1. (10%)
On July 2, 2018, Lake Company sold to Black merchandise having a sales price of $9,000 (cost $5,400) with terms of 2/10. n/30. f.o.b. shipping point. Lake estimates that merchandise with a sales value of $900 will be returned. An invoice totaling $120, terms n/30, was received by Black on July 6 from Pacific Delivery Service for the freight cost. Upon receipt of the goods, on July 3, Black notified Lake that $350 of merchandise contained flaws. The same day, Lake issued a credit memo covering the defective merchandise and asked that it be returned at Lake's expense. Lake estimates the returned items to have a fair value of $140. The freight on the returned merchandise was $20 paid by Lake on July 7.
On July 12, the company received a check for the balance due from Black.

Instructions
Prepare journal entries for Lake Company to record all the events noted above assuming sales and receivables are entered at net selling price.

2. (7%)
Warriors implemented a customer loyalty program that rewards a customer with 1 loyalty point for every $100 of purchases on a select group of Warriors products. Each point is redeemable for a $10 discount on any purchases of Warriors merchandise in the following 2 years. During 2018, customers purchased select group products for $1,000,000 (all products are sold to provide a 45% gross profit) and earned 10,000 points redeemable for future purchases. The standalone selling price of the purchased products is $1,000,000. Based on prior experience with incentives programs like this, Warriors expects 8,000 points to be redeemed related to these sales. Warriors appropriately uses this experience to estimate the value of future consideration related to bonus points. The points provide a material right to customers that they would not receive without entering into a contract.

Instructions
a. Prepare the journal entries for the bonus point sales for Warriors in 2018.
b. How much additional sales revenue is recognized by Warriors in 2019, assuming 5,000 bonus points are redeemed?

3. (9%)
To stimulate the sales of its Maverick breakfast cereal, Bull Company places 1 coupon in each box. Five coupons together with $2 are redeemable for a premium consisting of a children's hand puppet. In 2018, the company purchases 40,000 puppets at $3.5 each and sells 480,000 boxes of Maverick at $10 a box. From its experience with other similar premium offers, the company estimates that 40% of the coupons issued will be mailed back for redemption. During 2018, 120,000 coupons together with cash are presented for redemption. In addition it costs $0.5 to distribute each puppet.

Instructions
Prepare the journal entries that should be recorded in 2018 relative to the premium plan.

4. (12%)

Presented below is information related to the Accounts Receivable accounts of Cavalier Inc. during the current year 2018.

(1) An aging schedule of the accounts receivable as of December 31, 2018, is as follows:

Age	Net Debit Balance	% to Be Applied after Correction Is Made
Under 60 days	$172,000	1%
60-90 days	136,400	3%
91-120 days	39,900*	6%
Over 120 days	23,600	$3,700 definitely uncollectible;
	$371,900	estimated remainder uncollectible is 25%

*The $3,200 write-off of receivables is related to the 91-to-120 day category.

(2) The Accounts Receivable account has a debit balance of $371,900 on December 31, 2018.

(3) Two entries were made in the Bad Debt Expense account during the year: (1) a debit on December 31 for the amount credited to Allowance for Doubtful Accounts, and (2) a credit for $3,200 on November 3, 2018, and a debit to Allowance for Doubtful Accounts because of a bankruptcy.

(4) Allowance for Doubtful Accounts is as follows for 2018.

Allowance for Doubtful Accounts

Nov. 3	Uncollectible accounts written off	3,200	Jan. 1	Beginning balance	8,750
			Dec. 31	4% of $371,900	14,876

(5) A credit balance exists in Accounts Receivable (60-90 days) of $4,800, which represents an advance on a sales contract.

Instructions

Assuming that the books have not been closed for 2018, make the necessary correcting entries.

5. (11%)

Wizards Company issues a 4-year, 7.5% fixed-rate interest only, non-prepayable $1,000,000 note payable on December 31, 2018. It decides to change the interest rate from a fixed rate to variable rate and enters into a swap agreement with Hornet Corp. The swap agreement specifies that Wizards will receive a fixed rate at 7.5% and pay variable with settlement dates that match the interest payments on the debt. Assume that interest rates have declined during 2019 and that Wizards received $13,000 as an adjustment to interest expense for the settlement at December 31, 2019. The loss related to the debt (due to interest rate changes) was $42,000. The value of the swap contract increased $48,000.

