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American University of Beirut
School of Business
Accounting 220
2nd Exam
Time : 2 hrs

Instructor : Wael Hamdan

I Multiple choice	30 pt
II Gross Profit Method	20 pt
III Exchange of assets-boot received	15 pt
IV Depletion of Natural Resources	15 pt
V Effects of Inventory Errors	20 pt
Total	100 pt

I

1. For financial reporting purposes, the purchase discounts lost account is reported as a(n)

a. contra account to inventory.
b. liability.
c. addition to the cost of merchandise purchased.
d. financing expense.

2. Goods in transit at year-end purchased f.o.b. shipping point were appropriately recorded in the purchases account but were incorrectly excluded from the ending inventory. What effect will this omission have on the company's assets, liabilities, and retained earnings at year-end?

a. No effect, no effect, overstated.
b. No effect, no effect, understated.
c. Understated, no effect, overstated.
d. Understated, no effect, understated.

3. A $25,000 overstatement of the 1997 ending inventory was discovered after the financial statements for 1997 were published. The effect on the 1997 financial statements of the error in the ending inventory would be

a. current assets were overstated and pre-tax income was understated.
b. current assets were understated and pre-tax income was understated.
c. current assets were overstated and pre-tax income was overstated.
d. current assets were understated and pre-tax income was overstated.

4. The Hays Company sold merchandise to the Ross Company on September 15, 1998, and at the same time, Hayes agreed to repurchase the same merchandise from Ross during April 1999. This transaction is called a

a. conditional sale.
b. consignment.
c. product financing arrangement.
d. sale on approval.

5. Which inventory cost flow assumption normally will yield the highest cost of goods sold figure during a period of declining prices?

a. Weighted average.
b. First-in, first-out.
c. Last-in, first-out.
d. Moving average.

6. Assuming no inventory shortages, which of the following inventory cost flow methods will result in the same inventory dollar amount under either a periodic inventory system or a perpetual inventory system?

a. First-in, first-out.
b. Last-in, first-out.
c. Dollar-value LIFO.
d. Average cost.

7. In 1997, Hurst Corporation adopted the dollar-value LIFO inventory method. Hurst's inventory had a base-year cost of $200,000 at that time. The base year cost of the ending inventory for 1998 was $300,000 with an unadjusted cost of $360,000. What inventory cost should Hurst report in its December 31, 1998 balance sheet?

BY = 200 000
300 000
360000/x = 300 000
x = 1.2

a. $300,000.
b. $320,000.
c. $340,000.
d. $360,000.

8. Hanahan Manufacturing Company purchased inventory items from Hampton Suppliers on December 28, 1998 for $100,000. The terms of the purchase were 2%/10/net 30 and were shipped f.o.b. shipping-point. buyer The items were shipped December 30, 1998, received January 3, 1999, and paid for January 6, 1999. Shipping cost were $2,500. What amount should Hanahan include in its 1998 inventory in regards to this purchase?

a. $0.
b. $100,450.
c. $100,500.
d. $102,500.

9. On May 10, 1998, the Rainy Day Corporation should prepare which of the following entries to reflect the purchase commitment:

Amount of contract = 45000$
Contract signed on May 10
Execut° in 1999
→ market = 37500

		Dr.	Cr.
a.	Umbrella inventory	45,000	
	Accounts payable		45,000
b.	Purchase commitment	45,000	
	Accounts payable		45,000
c.	Deferred cost of inventory	45,000	
	Accounts payable		45,000
d.	No entry would be required on May 10, 1998.		

10- On December 31, 1998, the Rainy Day Corporation should prepare which of the following entries to reflect the effects of the commitment to purchase the umbrellas?

a. No entry would be required.

b. Umbrella inventory 45,000
   Accounts payable 45,000

c. Estimated loss on purchase commitment 7,500
   Estimated liability on purchase commitment 7,500

d. Umbrella inventory 37,500
   Estimated loss on purchase commitment 7,500
   Accounts payable 45,000

11- Mingwood's inventory data for the month of October is as follows:

	Cost	Retail
Inventory, 10/1	$15,000	$33,000
Purchases	45,000	92,000
Purchases discounts	(900)	
Freight in	1,400	
Markup, net		3,000
Markdowns, net		(2,000)
Sales		92,000
	60500	126000

60500/126000 = 48%
126000 - 92000 = 34000
34000 x 48% = 16320

Under the average cost retail method Mingwood's inventory at October 31 is

a. $16,725.
b. $16,456.
c. $16,325.
d. $16,070.

12- Assuming that you believe that a particular company has internally generated goodwill, which of the following costs would you capitalize and then amortize over their estimated useful lives?

a. The cost of maintaining the goodwill.
b. The cost of restoring some diminished goodwill.
c. Both the costs of maintaining and restoring the goodwill.
d. Internally generated goodwill should never be capitalized.

