(1) Botticelli Inc. was organized in late 2008 to manufacture and sell hosiery. At the end of its fourth year of operation, the company has been fairly successful, as indicated by the following reported net incomes.

Y2008	$140,000[a]	Y2010	$205,000
Y2009	160,000	Y2011	276,000

[a] Include a $10,000 increase because of change in bad debt experience rate.

The company has decided to expand operations and has applied for a sizable bank loan. The bank officer has indicated that the records should be audited and presented in comparative statements to facilitate analysis by the bank. Botticelli Inc. therefore hired the auditing firm of Check & Doublecheck Co. and has provided the following additional information.

1. In early 2009, Botticelli Inc. changed its estimate from 2% to 1% on the amount of bad debt expense to be charged to operations. Bad debt expense for 2008, if a 1% rate had been used, would have been $10,000. The company therefore restated its net income for 2008.
2. In 2011, the auditor discovered that the company had changed its method of inventory pricing from average cost to FIFO. The effect on the income statements for the previous years is as follows.

	Y2008	Y2009	Y2010	Y2011
Net income unadjusted—average cost basis	$140,000	$160,000	$205,000	$276,000
Net income unadjusted—FIFO basis	155,000	165,000	215,000	260,000
	$ 15,000	$ 5,000	$ 10,000	($ 16,000)

3. In 2011, the auditor discovered that:
   a. The company incorrectly overstated the ending inventory by €14,000 in 2010.
   b. A dispute developed in 2009 with the tax authorities over the deductibility of entertainment expenses. In 2008, the company was not permitted these deductions, but a tax settlement was reached in 2011 that allowed these expenses. As a result of the court's finding, tax expenses in 2011 were reduced by €60,000.

Questions:

(a) Indicate how each of these changes or corrections should be handled in the accounting records. Ignore income tax considerations. (8%)

(b) Present comparative net income numbers for the years 2008 to 2011. Ignore income tax considerations. (8%)

(2) The National Chung-Cheng Bank has a $200,000, 12% note receivable from the Priday Company that is due on December 31, 2013. On December 31, 2010, the company misses the interest payment due on that date. The bank expects that the company will also miss the next payment, but will pay the principal on the maturity date. On December 31, 2011 the company misses the interest payment due on that date. On December 31, 2012, the company pays half the interest payment due on that date and is not expected to pay the other half.

In early January 2013, the bank and the company agree to a loan restructuring because of the financial condition of the company. The bank forgives the unpaid interest, extends the loan to December 31, 2015, and reduces the interest rate to 6%. The market rate for the loan is estimated to be 10% at this time.

Questions:

(a) Compute the value of the impaired loan on December 31, 2010. (5%)

(b) Prepare the journal entries from 2010 to 2015 for the bank to record the above events. (6%)

(3) The Harper Corporation acquired 80,000 of the 200,000 outstanding shares of the Moore Corporation on April 1, 2010, for $400,000 and obtained significant influence. The following information concerning the Moore Corporation is available on the date of acquisition.

	Book Value	Fair Value
Depreciation assets (remaining life, 15 years)	$ 600,000	$ 700,000
Other assets	500,000	450,000
Total	$ 1,100,000	$ 1,150,000
Liabilities	$ 300,000	$ 320,000
Common stocks	250,000	
Retained earnings	550,000	
Total	$1,100,000	

Questions:

(a) Prepare journal entries for Harper to record the preceding information. (6%)

(b) What is the balance in Harper's investment account on December 31, 2010? (Show all computations.) (3%)

(c) Prepare Harper's net cash flow from operating activities section of its 2010 statement of cash flows under the indirect method, assuming the equity investment income is the only income Harper reports. Ignore income taxes. (4%)

(4) The Dyson Company sells computer games to teenagers. Selected accounts included in the trial balance at December 31, 2009 and 2010 are as follows:

	2009	2010
Installment accounts receivable, 2009	$ 80,000	$ 20,000
Installment accounts receivable, 2010		112,500
Allowance for doubtful installment accounts receivable, 2009	(5,000)	(3,200)
Allowance for doubtful installment accounts receivable, 2010		(7,000)
Deferred gross profit, 2009	(16,000)	(3,500)
Deferred gross profit, 2010		(22,500)

During 2010 installment method sales and cost of goods sold were $200,000 and $160,000, respectively. In 2010 the company repossessed games that had been sold in 2009 for $6,000 and on which $2,500 had been collected. The games were believed to be worth $1,000. No repossessions occurs on 2010 sales.

