FINANCIAL ACCOUNTING II

1. EQUITY

Loxley Corporation is authorized to issue 50,000 shares of $10 par value ordinary shares. During 2022, Loxley took part in the following selected transactions.

1. Issued 5,000 shares at $45 per share, less costs related to the issuance of the shares totaling $7,000.
2. Issued 1,000 shares for land appraised at $50,000. The shares were actively traded on a national securities exchange at approximately $46 per share on the date of issuance.
3. Purchased 500 treasury shares at $44 per share. The treasury shares purchased were issued in 2021 at $40 per share.

Instructions

1. Prepare the journal entry to record item 1.
2. Prepare the journal entry to record item 2.
3. Prepare the journal entry to record item 3 using the cost method.

Answers

1. Cash	218,000*	
Share Capital-Ordinary		50,000**
Share Premium-Ordinary		168,000
*(5,000 × $45) - $ 7,000		
**5,000 × $10		
2. Land	46,000*	
Share Capital-Ordinary		10,000**
Share Premium-Ordinary		36,000
*1,000 × $46		
**1,000 × $10		
3. Treasury Shares	22,000*	
Cash		22,000
*500 × $44		

2. DILUTIVE SECURITIES AND EARNINGS PER SHARE

Schuss SA issued €3,000,000 of 10%, 10-year convertible bonds on April 1, 2022, at 98. The bonds were dated April 1, 2022, with interest payable April 1 and October 1. Bond discount is amortized semiannually using the effective-interest method. The net present value of the bonds without the conversion feature discounted at 12% (its market rate) was €2,655,888.

On April 1, 2023, €1,000,000 of these bonds were converted into 30,000 shares of €20 par value ordinary shares. Accrued interest was paid in cash at the time of conversion.

Instructions

1. Prepare the entry to record the issuance of the convertible bond on April 1, 2022.
2. Prepare the entry to record the interest expense at October 1, 2022.
3. Prepare the entry or entries to record the conversion on April 1, 2023. (The book value method is used.)

Answers

1.

Cash	2,940,000*	
Bonds Payable		2,655,888
Share Premium-Conversion Equity		284,112

*€3,000,000 × 98%

2.

Interest Expense	159,353*	
Bonds Payable		9,353
Cash		150,000**

*(€2,655,888 × 12%) ÷ 2
**(€3,000,000 × 10%) ÷ 2

3.

Interest Expense	159,914*	
Bonds Payable		9,914
Cash		150,000**

*((€2,655,888 + €9,353) × 12%) ÷ 2
**(€3,000,000 × 10%) ÷ 2

Share Premium-Conversion Equity	94,704*	
Bonds Payable	891,719**	
Share Capital-Ordinary		600,000***
Share Premium-Ordinary		386,423

*€284,112 × (€1,000,000 ÷ €3,000,000)
**((€2,655,888 + €9,353 + €9,914) × (€1,000,000 ÷ €3,000,000)
***30,000 × €20

3. INVESTMENTS

Carow SA purchased on January 1, 2022, as a held-for-collection investment, €60,000 of the 8%, 5-year bonds of Harrison, Inc. for €65,118, which provides a 6% return. The bonds pay interest semiannually.

Instructions

1. Prepare Carow's journal entries for the purchase of the investment.
2. Prepare Carow's journal entries for the receipt of semiannual interest and premium amortization.

Answers

Date	Cash Received (a) $[€60{,}000 \times \frac{6}{12} \times 8\%]$	Interest Revenue (b) $[d_{n-1} \times \frac{6}{12} \times 6\%]$	Bond Premium Amortization (c) [a – b]	Carrying Amount of Bonds (d) $[d_{n-1} - c]$
Jan 1, 2022				65,118
July 1, 2022	2,400	1,954	446	64,672
Jan 1, 2023	2,400	1,940	460	64,212

1. Debt Investments	65,118	
Cash		65,118
2. Cash	2,400	
Debt Investments		446
Interest Revenue		1,954
Interest Receivable	2,400	
Debt Investments		460
Interest Revenue		1,940

4. REVENUE RECOGNITION (E18-28)

Celic SA manufactures and sells computers, which include an assurance-type warranty for the first 90 days. Celic offers an optional extended coverage plan under which it will repair or replace any defective part for 3 years from the expiration of the assurance-type warranty. Because the optional extended coverage plan is sold separately, Celic determines that the 3 years of extended coverage represents a separate performance obligation. The total transaction price for the sale of a computer and an extended warranty is €3,600 on October 1, 2022. Celic determines the standalone selling price of the computer and the warranty are €3,200 and €400, respectively. Based on historical experience, Celic estimates that it will incur €200 in costs to repair defects that arise within the 90-day coverage period for the assurance-type warranty. The cost of the computer is €1,440. Assume that the €200 in costs to repair defects in the computer occurred on October 25, 2022.

Instructions

1. Prepare the journal entry or entries to record the October transactions related to sale of the computer.
2. Briefly describe the accounting for the service-type warranty after the 90-day assurance-type warranty period.

Answers

1. To record sales revenue, warranties, and related COGS:

Cash	3,600	
Sales Revenue		3,200
Unearned Warranty Revenue		400
Cost of Goods Sold	1,440	
Inventory		1,440

   To record warranty expense on October 25, 2022:

Warranty Expense	200	
Cash, Parts, Labor		200

2. Celic recognizes warranty expenses linked with the assurance-type warranty as actual warranty costs are incurred during the first 90 days after the customer receives the computer. Celic recognizes revenue during the extended warranty period and recognizes the costs associated with providing the service-type warranty as they are incurred.

5. ACCOUNTING FOR INCOME TAXES

Youngman Corporation has temporary differences at December 31, 2022, that result in the following deferred taxes. All of these items are associated with the same taxing authority.

Deferred tax liability related to depreciation difference	$38,000
Deferred tax asset related to warranty liability	62,000
Deferred tax liability related to revenue recognition	96,000
Deferred tax asset related to litigation accruals	27,000

Instructions

Indicate how these balances would be presented in Youngman's December 31, 2022, statement of financial position.

Answers

Deferred tax liability ($38,000 + $96,000)	$134,000
Deferred tax asset ($62,000 + $27,000)	$ 89,000
Net deferred tax liability	$ 45,000

The net deferred tax liability of $45,000 should be reported as non-current deferred tax liability.