Course No: ACC 4024 **Course Title: Contemporary Accounting Issues** **Date: 20/09/2014** **No. of Questions: (5)** **Time: 2.25 hours** **Using Calculator (Yes)**	**University of Palestine** **Final Exam** **Summer Semester** **2013/2014** **Total Grade:**	**Instructor Name: Miss Laila Aldaoor** **Student No.: _________________** **Student Name: ________________** **College Name: Business and Finance** **Dep. / Specialist: Accounting-English** **Using Dictionary (No)**

Question One: *(20 Marks)*

1. Luther Corp. issued $35,000,000 par value 12% bonds at 101. One detachable stock purchase warrant was issued with each $1,000 par value bond. At the time of issuance, the warrants were selling for $6.50.
   Required: Use the incremental method to record the transaction.

2. MagTech Inc. requires funding to build a new factory and has decided to raise the additional capital by issuing $850,000 face value of bonds with a coupon rate of 10%. In discussions with investment bankers, it was determined that to help the sale of the bonds, detachable stock warrants should be issued at the rate of 5 warrants for each $1,000 bond sold. The value of the bonds without the warrants is considered to be $775,000, and the value of the warrants in the market is $75,000. The bonds sold in the market at issuance for $825,000.
   Required:
   (a) What entry should be made at the time of the issuance of the bonds and warrants? use the proportional method to record the transaction
   (b) If the warrants were non-detachable, would the entries be different?

3. On January 1, 2014, Yellow Car Company issued $50,000,000 face value, 4% convertible preferred shares, at par. Each $100 preferred share is convertible into 2 shares of Yellow Car common stock. None of the preferred shares were converted in 2014. Yellow Car's net income in 2014 was $8,680,000. The company had 2,650,000 shares of common stock issued and outstanding throughout 2014.
   Required: Compute basic and diluted earnings per share for 2014 while stating all required assumptions.

4. Lawson Company issues 50,000 shares of restricted stock to its CFO, on January 1, 2014. The stock has a fair value of $1,100,000 on this date. The service period related to this restricted stock is 4 years. Vesting occurs if CFO stays with the company for 4 years. The par value of the stock is $1. At December 31, 2014, the fair value of the stock is $1,750,000.
   Required: (a) Prepare the journal entries to record the restricted stock on January 1, 2014 (the date of grant) and the journal entry on December 31, 2015,
   (b) On August 1, 2017, the CFO leaves the company. Prepare the journal entry (if any) to account for this forfeiture,
   (c) Explain the restriction feature of restricted stock compensation plans.
5. On November 1, 2011, the shareholders of Chen Company approve a plan that grants the company's five executives options to purchase 2,000 shares each of the company's $1 par value common stock. The company grants the options on January 1, 2012. The executives may exercise the options at any time within the next 10 years. The option price per share is $60, and the market price of the shares at the date of grant is $70 per share. Under the fair value method, the company computes total compensation expense by applying an acceptable fair value option-pricing model. The fair value option-pricing model determines Chen's total compensation expense to be $220,000 and the expected period of benefit is two years, starting with the grant date. One of Chen's executives exercises 2,000 of the 10,000 options (20 percent of the options) on June 1, 2015 while the rest of them fail to exercise the remaining stock options before their expiration date.
   Required: (a) compare stock options with stock appreciation rights SARs in terms of the mechanisms,
   (b)Prepare journal entries to record issuance of the stock options, termination of the stock options, exercise of the stock options, and charges to compensation expense.

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Question Two: *(15 Marks)*

Tipper Company has two temporary differences between its income tax expense and income taxes payable. The following information is available.

	2014	*2015*	*2016*
Pretax financial income	$225,000	$268,000	$365,000
Excess of depreciation expense on tax return	(20,000)	(15,000)	(20,000)
Excess of warranty expense on financial income	10,000	15,000	16,000
Taxable income	$215,000	$268,000	$361,000

The income tax rate for all years is 30%.

Required:
(a) Prepare the journal entry to record income tax expense, deferred income taxes, and income tax payable for 2014, 2015, and 2016.
(b) Prepare the income tax expense section of the income statement for 2015, beginning with the line "Pre-tax financial income."
(c) What are the two main types of differences that cause pre-tax financial income and taxable income to differ and compare the impact of both types?

Question Three: *(20 Marks)*

Horizon Leasing Inc. signs an agreement on January 1, 2014, to lease equipment to one of its customers. The following information relates to this agreement.
1. The term of the non-cancellable lease is 8 years with no renewal option. The equipment has an estimated economic life of 10 years.
2. The cost of the asset to the lessor is $850,000. The fair value of the asset at January 1, 2014, is $850,000.
3. The asset will revert to the lessor at the end of the lease term at which time the asset is expected to have a residual value of $92,547, none of which is guaranteed.
4. The lessee assumes direct responsibility for all executory costs.
5. The agreement requires equal annual rental payments, beginning on January 1, 2014.
6. Collectibility of the lease payments is reasonably predictable. There are no important uncertainties surrounding the amount of costs yet to be incurred by the lessor.

Required:
(a) Assuming the lessor desires an 8% rate of return on its investment; calculate the amount of the annual rental payment required. Round to the nearest dollar.
(b) Prepare an amortization schedule that would be suitable for the lessor for the first two years of the lease term (only 2014 and 2015) and then prepare the required journal entries for the lessor for 2014 and 2015. Assume the lessor's annual accounting period ends on December 31.
(c) How do you expect the accounting treatment to differ for the lessor in case this was an operating lease?

Question Four: *(10 Marks)*

Black Hoe Construction changed from the completed-contract to the percentage-of-completion method of accounting for long-term construction contracts during 2015. For tax purposes, the company employs the completed-contract method and will continue this approach in the future. The appropriate information related to this change is as follows.

Pre-tax Income From	*Percentage-of-Completion*	*Completed-Contract*	*Difference*
2014	$125,000	$ 25,000	$100,000
2015	360,000	200,000	160,000

Required:
(a) Assuming that the tax rate is 40%, what is the amount of net income that would be reported in 2015?
(b) What entry(ies) are necessary to adjust the accounting records for the change in accounting principle?
(c) Differentiate between the two main types of accounting changes: changes in principles and changes in estimates.

Question Five: *(15 Marks)*

You have been engaged to review the financial statements of Water Sync Inc. In the course of your investigation you find a number of irregularities during the current year.
1. Insurance for a 6-month period purchased on October 1 of this year was charged to prepaid insurance in the amount of $5,000.
2. Year-end estimate of bonuses totalled $61,000 and was not recorded because the payment would not be made until next year.
3. Warranty expense averages 5% on current year sales of $5,000,000. Warranty expense is automatically debited for 5% of each sale. During the current year, the company also paid $225,000 in warranty related claims. The bookkeeper thought that the payments were an expense and debited warranty expense.
4. Office rent is paid quarterly in advance. The first quarter rent for next year ($25,000) was paid in December and rent expense was debited.

Required:
Prepare the necessary correcting entries, assuming that Water Sync Inc. uses a calendar-year basis.

End of Questions
Good Luck