A. Treasury shares
B. Convertible shares
C. Subscribed shares
D. Callable shares
E. Authorized shares
F. Unissued shares
G. Redeemable shares
H. Cumulative shares

Definitions
___ 1. Shares that have been sold under contract, but not yet issued because collection has not been made.
___ 2. The difference between total shares issued and total shares outstanding.
___ 3. Shares on which dividends in arrears must be paid prior to payment of any current dividends.
___ 4. Shares that may, at the option of the holder, be turned in for another security.
___ 5. Shares that have been issued, repurchased, and held.
___ 6. Shares that, at the option of the issuer, may be called in and paid off.
___ 7. The difference between authorized and issued shares.
___ 8. Shares which, at the option of the shareholder, may be surrendered for a specified amount of cash.

Ans: 1: C, 2: A, 3: H, 4: B, 5: A, 6: D, 7: F, 8: G
Difficulty: Medium
Level of Learning: Application
Topic: LO1

164. DXC has the following outstanding shares:
$5 Preferred, 2,000 shares issued at $100 per share common, no-par value, 5,000 shares issued at $60 per share
(Matching dividend, if applicable $3)
Compute the amount of dividends per share payable to each class of shares for each independent case. Show computations.

	Per Share **Preferred Stock Provisions**	**Preferred**	**Common**
(a)	Preferred is noncumulative and non-participating. Dividends declared, $40,000	$__________	$__________
(b)	Preferred is cumulative and non-participating; in arrears three years (in addition to the current year). Dividends declared, $65,000	$__________	$__________
(c)	Preferred is cumulative, in arrears three years (in addition to the current year); fully participating. Dividends declared, $75,000.	$__________	$__________

Ans:

Share	capital common	=	$300,000	(60
	preferred	=	$200,000	(40%)
	total	=	$500,000	(100%)
			=======	

(a)	Preferred: $2,000 x $5 = $10,000 ÷ 2,000 shares	=	$5.00
	Common: $40,000 - $10,000 = $30,000 ÷ 5,000 shares	=	$6.00
(b)	Preferred: $30,000 + $10,000 = 40,000 ÷ 2,000 shares	=	$20.00
	Common: $65,000 - $40,000 = $25,000 ÷ 5,000 shares	=	$5.00
(c)	Preferred: $30,000 + $10,000 + $8,000(ii) = $48,000 ÷ 2,000	=	$24.00
	Common: $15,000(i) + $12,000(iii) = $27,000 ÷ 5,000	=	$5.40

(i)	5,000 x $3	
(ii)	75,000 - (30,000 - 10,000) - 15,000	= 20,000; 20,000 x
	(200,000 ÷ [200,000 + 300,000])	= 8,000
(iii)	20,000 x (300,000 ÷ [200,000 + 300,000])	= $12,000

Difficulty: Medium
Level of Learning: Application
Topic: LO6

165. SXC reported income during four successive years as follows: $1,000, $2,000, $3,000, and $11,000. The share capital outstanding consisted of 3,000 common shares issued at $20 each, and 5,000, $.50 preferred shares issued at $10 each. (Matching common dividend, if applicable, $1). If income in full were declared as dividends each year, determine the amount that would be paid on each class of shares for each of the four years assuming:

		Year	Common	Preferred
(a)	Preferred is noncumulative and non-participating.	1	$________	$________
		2	$________	$________
		3	$________	$________
		4	$________	$________
(b)	Preferred is cumulative and non-participating.	1	$________	$________
		2	$________	$________
		3	$________	$________
		4	$________	$________
(c)	Preferred is noncumulative and fully participating.	1	$________	$________
		2	$________	$________
		3	$________	$________
		4	$________	$________
(d)	Preferred is cumulative and fully participating.	1	$________	$________
		2	$________	$________
		3	$________	$________
		4	$________	$________

Ans: Annual preferred dividend = $2,500 (5,000 x $.50)

		Common	Preferred
(a)	Year 1	$None	$1,000
	Year 2	$None	$2,000
	Year 3	$500	$2,500
	Year 4	$8,500	$2,500
(b)	Year 1	$None	$1,000
	Year 2	$None	$2,000
	Year 3	$None	$3,000
	Year 4	$7,000	$4,000
(c)	Year 1	$None	$1,000
	Year 2	$None	$2,000
	Year 3	$500	$2,500
	Year 4	$6,000	$5,000
(d)	Year 1	$None	$1,000
	Year 2	$None	$2,000
	Year 3	$None	$3,000
	Year 4	$5,182	$5,818*

		C	P
*	arrear dividends = 3($2,500) - $6,000 =		$1,500
	current year	$3,000	2,500
	remaining for participation: $4,000		
	$4,000 x (60,000 ÷ [60,000 + 50,000])	2,182	
	$4,000 x (50,000 ÷ [60,000 + 50,000])		1,818
	$5,182		$5,818
	======		======

Difficulty: Medium
Level of Learning: Application
Topic: LO6

166. On January 1, 1999, the accounts of CXC reflected the following:

The single-transaction method is used. On February 1, 1999, CXC purchased 5,000 of its own shares at $2.10 per share. Later, on
December 1, 1999, CXC sold 2,000 of these treasury shares at $1.50 per share. Give the journal entry on December 1, 1999, to record this sale of treasury stock.

