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BIRZEIT UNIVERSITY
FACULTY OF BUSINESS AND ECONOMICS
ACCOUNTING DEPARTMENT

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FIRST SEM. 2013/2014
FIRST HOUR EXAM

ACCT336

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Student #: 1111125 Section Time: 9:30 W: R 9:30

Question 1 (12 points)

On March 1, 2013, Union bank contracted Nabali & Fares Construction Co. to construct a building for \$2,000,000 on land costing \$200,000 purchased from the contractor and included in the first payment.

Construction was begun on May 1, 2013 and was completed on December 31, 2013. Union bank made the following payments to the construction company during 2013:

<u>Date</u>	<u>Payment</u>
May 1, 2013	\$600,000 ^{200,000}
September 1, 2013	600,000
December 31, 2013	<u>1,000,000</u>
Total	<u>\$2,200,000</u>

Nabali & Fares completed the building on December 31, 2013. Union Bank had the following debt outstanding at December 31, 2013.

- 1) 15%, 3-year note in the amount of \$500,000, to finance purchase of land and construction of the building, dated May 1, 2013, with interest payable annually on December 31.
- 2) 10%, 5-year note in the amount of \$1,200,000 dated December 31, 2010, with interest payable annually on December 31.

Required

- a) Determine the amount of interest to be capitalized in 2013 in relation to the construction of the building.
- b) Prepare the journal entry to record the capitalization of interest and the recognition of interest expense, if any, at December 31, 2013.

$$\frac{11.5}{12}$$

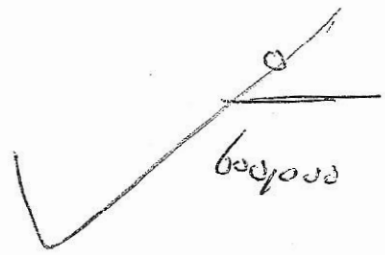
Solution

a)

Weighted Average Acc. exp.

W.A.A.E

Date	Amount	x	Capitalization period
Mar, 2013	600,000		$\frac{8}{12}$
September 1	600,000		$\frac{4}{12}$
Dec. 31	1,000,000		0
	<u>2,200,000</u>		



Avoidable interest = ~~500,000~~ * $500,000 \times 8\%$ = 75,000
 + $100,000 \times 10\%$ = 10,000

85,000

~~Actual interest~~ \Rightarrow

Amount to capitalize is equal to Avoidable interest because it is lower than Actual cost interest

Actual interest $500,000 \times 8\% \times \frac{8}{12} = 7,500$

$1,200,000 \times 10\% \times \frac{12}{12} = 120,000$
~~127,500~~ / 70,000

b)

Dr Building - capitalized interest 85,000

Dr interest exp 42,500

Cr cash ~~127,500~~

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Question 2 (14 points)

Use the following table to fill in your answer for each case and company.

Case	Recognized Loss (if any)	Recognized Gain (if any)	Deferred Gain (if any)	FMV of New Asset
Ramallah Co. Case (1)	150,000	10,000		70,000 58,000
Birzeit Co. Case (1)		20,000 8,000		70,000 70,000
Ramallah Co. Case (2)		150,000 17,14	8,000 8,286	62,000 49,714
Birzeit Co. Case (2)			8,000 8,000	62,000 62,000
Ramallah Co. Case (3)		6,000	9,000 9,000	45,000 45,000
Birzeit Co. Case (3)	5,000			75,000

Case (1)

On March 1, Ramallah Co. exchanged productive assets with Birzeit Co.. Ramallah's asset is referred to below as "Asset A", and Birzeit's is referred to as "Asset B". The following facts pertain to these assets. Assume the exchange has a commercial substance.

Information	Ramallah Company (Asset A)	Birzeit Company (Asset B)
Original cost	\$150,000	\$90,000
Acc. dep. (to date of exchange)	90,000	40,000
Fair value at date of exchange	70,000	68,000
Cash received	12,000	
Cash paid		12,000

Ramallah: $B.V. 150,000 - 90,000 = 60,000$
 gain loss
 $F.V. 70,000$
 $F.V. 70,000 + 0 = 70,000$
 gain received = $\frac{12,000}{70,000 + 12,000} \times 60,000 = 1463$
 $F.V. 70,000 = (F.V. + 12,000)$
 $F.V. = 70,000 = 12,000 + 58,000$

Case (2)

Using the same information in case (1) but, assume that the exchange of Assets A and B lacks commercial substance.

