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Chapter 01

Intercorporate Acquisitions and Investments in Other Entities

Multiple Choice Questions

1. Assuming no impairment in value prior to transfer, assets transferred by a parent company to another entity it has created should be recorded by the newly created entity at the assets':

A. cost to the parent company.

B. book value on the parent company's books at the date of transfer.

C. fair value at the date of transfer.

D. fair value of consideration exchanged by the newly created entity.

2. Given the increased development of complex business structures, which of the following regulators is responsible for the continued usefulness of accounting reports?

 1-1

A. Securities and Exchange Commission (SEC)

B. Public Company Accounting Oversight Board (PCAOB)

C. Financial Accounting Standards Board (FASB)

D. All of these

1-2

3. A business combination in which the acquired company's assets and liabilities are combined with those of the acquiring company into a single entity is defined as:

A. Stock acquisition

B. Leveraged buyout

C. Statutory Merger

D. Reverse statutory rollup

4. In which of the following situations do accounting standards not require that the financial statements of the parent and subsidiary be consolidated:

A. A corporation creates a new 100 percent owned subsidiary

B. A corporation purchases 90 percent of the voting stock of another company

C. A corporation has both control and majority ownership of an unincorporated company

D. A corporation owns less-than a controlling interest in an unincorporated company

5. During its inception, Devon Company purchased land for $100,000 and a building for $180,000. After exactly 3 years, it transferred these assets and cash of $50,000 to a newly created subsidiary, Regan Company, in exchange for 15,000 shares of Regan's $10 par value stock. Devon uses straight-line depreciation. Useful life for the building is 30 years, with zero residual value. An appraisal revealed that the building has a fair value of $200,000.

Based on the information provided, at the time of the transfer, Regan Company should record:

A. Building at $180,000 and no accumulated depreciation.

B. Building at $162,000 and no accumulated depreciation.

C. Building at $200,000 and accumulated depreciation of $24,000.

D. Building at $180,000 and accumulated depreciation of $18,000.

1-3

6. During its inception, Devon Company purchased land for $100,000 and a building for $180,000. After exactly 3 years, it transferred these assets and cash of $50,000 to a newly created subsidiary, Regan Company, in exchange for 15,000 shares of Regan's $10 par value stock. Devon uses straight-line depreciation. Useful life for the building is 30 years, with zero residual value. An appraisal revealed that the building has a fair value of $200,000.

   Based on the information provided, what amount would be reported by Devon Company as investment in Regan Company common stock?

   A. $312,000

   B. $180,000

   C. $330,000

   D. $150,000

7. During its inception, Devon Company purchased land for $100,000 and a building for $180,000. After exactly 3 years, it transferred these assets and cash of $50,000 to a newly created subsidiary, Regan Company, in exchange for 15,000 shares of Regan's $10 par value stock. Devon uses straight-line depreciation. Useful life for the building is 30 years, with zero residual value. An appraisal revealed that the building has a fair value of $200,000.

   Based on the preceding information, Regan Company will report

   A. additional paid-in capital of $0.

   B. additional paid-in capital of $150,000.

   C. additional paid-in capital of $162,000.

   D. additional paid-in capital of $180,000.

 1-4

8. Which of the following situations best describes a business combination to be accounted for as a statutory merger?

A. Both companies in a combination continue to operate as separate, but related, legal entities.

B. Only one of the combining companies survives and the other loses its separate identity.

C. Two companies combine to form a new third company, and the original two companies are dissolved.

D. One company transfers assets to another company it has created.

9. A statutory consolidation is a type of business combination in which:

A. one of the combining companies survives and the other loses its separate identity.

B. one company acquires the voting shares of the other company and the two companies continue to operate as separate legal entities.

C. two publicly traded companies agree to share a board of directors.

D. each of the combining companies is dissolved and the net assets of both companies are transferred to a newly created corporation.

 1-5

10. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, what number of shares of $7 par value stock did Spin issue to Conservative?

A. 10,000

B. 7,000

C. 8,000

D. 25,000

11. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, what was Conservative's book value of assets transferred to Spin Company?

A. $243,000

B. $263,000

C. $221,000

D. $201,000

1-11

12. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, what amount did Conservative report as its investment in Spin after the transfer of assets and liabilities?