Common shares, 40,000 shares outstanding.	$80,000
Contributed capital from treasury stock transactions.	1,500
Retained earnings.	50,000

Ans:

Cash (2,000 x $1.50)	3,000	
Contributed capital from T.S. transactions	1,200	
Treasury stock (2,000 x $2.10)		4,200

Difficulty: Medium
Level of Learning: Application
Topic: LO4

167. Explain the options available to a corporation that issues share subscriptions where partial payment has been received but the subscriber defaults on the balance.
Ans: A corporation has three options available. They may issue shares in proportion to the cash received. They may also return all payments to the subscriber and issue no shares. Finally, the corporation may retain the money received. The third option is not common; however, legislation does not prohibit it.
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO2

168. Brimley Corp. issued 5,000 common shares, no par, and 800 preferred shares. At the time of issue the common shares were selling at $30 per share and the preferred at $25. Total cash received was $162,000. Prepare the journal entry to record the issuance of the shares.

Ans: Since market prices are known the proportional method can be used.

Market value of common (5,000 shares x $30)	$150,000 (88% of total)
Market value of preferred (800 shares x $25)	20,000 (12% of total)
Total market value	$170,000

Allocation of lump-sum sale price of	$162,000
Common ($162,000 x 88%)	$142,560
Preferred ($162,000 x 12%)	19,440
	$162,000

Journal Entry:

Dr. Cash	162,000	
Cr. Common shares		142,560
Cr. Preferred shares		19,440

Difficulty: Medium
Level of Learning: Application
Topic: LO6

169. Brimley Corp. issued 5,000 common shares, no par, and 800 preferred shares. At the time of issue the common shares were selling at $30 per. There is no current market value for the preferred shares. Total cash received was $162,000. Prepare the journal entry to record the issuance of the shares.

Ans: Since market values for preferred shares are not known, the incremental method should be used.

Journal Entry:

Dr. Cash	162,000	
Cr. Common shares (5,000 shares		$150,000
Cr. Preferred shares		12,000

Difficulty: Medium
Level of Learning: Application
Topic: LO2

170. Explain what is meant by share issue costs and how they are treated for accounting purposes.
Ans: Share issue costs include legal fees, accounting fees, underwriting costs, printing, clerical and other costs associated with the share issue. There are three methods to deal with share issue costs:

Offset Method: Record the costs as a reduction in the amount received from the sale of the shares as they are argued to be one-time costs. Share costs are debited to the share capital account.

Retained earnings method: Share issue costs are charged directly to retained earnings.
Deferred Charge Method: Less common method. Costs are recorded as a deferred charge and amortized over a reasonable time period.
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO2

171. Explain why companies may want to reacquire their own shares?
Ans: (1) To increase earnings per share
(2) To provide cash flow to shareholders in lieu of dividends
(3) To acquire shares when they appear to be undervalued
(4) To reduce the possibility of a takeover bid
(5) To reduce future dividend payments (i.e. less shares outstanding)
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO3, 4

Use the following to answer questions 172-178:

On 2 January 20X4, GHI Corporation was incorporated in the province of Ontario. It was authorized to issue an unlimited number of no-par value common shares, and 10,000 shares of no-par, $8, cumulative and non-participating preferred. During 20X4, the firm completed the following transactions:

8 Jan.	Accepted subscription for 40,000 common shares at $12 per share. Down payment on the subscribed shares totalled $150,000.
30 Jan	Issued 4,000 preferred shares in exchange for the following assets: Machinery With a fair market value of $35,000, a factory with a fair market value of $110,000, and land with an appraised value of $295,000.
15 Mar.	Machinery with a fair market value of $55,000 was donated to the company.
25 Apr.	Collected the balance of the subscriptions receivable and issued common Shares.
30 Jun.	Purchased 2,200 common shares at $18. per share. The shares were retired.
31 Dec.	Declared sufficient cash dividends to allow a $1. Per share dividend for Outstanding common shares. The dividend is payable on 10 January 20X2, To shareholders of record on 5 January 20X2.
31 Dec.	Closed the income summary to retained earnings. The income for the period. Was $98,000.