Case (3)

Information	Ramallah Company (Asset A)	Birzeit Company (Asset B)
Original cost	\$150,000 <i>B.V. 60,000</i>	\$90,000 <i>B.V. 20,000</i>
Acc. dep. (to date of exchange)	90,000	40,000
Fair value at date of exchange	75,000 <i>gain 15,000</i>	? <i>45,000 loss 5,000</i>
Cash received	30,000 <i>paid</i>	
Cash paid		30,000

Assume that the exchange of Assets A and B lacks commercial substance.

$$75,000 + 0 = F.V. + 30,000$$

$$= 45,000$$

$$\frac{30,000}{30,000 + 45,000} \times 15,000 = 6,000 \text{ gain}$$

deferred $15,000 - 6,000 = 9,000$

Question 3 (12 points) \ 17 / 2012

On July 1, 2012, Maher Co. purchased a manufacturing machine for \$648,000. The machine has a five year estimated useful life and a \$90,000 estimated salvage value. Maher expects to manufacture 1,395,000 units over the life of the machine. During year 2013, Maher manufactured 280,000 units.

For each item, calculate depreciation expense for year 2013 for the manufacturing machine described above using the method listed. Round all amounts to the nearest whole number.

Depreciation Method	Amount
1. Units of production	112,000
2. Sum-of-the-years'-digits	167,400
3. Double-declining-balance	233,280
4. Straight-line	111,600

① unit of prod = $\frac{648,000 - 90,000}{1,395,000} = 0.4 \times 280,000$

② $\frac{5}{15} (648,000) \times \frac{6}{12} + \frac{4}{15} (648,000) \times \frac{6}{12}$
 $93,000 + 74,400 = 167,400$

③ $\frac{1}{5} \times 2 (648,000) \times \frac{6}{12} + 400 (648,000 - 129,600) \times \frac{6}{12}$
 $129,600 + 103,680 = 233,280$

④

$$B.V = 7000,000$$

3000,000 Acceler

Question 4 (20 points)

Each of the following situations is independent:

1. Rantisi Company uses special pressing equipment in its pressing olive oil service. The equipment was purchased in January 2011 for \$10,000,000 and had an estimated useful life of 10 years with no salvage value. At December 31, 2013, new technology was introduced that would accelerate the obsolescence of Rantisi's equipment. Rantisi's controller estimated that expected future net cash flows on the equipment will be \$6,500,000 and that the fair value of the equipment is \$5,500,000. Rantisi intends to continue using the equipment, but it is estimated that the remaining useful life is 4 years. Rantisi uses straight-line depreciation. The fair value of the equipment at December 31, 2014, is estimated to be \$6,000,000.

~~10,000,000~~ 1000,000 Dep

$$\frac{5,500,000}{4} = 1,375,000$$

2. Assume that Rantisi intends to dispose of the equipment and that it has not been disposed of as of December 31, 2014. It is expected that the cost of disposal will be \$100,000.

$$B.V = 2000,000 - 400,000 = 1600,000$$

3. Climatic Company purchased a patent in January 2010 for \$2,000,000 and had an estimated useful life of 8 years with salvage value in the amount of \$20,000. At December 31, 2013, Climatic's controller estimated that expected future net cash flows on the patent will be \$900,000 and that fair value of the patent is \$830,000. Climatic intends to continue using the patent, but it is estimated that the remaining useful life is 2 years. Climatic uses straight-line depreciation. The fair value of the patent at December 31, 2014 is estimated to be \$1,500,000.

180,000

1,200,000

4. Pinar Company owned a trade name at December 31, 2008 at a cost of \$5,000,000 with indefinite useful life and no salvage value. At December 31, 2013, it is determined that the fair value of the trade name is \$4,000,000. Assume that Pinar intends to dispose of the trade name and that it has not been disposed of as of December 31, 2014. It is expected that the cost of disposal will be \$150,000. The fair value of the trade name at December 31, 2014 is estimated to be \$4,700,000.