A. $181,000

B. $221,000

C. $263,000

D. $243,000

13. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, immediately after the transfer,

A. Conservative's total assets decreased by $23,000.

B. Conservative's total assets decreased by $20,000.

C. Conservative's total assets increased by $56,000.

D. Conservative's total assets remained the same.

16. Burrough Corporation paid $80,000 to acquire all of Helyar Company's net assets. Helyar reported assets with a book value of $100,000 and fair value of $98,000 and liabilities with a book value and fair value of $23,000 on the date of combination. Burrough also paid $3,000 to

14. Rivendell Corporation and Foster Company merged as of January 1, 20X9. To effect the merger, Rivendell paid finder's fees of $40,000, legal fees of $13,000, audit fees related to the stock issuance of $10,000, stock registration fees of $5,000, and stock listing application fees of $4,000.

Based on the preceding information, under the acquisition method, what amount relating to the business combination would be expensed?

A. $72,000

B. $19,000

C. $53,000

D. $63,000

15. Rivendell Corporation and Foster Company merged as of January 1, 20X9. To effect the merger, Rivendell paid finder's fees of $40,000, legal fees of $13,000, audit fees related to the stock issuance of $10,000, stock registration fees of $5,000, and stock listing application fees of $4,000.

Based on the preceding information, under the acquisition method:

A. $72,000 of stock issue costs are treated as goodwill.

B. $19,000 of stock issue costs are treated as a reduction in the issue price.

C. $19,000 of stock issue costs are expensed.

D. $72,000 of stock issue costs are expensed.

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16. Burrough Corporation paid $80,000 to acquire all of Helyar Company's net assets. Helyar reported assets with a book value of $100,000 and fair value of $98,000 and liabilities with a book value and fair value of $23,000 on the date of combination. Burrough also paid $3,000 to a search firm for finder's fees related to the acquisition. What amount will be recorded as goodwill by Burrough Corporation while recording its investment in Helyar?

A. $0

B. $5,000

C. $8,000

D. $13,000

17. Plummet Corporation reported the book value of its net assets at $400,000 when Zenith Corporation acquired 100 percent ownership. The fair value of Plummet's net assets was determined to be $510,000 on that date.

Based on the preceding information, what amount of goodwill will be reported in consolidated financial statements presented immediately following the combination if Zenith paid $550,000 for the acquisition?

A. $0

B. $50,000

C. $150,000

D. $40,000

18. Plummet Corporation reported the book value of its net assets at $400,000 when Zenith Corporation acquired 100 percent ownership. The fair value of Plummet's net assets was determined to be $510,000 on that date.

Based on the preceding information, what amount will be recorded by Zenith as its investment in Plummet, if it paid $500,000 for the acquisition?

A. $610,000

B. $400,000

C. $500,000

D. $510,000

19. Plummet Corporation reported the book value of its net assets at $400,000 when Zenith Corporation acquired 100 percent ownership. The fair value of Plummet's net assets was determined to be $510,000 on that date.

Based on the preceding information, what amount of goodwill will be reported in consolidated financial statements presented immediately following the combination if Zenith paid $500,000 for the acquisition?

A. $0

B. $50,000

C. $150,000

D. $40,000

20. The fair value of net identifiable assets of a reporting unit of X Company is $300,000. On X Company's books, the carrying value of this reporting unit's net assets is $350,000, including $60,000 goodwill. If the fair value of the reporting unit as a whole is $335,000, what amount of goodwill impairment will be recognized for this unit?

A. $0

B. $10,000

C. $25,000

D. $35,000

21. The fair value of net identifiable assets of a reporting unit of Y Company is $270,000. The carrying value of the reporting unit's net assets on Y Company's books is $320,000, including $50,000 goodwill. If the reported goodwill impairment for the unit is $10,000, what would be the fair value of the reporting unit?

A. $320,000

B. $310,000

C. $270,000

D. $290,000

22. Following its acquisition of the net assets of Dan Company, Emp Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

	Carrying Amount	Fair Value
Cash	$20,000	$20,000
Inventory	35,000	40,000
Equipment	125,000	160,000
Goodwill	60,000	
Accounts Payable	30,000	30,000

Based on the preceding information, what amount of goodwill (after any impairment) will be reported for this division if its fair value is determined to be $200,000?

A. $0

B. $60,000

C. $30,000

D. $10,000

23. Following its acquisition of the net assets of Dan Company, Empire Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

of $60,000 to one of the reporting divisions. Information for this division follows:

Carrying Amount Fair Value

	Carrying Amount	Fair Value
Cash	$20,000	$20,000
Inventory	35,000	40,000
Equipment	125,000	160,000
Goodwill	60,000	
Accounts Payable	30,000	30,000

Based on the preceding information, what amount of goodwill impairment will be recognized for this division if its fair value is determined to be $195,000?