13. On March 1, 1998 Ohio Company paid $740,000 for all of the outstanding common stock of Wisconsin Corporation. The transaction was accounted for using the purchase method. Wisconsin had the following book balances on that date:

Cash	$ 80,000	
Inventory	210,000	180000
Property and Equipment (net)	440,000	490000
Patents (net)	50,000	
Liabilities	(130,000)	
Net assets	650,000	

On March 1 Wisconsin's inventory had a fair value of $180,000 and the property and equipment had a fair value of $490,000. What amount of goodwill should Ohio record for this transaction?

a. $100,000.
b. $ 90,000.
c. $ 80,000.
(d). $ 70,000.

14. Valdosta Corp. purchased a new machine for its cheese factory. Valdosta paid $75,000 in cash and signed a one-year, 10% note for $35,000. Following the purchase, Valdosta incurred freight charges of $3,000 to ship the equipment to its factory. After the machine arrived, Valdosta paid contractors $1,500 for installation. Valdosta also used $1,200 of milk and $300 of labor on trial runs. Production cost for the first six months were $15,000. What amount should Valdosta capitalize for the cost of this machine?

(a) $81,000.
b. $113,000.
c. $116,000.
d. $131,000.

15. Georgia Company exchanged similar productive assets with Alabama Company. The following information pertains to this exchange:

Georgia:	Book value of asset given up	$ 30,000.
	Market value of asset given up	40,000.
	Cash paid	100,000.
Alabama:	Book value of asset given up	$ 85,000.
	Market value of asset given up	140,000.
	Cash received	100,000.

What amount should Georgia record as the basis for the new asset?

a. $ 85,000.
(b). $130,000.
c. $140,000.
d. $185,000.

II Gross Profit Method

The Franklin Company had its entire inventory destroyed when a fire swept through the company's warehouse on April 30, 1998. Fortunately, the accounting records were locked in a fireproof safe and were not damaged. The following information for the period up to the date of the fire was taken from the accounting records:

Sales	$655,900
Sales returns	9,800
Purchases	395,900
Beginning inventory	178,500
Purchase returns	18,200
Freight in	8,500

REQUIRED:

1. Assuming that the gross profit has averaged 25 percent of selling price, what is the estimated value of the inventory destroyed in the fire? Show all calculations in good form.

2. Assuming that the markup percentage on cost is 40 percent, what is the estimated value of the inventory destroyed in the fire? Show all calculations in good form. Round calculations to the nearest dollar.

III Exchange of assets - boot received

Yoko Company exchanged a tract of land for a similar tract. Yoko had originally paid $35,000 for the tract it traded, however, its fair value was not known at the time of the exchange. The tract that Yoko received in the exchange had a fair value of $45,000 and a mortgage of $15,000 which Yoko assumed. Yoko also received cash of $10,000 as part of this exchange.

Required: Prepare the journal entry to record the above transaction for Yoko.

IV Depletion of Natural Resources

Kentucky Mining Company purchased some mining property on March 18, 1998, at a cost of $4,400,000. Geologists estimate that the company will be able to take 9,500,000 tons of ore out of the mine. Once the ore has been taken out, the company expects to be able to sell the remaining land for $400,000. However, prior to sale, the company will have to incur cost of $275,000 to restore the property to its original surface state.

REQUIRED:

1. Prepare the journal entry to record the purchase of the mining property on March 18, 1998.

2. Assuming that the company mines 500,000 tons of ore during 1998, prepare the journal entry for depletion that would be made at December 31, 1998.

3. During 1999, the company mined 2,000,000 tons of ore. Also, the geologists changed their estimate of the reserves available. Instead of 9,500,000 tons, as originally estimated, the extractable ore should have been estimated as only 8,700,000 tons. All other estimates remain the same. Prepare the December 31, 1999, depletion entry based on 1999 production and the new 1999 estimate of ore reserves.

V Effects of Inventory Errors

The Hollies Carpet Company reported the following amounts for cost of goods sold and income for the years 1998, 1999, and 2000:

Year	Cost of Goods Sold	Income
1998	$50,000	$ 9,000
1999	58,000	8,200
2000	72,000	13,600

During the annual audit at December 31, 1997, the CPA reviewed inventory transactions, and the following events and transactions were discovered:

1997: The ending inventory was overstated by $5,000.

1998: Merchandise purchased and received on November 30 for $2,500 was not recorded. However, it was correctly included in the ending inventory.

1999: Merchandise held on consignment by the Hollies Carpet Company was included in ending inventory for $6,000. The consigned merchandise was not recorded as a purchase.

Merchandise was shipped f.o.b. destination (seller) to the Grande Seasons Hotel on December 24, and it arrived on January 3, 2000. The merchandise cost $5,000 and was sold for $14,000. The sale was recorded on December 24, and the goods were excluded from the 1999 ending inventory.

2000: Merchandise ordered on December 26, costing $6,500, was shipped to Hollies Carpets on December 30, f.o.b. shipping point. The invoice was received on December 30 and a purchase was recorded. However, the goods were not included in inventory since the goods did not arrive until January 6, 2001.

REQUIRED: Prepare a schedule to calculate the correct amount of cost of goods sold and the correct amount of income for each of the years 1998, 1999, and 2000. Ignore income taxes. The company uses a periodic inventory system.