172. Prepare Journal entries to record the subscription of common shares

Ans: Cash	$ 150,000	
Stock subscription receivable	$ 330,000	
Common shares subscribed (40,000 shares)		$ 480,000

Difficulty: Medium
Level of Learning: Application
Topic: LO2

173. Prepare Journal entries to record the issuance of preferred shares in exchange for assets; recorded at fair market value of the assets in the absence of a value for the preferred shares.

Ans: Machinery	$ 35,000	
Factory	$ 110,000	
Land	$ 295,000	
Preferred shares (4,000 shares)		$440,000

Difficulty: Medium
Level of Learning: Application
Topic: LO2

174. Prepare Journal entries to record the receipt of donated assets.

Ans: Machinery	$ 55,000	
Contributed capital – donations		$55,000

Difficulty: Medium
Level of Learning: Application
Topic: LO2

175. Prepare Journal entries to record the receipt of cash for subscribed shares and issuance of shares.

Ans: Cash	$ 330,000	
Stock subscription receivable		$ 330,000

Difficulty: Medium
Level of Learning: Application
Topic: LO2

176. Prepare Journal entries to record the acquisition and retirement of common shares.

Ans: Common Shares ($480,000 / 40,000) x 2,200	26,400	
Retained Earnings	13,200	
Cash ($18 x 2,200)		39,600

Difficulty: Medium
Level of Learning: Application
Topic: LO2, 3

177. Prepare Journal entries to record dividends declared.

Ans: Retained Earnings	69,800	
Dividends payable, preferred shares		32,000
Dividends payable, common shares		37,800

Preferred dividend: 4,000 shares x 8
Common dividend: 37,800 shares x $1
Difficulty: Medium
Level of Learning: Application
Topic: LO6

178. Prepare Journal entries to record the closing of the income summary account.

Ans: Income Summary	98,000	
Retained earnings		98,000

Difficulty: Medium
Level of Learning: Application
Topic: LO6

179. On December 31st, 2011, JKL Inc. had the following account balances:

Common Shares	
(No par, 10,000 shares issued, 8,000 shares outstanding)	$100,000
Preferred Shares	
($1, non-cumulative, 10,000 shares issued and outstanding)	$ 50,000
Retained Earnings	$180,000
Treasury Shares (2,000 shares)	($20,000)
Total	$310,000

During 2012, the following took place:

- JKL Inc. had a total Comprehensive Income of $150,000.
- During 2012, JKL Inc. bought 2,000 shares of MNO Inc. for $45 per share. On December 31st, 2012, these shares were trading at $60 per share. These shares, which were all on hand at the end of 2012, were designated by management as FVTOCI.
- Half of the treasury shares held by management at the start of 2012 were sold during the year for $15,000.
- JKL declared at total of $30,000 in dividends, which included a common stock dividend valued at $10,000.

Required:
A) Prepare a Statement of Changes in Equity for JKL Inc. as per IFRS as at December 31st, 2012.
B) Briefly explain how JKL Inc's reporting requirements would differ if it complied with ASPE instead of IFRS.

Ans:

A)

JKL Inc.

Statement of Changes in Equity

For the year ended December 31st, 2012

	Common Stock	Preferred Shares	Retained Earnings	Cumulative OCI	Treasury Shares	Contributed Surplus-Treasury Shares	Total
Balances, January 1, 2012	100,000	50,000	180,000		-20,000		310,000
Comprehensive Income			120,000	30,000			150,000

Treasury Share - resale					10,000	5,000	15,000
Dividends:							-
Cash			-20,000				-20,000
Common Stock Dividend	10,000		-10,000				-
Balances, December 31st, 2012	110,000	50,000	270,000	30,000	-10,000	5,000	455,000

B) Had JKL Inc. been following ASPE, only a Statement of Retained Earnings would be required, not a Statement of Changes in Equity. Moreover, there is no Comprehensive Income under ASPE. This would mean that the shares in MNO Inc. could not be designated as FVTOCI. These shares would be designated as FVTPL.

Difficulty: Hard
Level of Learning: Application
Topic: LO8, 9

Beechy, Conrod & Farrell *Intermediate Accounting* Fifth Edition, Volume 2 – Test Bank
Chapter 14 – Complex Debt and Equity Instruments

1. The accounting classification of a financial instrument is determined by its tax status.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

2. Induced conversions of convertible debt arise when the debtor offers a "sweetener" to encourage the creditor to promptly convert the debt.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 2

3. When stock rights are issued to current shareholders, it may require more than one such right to later acquire one additional share of the stock covered by the rights.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO3

4. The measurement date of a compensatory stock option must precede the date of grant.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 3

5. General debt carries a firm commitment to interest payments and repayment of capital at maturity.

   Ans: True
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 1

6. Options are ONLY for the purpose of buying or selling financial instruments.

   Ans: False
   Difficulty: Easy
   Level of Learning: Knowledge
   Topic: LO 7