A. $5,000

B. $30,000

C. $60,000

D. $55,000

24. Following its acquisition of the net assets of Dan Company, Emperor Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

	Carrying Amount	Fair Value
Cash	$20,000	$20,000
Inventory	35,000	40,000
Equipment	125,000	160,000
Goodwill	60,000	
Accounts Payable	30,000	30,000

Based on the preceding information, what amount of amount of goodwill impairment will be recognized for this division if its fair value is determined to be $245,000?

A. $0

B. $5,000

C. $60,000

D. $55,000

25. Public Equity Corporation acquired Lenore Company through an exchange of common shares. All of Lenore's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available.

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what number of shares was issued at the time of the exchange?

A. 5,000

B. 17,500

C. 12,500

D. 10,000

 1-25

26. Public Equity Corporation acquired Lenore Company through an exchange of common shares. All of Lenore's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available.

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what is the par value of Public's common stock?

A. $10

B. $1

C. $5

D. $4

27. Public Equity Corporation acquired Lenore Company through an exchange of common shares. All of Lenore's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available.

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what is the fair value of Lenore's net assets, if goodwill of $56,000 is recorded?

A. $306,000

B. $244,000

C. $194,000

D. $300,000

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28. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta	ı
Carrying value	$200,000	$320,000	$370,000	$300,000	00
Goodwill included in carrying value	20,000	34,000	50,000	30,000	00
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000	00
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000	00

Based on the preceding information, what amount of goodwill will be reported for Alpha at year-end?

A. $0

B. $20,000

C. $30,000

D. $10,000

20. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta	ı
Carrying value	$200,000	$320,000	$370,000	$300,000	00
Goodwill included in carrying value	20,000	34,000	50,000	30,000	00
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000	00
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000	00

Based on the preceding information, what amount of goodwill will be reported for Beta at year-end?

A. $0

B. $14,000

C. $34,000

D. $50,000

21. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta	ı
Carrying value	$200,000	$320,000	$370,000	$300,000	00
Goodwill included in carrying value	20,000	34,000	50,000	30,000	00
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000	00
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000	00

Based on the preceding information, for Gamma:

A. no goodwill should be reported at year-end.

B. goodwill impairment of $30,000 should be recognized at year-end.

C. goodwill impairment of $20,000 should be recognized at year-end.

D. goodwill of $30,000 should be reported at year-end.

22. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta	ı
Carrying value	$200,000	$320,000	$370,000	$300,000	00
Goodwill included in carrying value	20,000	34,000	50,000	30,000	00
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000	00
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000	00

Based on the preceding information, for Delta:

A. no goodwill should be reported at year-end.

B. goodwill impairment of $15,000 should be recognized at year-end.

C. goodwill impairment of $20,000 should be recognized at year-end.

D. goodwill of $30,000 should be reported at year-end.

23. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta	ı
Carrying value	$200,000	$320,000	$370,000	$300,000	00
Goodwill included in carrying value	20,000	34,000	50,000	30,000	00
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000	00
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000	00

Based on the preceding information, what would be the total amount of goodwill that Wilson should report at year-end?

A. $0

B. $69,000

C. $79,000

D. $94,000

33. Which of the following observations is (are) consistent with the acquisition method of accounting for business combinations?

I. Expenses related to the business combination are expensed.

II. Stock issue costs are treated as a reduction in the issue price.

III. All merger and stock issue costs are expensed.

IV. No goodwill is ever recorded.

A. III

B. IV

C. I and II

D. I, II, and IV

34. Which of the following observations refers to the term differential?

A. Excess of consideration exchanged over fair value of net identifiable assets.

B. Excess of fair value over book value of net identifiable assets.

C. Excess of consideration exchanged over book value of net identifiable assets.

D. Excess of fair value over historical cost of net identifiable assets.

35. Which of the following observations concerning "goodwill" is NOT correct?

A. Once written down, it may be written up for recoveries.

B. It must be tested for impairment at least annually.

C. Goodwill impairment losses are recognized in income from continuing operations or income before extraordinary gains and losses.

D. It must be reported as a separate line item in the balance sheet.

36. Big Company acquired the following assets and liabilities of Little Company (fair values listed below) for $470,000 cash.