Instructions

a. Prepare the journal entry to record the payment of interest expense on December 31, 2019.
b. Prepare the journal entry to record the receipt of the swap settlement on December 31, 2019.
c. Prepare the journal entry to record the change in the fair value of the swap contract on December 31, 2019.
d. Prepare the journal entry to record the change in the fair value of the debt on December 31, 2019.

6. (14%)

Clippers Inc. has a debt investment in the bonds issued by Thunder Corporation. The bonds were purchased at par for $400,000 and, at the end of 2018, have a remaining life of 3 years with annual interest payments at 10%, paid at the end of each year. This debt investment is classified as held-for-collection. Thunder is facing a tough economic environment and informs its investors that it will be unable to make all payments according to the contractual terms. The controller of Clippers has prepared the following revised expected cash flow forecast for this bond investment. The market rate is 8% at December 31, 2018.

Dec. 31	Expected Cash Flows
2019	$ 35,000
2020	35,000
2021	385,000
Total cash flows	$455,000

Instructions

a. Prepare the entry to record the impairment loss for Clippers at December 31, 2018.

b. On January 25, 2019, Thunder receives a major capital infusion from a private equity investor. It informs Clippers that the bonds now will be paid according to the contractual terms. Prepare the entry (if any) to record this information.

c. Assume that the bond investment in Thunder Corporation was held-for-collection and selling and the expected credit loss was $25,000. At December 31, 2019, the bond investment are valued at $320,000. Prepare the entry to record this impairment on December 31, 2019.

7. (13%)

On January 1, 2018, Trailblazer Company issued a convertible bond with a par value of $1,000,000 in the market for $1,200,000. The bonds are convertible into 12,000 ordinary shares of $10 per share par value. The bond has a 5-year life and has a stated interest rate of 10% payable annually. The market interest rate for a similar non-convertible bond at January 1, 2018, is 8%.

Instructions

a. Prepare the journal entry to record the issuance of the convertible bond on January 1, 2018.

b. Assume that the bonds were converted on December 31, 2020. The fair value of the liability component of the bond is determined to be $1,080,000 on December 31, 2020. Prepare the journal entry to record the conversion on December 31, 2020. Assume that the accrual of interest related to 2020 has been recorded.

c. Assume that the convertible bonds were repurchased on December 31, 2020, for $1,110,000 instead of being converted. As indicated, the liability component of the bond is determined to be $1,080,000 on December 31, 2020. Assume that the accrual of interest related to 2020 has been recorded. Prepare the journal entry(ies) to record this transaction.

8. (24%)

Grizzlies Company manufactures an X-ray machine with an estimated life of 12 years and leases it to Pelicans Medical Center for a period of 10 years. The normal selling price of the machine is $495,678, 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. Grizzlies incurred costs of $300,000 in manufacturing the machine and $14,000 in legal fees directly related to the signing of the lease. Grizzlies has determined that the collectability of the lease payments is probable and that the implicit interest rate is 5%

Instructions

a. Discuss the nature of this lease in relation to the lessor and prepare all of the lessor's journal entries for the first year.

b. Assume the same data as above and that Pelicans Medical Center has an incremental borrowing rate of 6% and an expected residual value at the end of the lease of $10,000. The implicit interest rate used by Grizzlies is known to Pelicans. Pelicans Medical Center amortizes its leased machine on a straight-line basis. Prepare all of the lessee's journal entries for the first year.

c. Suppose Pelicans Medical Center incurred $6,000 of document preparation costs after the execution of the lease. Compute the amounts of the initial measurement of the lease liability and right-of-use asset.

Periods	Present Value of 1			
	5%	6%	8%	10%
3	0.86384	0.83962	0.79383	0.75131
5	0.78353	0.74726	0.68058	0.62092
10	0.61391	0.55839	0.46319	0.38554
12	0.55684	0.49697	0.39711	0.31863

Periods	Present Value of an Ordinary Annuity of 1			
	5%	6%	8%	10%
3	2.72325	2.67301	2.57710	2.48685
5	4.32948	4.21236	3.99271	3.79079
10	7.72173	7.36009	6.71008	6.14457
12	8.86325	8.38384	7.53608	6.81369