

Name \_\_\_\_\_

Time of Exam: Circle one (only).

8:00 am

4:00 pm

**Instructions.**

This exam is 100 minutes long. Upon receiving the exam, you should write your name and circle the time at which you are taking the exam.. Then read the remainder of this page and stop.

**Do not proceed beyond this cover page till you are told to do so by the instructor or the TA.**

1. This exam has 11 (eleven) questions on 11 (eleven) pages. There are **seven** multiple choice questions (**35 points**), **two** problems (**45 points**) and **two** essay questions (**20 points**). **Check your copy of the exam to make sure you have a complete copy.**
2. **Not all questions have equal weight. Weights are shown at the beginning of each problem. Use your time judiciously and solve the easy problems first.**
3. **Show all your work wherever possible. It may help you earn partial or substantial credit. No partial credit will be given for questions 1,2,3, 6 and 7.**
4. Please note that there is substantial white space between problems to allow you plenty of room to write your answers and show your work on the printed side of each page of the exam. **Do not write answers for which you expect to earn a grade on the backs of pages (you may use those for additional scratch work if you like).**
5. **Make sure you read all pages of the exam and follow instructions exactly. If answers are illegible, incomprehensible or written down in the wrong place, we may fail to evaluate them correctly.**
6. The exam is closed book, no-notes. Only numeric calculators should be used. Text-storing calculators may be used only if you have purged all stored text. You may use electronic dictionaries if your native language is not English. Students are presumed to be familiar with the *Code of Policies and Regulations Applying to All Students*. In particular, please the following provision (ibid, §33):

“It is the responsibility of the student to refrain from infractions of academic integrity, from conduct that may lead to suspicion of such infractions, and from conduct that aids others in such infractions.”

**Detected violations of academic integrity will result in a score of zero for this exam as well as additional disciplinary action consistent with University policy.**
7. No questions will be answered during the exam. **If you cannot understand some part of the exam, if you find a typographical error or if you believe the exam is in any way erroneous or unworkable, please state your difficulty in writing on the exam itself.**
8. This exam is a test of your individual knowledge and ability to complete the assigned tasks at this moment in time. **You may not consult anybody regarding any portions of the exam before you turn it in to the instructor or the TA.**
9. If you need to leave the room during the exam for personal reasons, you may do so after seeking the permission of the instructor or TA. Before leaving your seat, please make sure that your exam is closed and turned over so that no writing is visible. You should turn off or put away your calculators/dictionaries as well.

**For the following seven questions, identify the letter of the choice that best completes the statement or answers the question.**

- \_\_\_\_\_ 1. (5 points) A U.S. company that has sold its product to a German firm would be exposed to a net exchange gain on the unpaid receivable if the
- a. amount to be paid was denominated in dollars.
  - b. dollar weakened relative to the German mark and the mark was the denominated currency.
  - c. dollar strengthened relative to the German mark and the mark was the denominated currency.
  - d. U.S. company purchased a forward contract to buy German marks.

- \_\_\_\_\_ 2. (5 points) Given the following information for a 90 day contract:
- |                   |            |       |
|-------------------|------------|-------|
|                   | US Dollars | FC    |
| Value Today       | 3,750      | 5,000 |
| Int Rate          | 4%         | 7%    |
| 3 months interest | 37.50      | 87.50 |
| Value in 3 months | ??         | ??    |
- The spot rate today is 1FC = .75

What will be the forward rate?

- a. 1FC = .75 US Dollars
  - b. 1FC = .57 US Dollars
  - c. 1FC = .745 US Dollars
  - d. 1FC = .70 US Dollars
- \_\_\_\_\_ 3. (5 points) Parson, Inc. sold merchandise for 600,000 FC to a Swiss vendor on November 30, 20X3. Payment in Swiss francs is due January 31, 20X4. On the same day, Jones signed an agreement with a foreign exchange broker to sell 600,000 FC on January 31, 20X4. Exchange rates to purchase 1 FC are as follows:

	<u>Nov. 30, 20X3</u>	<u>Dec. 31, 20X3</u>	<u>Jan. 31,</u>
<u>20X4</u>			
Spot.....	\$1.49	\$1.46	\$1.43
30 day.....	\$1.48	\$1.43	\$1.44
60 day.....	\$1.47	\$1.40	\$1.42

What will be the amount of the Forward Contract Receivable-Dollars on November 30, 20X3?