Inventory	$70,000
Land	100,000
Buildings and Equipment	320,000
Current Liabilities	50,000

Assuming these items are all recorded at their acquisition date fair values, what additional item needs to be recorded and how will it be accounted for in the future?

A. $30,000 Goodwill, capitalized and tested for impairment

B. $30,000 Bargain purchase, recognized in current earnings

C. $30,000 Bargain purchase, capitalized and recognized over time

34. Which of the following observations refers to the term differential?

37. Paul Corp. acquired 100 percent of Sato Inc.'s voting stock on July 1, 20X1. The following

D. $30,000 Goodwill, capitalized and amortized over time

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34. Which of the following observations refers to the term differential?

37. Paul Corp. acquired 100 percent of Sam Inc.'s voting stock on July 1, 20X1. The following information was available as of December 31, 20X1:

	Net Income Jan 1 – June 30, 20X1	Net Income July 1, 20X1 – Dec 31, 20X1
Paul Corp.	$300,000	$420,000
Sam Inc.	$150,000	$220,000

How much net income should be reported in Paul Corp's income statement for 20X1?

A. $370,000

B. $720,000

C. $940,000

D. $1,090,000

38. Note: This is a Kaplan CPA Review Question

On August 31, 20X1, Wood Corp. issued 100,000 shares of its $20 par value common stock for the net assets of Pine, Inc. in a business combination accounted for by the acquisition method. The market value of Wood's common stock on August 31 was $36 per share. Wood paid a fee of $160,000 to the consultant who arranged this acquisition. Costs of registering and issuing the equity securities amounted to $80,000. No goodwill was involved in the purchase. What amount should Wood capitalize as the cost of acquiring Pine's net assets?

A. $3,680,000

B. $3,600,000

C. $3,760,000

D. $3,840,000

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39. Note: This is a Kaplan CPA Review Question

Company X acquired for cash all of the outstanding common stock of Company Y. How should Company X determine in general the amounts to be reported for the inventories and long-term debt acquired from Company Y?

Inventories	Long-term debt
A. Fair value	Fair value
B. Fair value	Recorded value
C. Recorded value	Fair value
D. Recorded value	Recorded value

A. Option A

B. Option B

C. Option C

D. Option D

40. Point Co. purchased 90% of Sharpe Corp.'s voting stock on January 1, 20X2 for $5,580,000. Prior to the acquisition, Point held a 10% equity position in Sharpe Company. On January 1, 20X2 Pointe's 10% investment in Sharpe has a book value of $340,000 and a fair value of $620,000. On January 1, 20X2 Point records the following:

A. Debit Gain on revaluation of Sharpe's stock $280,000

B. Credit Gain on revaluation of Sharpe's stock $280,000

C. Credit Investment in Sharpe stock $5,860,000

D. Debit Investment in Sharpe stock $6,200,000

41. The length of the measurement period allowed to value the assets and liabilities in an acquired business combination starts on the date of acquisition and lasts until:

A. All necessary information about the facts of the acquisition is obtained

B. All necessary information about the facts of the acquisition is obtained, not to exceed one month

C. All necessary information about the facts of the acquisition is obtained, not to exceed one reporting period

D. All necessary information about the facts of the acquisition is obtained, not to exceed one year

42. ASC 805 requires contingent consideration in a business combination to be classified as:

A. An asset

B. A liability or equity

C. An asset or equity

D. An asset or a liability

43. For all acquired contingencies, the acquirer should do all of the following except:

A. Provide documentation from the acquirer's attorney regarding pending lawsuits and loan guarantees

B. Provide a description of each contingency

C. Disclose the amount recognized at the acquisition date

D. Describe the estimated range of possible undiscounted outcomes of the contingency

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44. ASC 805 requires that ongoing research and development projects be treated in all of the following ways except:

A. Recorded at acquisition-date fair values

B. Classified as intangible assets having indefinite lives

C. Expensed immediately

D. Tested for impairment periodically

Essay Questions

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45. On January 1, 20X8, Alaska Corporation acquired Mercantile Corporation's net assets by paying $160,000 cash. Balance sheet data for the two companies and fair value information for Mercantile Corporation immediately before the business combination are given below:

	Alaska	Mercantile	
	Book Value	Book Value	Fair Value
Cash	$200,000	$30,000	$30,000
Accounts Receivable	40,000	22,000	22,000
Inventory	120,000	25,000	36,000
Patents	50,000	20,000	40,000
Buildings and Equipment	330,000	250,000	150,000
Less: Accumulated Depreciation	-140,000	-150,000	
Total Assets	$600,000	$197,000	$278,000
Accounts Payable	$85,000	$55,000	$55,000
Notes Payable	100,000	80,000	80,000
Common Stock:			
$5 par value	120,000		
$2 par value		20,000	
Additional Paid-In Capital	140,000	25,000	
Retained Earnings	155,000	17,000	
Total Liabilities and Equities	$600,000	$197,000	

Required:

Prepare the journal entry to record the acquisition of Mercantile Corporation.