Questions:

Prepare summary journal entries for 2010. (6%)

(5) Amirante Inc. manufactures an X-ray machine with an estimated life of 12 years and leases it to Chambers Medical Center for a period of 10 years. The normal selling price of the machine is $411,324, and its guaranteed residual value at the end of the non-cancelable lease term is estimated to be $15,000. The hospital will pay rents of $60,000 at the beginning of each year and all maintenance, insurance, and taxes. Amirante Inc. incurred costs of $250,000 in manufacturing the machine and $14,000 in negotiating and closing the lease. Amirante Inc. has determined that the implicit interest rate is 10%.

Questions:

(Round all numbers to the nearest dollar.)

(a) Discuss the nature of this lease in relation to the lessor and compute the amount of each of the following items. (7%)

1. Lease receivable at inception of the lease.
2. Sales prices.
3. Cost of sales.

(b) Prepare a 10-year lease amortization schedule. (5%)

(c) Prepare all of the lessor's journal entries for the first year. (8%)

(6) After a two-year search for a buyer, Hobson, Inc. sold its idle plant facility to Jackson Company for $700,000 on January 1, 2008. On this date the plant had a depreciated cost on Hobson's books of $500,000. Under the agreement Jackson paid $100,000 cash on January 1, 2008, and signed a $600,000 note bearing interest at 10%. The note was payable in installments of $100,000, $200,000, and $300,000 on January 1, 2009, 2010, and 2011, respectively. The note was secured by a mortgage on the property sold. Hobson appropriately accounted for the sale under the cost recovery method since there was no reasonable basis for estimating the degree of collectability of the note receivable. Jackson repaid the note with three late installment payments, which were accepted by Hobson, as follows:

Date of payment	Principal	Interest
July 1, 2009	$100,000	$90,000
December 31, 2010	200,000	75,000
February 1, 2012	300,000	32,500

Questions:

Prepare a schedule (using the following format) to record the initial transaction for the sale of the idle plant facility, the application of subsequent cash collections on the note, and the necessary journal entry on the date of the transaction is complete. (14%)

Date	Cash Received Debit	Note Receivable Dr. (Cr.)	Idle Plant (Net) Dr. (Cr.)	Deferred Income Dr. (Cr.)	Income Recognized (Credit)
Jan. 1, 2008	$100,000				
July 1, 2009	190,000				
Dec. 31, 2010	275,000				
Feb. 1, 2012	332,500				
Feb. 1, 2012					

(7) During the first quarter of 2010, the Payne Corporation entered into the following transactions:

Jan. 1 Acquired 150 shares of Block Corporation common stock for $20 per share, and 100 shares of Alpha Corporation common stock for $25 per share. These are the only shares the company owns and all are classified as securities available for sale.

Feb. 1 Purchased 12% A Company bonds with a face value of $20,000 at par, plus accrued interest. Interest on the bonds is payable February 28 and August 31 each year, and the bonds are due August 31, 2013. Also purchased 10% B Company bonds with a face value of $12,000 at par, plus accrued interest. Interest on the bonds is payable March 31 and September 30, and the bonds are due September 30, 2016. These are the only bonds the company owns and all are classified as securities available for sale.

Feb. 1　Established a petty cash fund for incidental expenditures at $500.

Feb. 28　Received the semiannual interest on the A Company bonds

Feb. 28　A count of cash on hand indicated that $125.50 remained in the petty cash fund. A sorting of petty cash vouchers disclosed that $110.00 was spent for postage, $170.65 was spent for office supplies, $45.00 was spent for transportation, and $43.50 was spent for miscellaneous items. The fund was replenished.

Mar. 31　Received first quarter dividends of $1,500 and the semiannual interest on the B Company bonds. On this date, the aggregate fair value of Payne's securities available for sale is $42,600.

Mar. 31　A count of cash on hand indicated that $230.50 remained in the petty cash fund. A sorting of petty cash vouchers disclosed that $140.00 was spent for postage, $75.30 was spent for office supplies, and $54.20 was spent for miscellaneous items. The fund was replenished.

The bank statement and the accounting records of the Payne Corporation for the month of March 2010 indicated that the cash collected from the dividends and the B Company bond interest was deposited on March 31 but did not appear on the March bank statement. There were no other deposits in transit. The bank statement showed a balance on March 31 of $13,459.75, which included collection of a $1,500 note and $100 of interest by the bank for the Payne Corporation. Also listed was a $20 bank service charge and a $75.60 NSF check returned by the bank. The cash balance per the accounting records on March 31 was $11,689.95, which included checks totaling $2,365.40 that had not yet cleared the bank.

Questions:

(a) Prepare journal entries to record the preceding transactions of the Payne Corporation for the first quarter of 2010. (8%)

(b) Prepare a bank reconciliation for Payne for March 31, 2010. (8%)

(c) Prepare any journal entries necessary to adjust Payne's books on March 31, 2010. (4%)