4000,000

5. Bisan Company spent \$6,000,000 developing its new "Bisan" software package. Of this amount, \$2,000,000 was spent before technological feasibility was established for the product, which is to be marketed to third parties. At December 31, 2013, new technology was introduced that would accelerate the obsolescence of the software. Bisan's controller estimated that expected future net cash flows from the software will be \$3,500,000 and that the fair value of the software is \$3,000,000. Bisan intends to continue selling the software. Bisan estimated that the remaining useful life is 4 years for this software with total revenues of \$15,000,000. During 2014 Bisan realized revenues of \$2,500,000. The fair value of the software at December 31, 2014 is estimated to be \$3,500,000.

$$\frac{3000,000}{4} = 750,000$$

$$\frac{2500,000}{1500,000} \times 3000,000 = 500,000$$

6. Presented below is net asset information related to Bravo Division of Asalah Co.

Bravo Division
Net Assets
As of December 31, 2013

Cash		\$0	\$80,000,000
Receivables		\$	10,000,000 - 2,000,000
Property, plant, and equipment (net)		01	60,000,000 + 1,000,000
Goodwill		4	4,000,000
Less: Notes payable		60	(54,000,000) - 4,000,000
Net assets			<u>\$100,000,000</u>

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At December 31, 2013, Bravo division experienced operating losses. In addition, it now appears that it will generate substantial losses for the foreseeable future. It is determined that the fair value of the Bravo division is \$96,000,000. The recorded amounts for Bravo's net assets (excluding goodwill) is the same as fair value, except for property, plant and equipment, which has a fair value of \$1,000,000 above carrying value, receivables, which has a fair value of \$2,000,000 below carrying value and notes payable, which has a fair value of \$4,000,000 below carrying value.

The following four responses are required for each item (if any).

- Select from the list below the proper impairment test/s code.
- Compute the amount of impairment loss,
- Compute the depreciation/amortization expense
- Compute the recovery of impairment loss.

400,000

46,000,000
- 99,000,000

3,000,000

Impairment Test Type	Code
Recoverability test	A
Fair value test	B
Fair value of business unit	C
Fair value of implied Goodwill	D

Use the following table to fill in your answer for each situation.

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Item	Type of Test/s	Impairment Loss at Dec. 31, 2013 (if any)	Depreciation/Amortization Expense for 2014 (if any)	Recovery of Impairment Loss at Dec. 31, 2014 (if any)
1.	A ✓ B	there is an impairment 1,500,000	1,375,000	No Restoration
2.	A ✓ B	1,400,000	No dep.	500,000 Restoration of impairment loss
3.	A ✓ B	1,400,000	1,400,000	No Restoration
4.	✓ B	1,000,000	No dep Amort.	No Restoration
5.	A ✓ B	1,000,000	Amort. 750,000	No restoration
6.	C ✓ D	1,000,000	No Amort.	No Restoration

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Question 5 (12 points)

Space Company is involved in a number of projects related to its future success. Some of these projects are considered operational activities while others are considered research and development (R&D) activities. Space must determine the proper accounting treatment in assessing certain expenditures for the year.

From the answer choices listed below, select the proper accounting treatment for each of the expenditures listed below. Each choice may be used once, more than once, or not at all.

Expenditure	Choice
1. Executive Salaries	H
2. Costs incurred to upgrade current production facility	C
3. Legal fees to obtain a patent on a new rocket engine	B
4. Salaries of research staff designing new rocket engine	F
5. Marketing research costs to promote new rocket engine	H
6. Costs incurred to improve engine currently in production	X
7. Material, labor, and overhead costs of new rocket engine	F E
8. Costs incurred to successfully defend patent on the new rocket engine	B
9. Acquisition of machinery to be used on current and future R&D projects	D
10. Research costs by Electro Company under contract for new rocket engine	F
11. Research costs incurred under contract for Palestine Company and billed monthly	A
12. Costs of quality control in early stages of new rocket engine commercial production	G

Answer Choices	
A. Record as receivable	E. Expense as consumed as R&D expense
B. Capitalize and amortize	F. Expense immediately as R&D expense
C. Capitalize and depreciate	G. Expense as manufacturing cost
D. Capitalize and depreciate as R&D expense	H. Expense as operating expense