- a. \$894,000
- b. \$888,000
- c. \$882,000
- d. \$858,000

- \_\_\_\_\_ 4. (5 points) Company P purchased an 80% interest in Company S on January 1, 20X3, for \$700,000. On the purchase date, Company S stockholders' equity was \$800,000. Any excess of cost over book value was attributed to a patent with a 15-year life. In 20X3, Company P reported internally generated net income before taxes of \$80,000. Company S reported a net income before taxes of \$40,000. The firms file separate tax returns at a 30% tax rate. Assume an 80% dividend exclusion rate on intercompany dividends. The controlling share of consolidated net income is \_\_\_\_\_.
- a. \$81,200
  - b. \$79,280
  - c. \$78,480
  - d. \$74,256

Computation space (for partial credit):

- \_\_\_\_\_ 5. (5 points) Company P purchased a 30% interest in the Company S for \$345,000 on January 1, 20X1. At that time, Company S had stockholders' equity of \$1,000,000. Any excess cost over book value was attributed to a patent with a 15-year life. During 20X1, Company S earned \$60,000 and paid dividends of \$15,000. What is the balance in the investment account on December 31, 20X1, using the sophisticated equity method?
- a. \$363,000
  - b. \$360,000
  - c. \$355,500
  - d. \$349,500

Computation space (for partial credit):

6. (5 points) Rage is a German company wholly owned by a U.S. firm. Its inventory is valued at the lower of cost or market, with cost being measured by the average cost method. Purchases of inventory occur evenly throughout the period. In 1998 Rage's ending inventory was 50,000 DM at cost and 48,000 DM at market. Assume the following exchange rates:

Jan. 1, 1998    1 DM = \$1.40 U.S.  
Dec. 31, 1998   1 DM = \$1.53 U.S.  
1998 average    1 DM = \$1.45 U.S.

Determine the translated value of Rage's inventory to be included in the consolidated balance sheet for the U.S. parent given Rage's functional currency is the German mark.

- a. \$73,440
- b. \$76,500
- c. \$69,600
- d. \$72,500

7. (5 points) During the first quarter, a company's application of lower of cost or market methods indicated a \$150,000 loss from a temporary market decline, which is expected to be restored in the fiscal year. During the second quarter, the market reversed the decline. Which of the following situations indicates a proper treatment of these facts?

- a. A \$37,500 loss recognized in the first quarter and no recovery recognized in the second quarter.
- b. A \$150,000 loss recognized in the first quarter and a \$90,000 recovery in the second quarter.
- c. A \$150,000 loss recognized in the first quarter and a \$50,000 recovery in the second quarter.
- d. No loss recognized in the first quarter and no recovery recognized in the second quarter.

8. (20 points) Martel, Tusk, and Davis are partners with present capital balances of \$40,000, \$50,000, and \$20,000, respectively. The partners share profits and losses according to the following percentages: 60% for Martel, 30% for Tusk, and 10% for Davis. Frank is to join the partnership upon contributing \$40,000 to the partnership in exchange for a 25% interest in capital and a 20% interest in profits and losses. An appraisal of the existing partnerships' assets reveals the following:

Accounts Receivable	\$20,000 overvalued
Inventory	\$10,000 overvalued
Land	\$10,000 undervalued
Building	\$15,000 undervalued

Required:

Calculate the capital balances for each individual in the new partnership assuming use of the bonus and goodwill methods.

Question 8 continued ...

9. (25 points) On January 1, 20X1, Parent Company purchased 100% of the common stock of Subsidiary Company for \$360,000. On this date, Subsidiary had common stock, other paid-in capital, and retained earnings of \$50,000, \$100,000 and \$150,000 respectively. Net income and dividends for two years for Subsidiary Company were:

	<u>20X1</u>	<u>20X2</u>
Net income.....	\$60,000	\$90,000
Dividends.....	20,000	30,000

On January 1, 20X1, the only tangible assets of Subsidiary which were undervalued were inventory and building. Inventory, for which FIFO is used, was worth \$10,000 more than cost. The inventory was sold in 20X1. Land had a fair value of \$80,000. Buildings had a fair value of \$320,00, a remaining life of 10 years and straight-line depreciation is used. The book value of the land and building are \$50,000 and \$260,000 respectively. patent, if any, is to be amortized over 10 years.

Parent uses the simple equity method in accounting for its Investment in Subsidiary Company.

Required:

**Note: This question has 2 parts, a & b. You must answer both.**

a. (10 points) Using the information above, prepare a determination and distribution of excess schedule.

Question 9(a) continued ...

- b. (15 points) Compute the minority interest, investment in subsidiary and retained earnings as they would appear in the consolidated Balance Sheet for 20X2.

Question 9(b) continued ...

10. (10 points) Identify two distinct reasons for merger and acquisition activities and identify similarities and dissimilarities you would expect to find in the resulting financial reports. **Confine your answer to the rest of this page.**

11. (10 points) Identify reasons why allowing discretion in financial reporting policies may be good and bad for investors. What conclusions can you draw about the role of financial reporting in improving economic efficiency? **Confine your answer to the rest of this page.**