46. On January 1, 20X8, Line Corporation acquired all of the common stock of Staff Company for $300,000. On that date, Staff's identifiable net assets had a fair value of $250,000. The assets acquired in the purchase of Staff are considered to be a separate reporting unit of Line Corporation. The carrying value of Staff's investment at December 31, 20X8, is $310,000. The fair value of the net assets (excluding goodwill) at that date is $220,000 and the fair value of the reporting unit is determined to be 260,000.

Required:

1) Explain how goodwill is tested for impairment for a reporting unit.

2) Determine the amount, if any, of impairment loss to be recognized at December 31, 20X8.

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47. SeaLine Corporation is involved in the distribution of processed marine products. The fair values of assets and liabilities held by three reporting units and other information related to the reporting units owned by SeaLine are as follows:

	Unit X	Unit Y	Unit Z
Cash	$15,000	$45,000	$35,000
Accounts Receivables	15,000	18,000	10,000
Inventory	35,000	60,000	35,000
Land	30,000	45,000	20,000
Buildings	120,000	80,000	50,000
Equipment	140,000	45,000	50,000
Accounts Payable	25,000	45,000	25,000
Fair Value of Reporting Unit	360,000	230,000	220,000
Carrying Value of Investment	375,000	240,000	240,000
Goodwill Included in Carrying Value	50,000	25,000	40,000

Required: Determine the amount of goodwill that SeaLine should report in its current financial statements.

Chapter 01 Intercorporate Acquisitions and Investments in Other Entities

Answer Key

Multiple Choice Questions

1. Assuming no impairment in value prior to transfer, assets transferred by a parent company to another entity it has created should be recorded by the newly created entity at the assets':

A. cost to the parent company.

<u>B.</u> book value on the parent company's books at the date of transfer.

C. fair value at the date of transfer.

D. fair value of consideration exchanged by the newly created entity.

AACSB: Reflective Thinking

AICPA FN: Decision Making

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.

Learning Objective: 01-04 Understand and explain the differences between different forms of business combinations.

Topic: Internal Expansion: Creating a Business Entity

Topic: Valuation of Business Entities

 1-32

2. Given the increased development of complex business structures, which of the following regulators is responsible for the continued usefulness of accounting reports?

A. Securities and Exchange Commission (SEC)
B. Public Company Accounting Oversight Board (PCAOB)
C. Financial Accounting Standards Board (FASB)
<u>D.</u> All of these

AACSB: Reflective Thinking
AICPA FN: Reporting
Blooms: Remember
Difficulty: 1 Easy
Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.
Topic: An Introduction to Complex Business Structures

3. A business combination in which the acquired company's assets and liabilities are combined with those of the acquiring company into a single entity is defined as:

A. Stock acquisition
B. Leveraged buyout
<u>C.</u> Statutory Merger
D. Reverse statutory rollup

AACSB: Reflective Thinking
AICPA FN: Decision Making
Blooms: Remember
Difficulty: 1 Easy
Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.
Topic: Organizational Structure and Financial Reporting

 1-33

4. In which of the following situations do accounting standards not require that the financial statements of the parent and subsidiary be consolidated:

A. A corporation creates a new 100 percent owned subsidiary

B. A corporation purchases 90 percent of the voting stock of another company

C. A corporation has both control and majority ownership of an unincorporated company

D. A corporation owns less-than a controlling interest in an unincorporated company

AACSB: Reflective Thinking
AICPA FN: Decision Making
Blooms: Remember
Difficulty: 1 Easy
Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.
Topic: Organizational Structure and Financial Reporting

5. During its inception, Devon Company purchased land for $100,000 and a building for $180,000. After exactly 3 years, it transferred these assets and cash of $50,000 to a newly created subsidiary, Regan Company, in exchange for 15,000 shares of Regan's $10 par value stock. Devon uses straight-line depreciation. Useful life for the building is 30 years, with zero residual value. An appraisal revealed that the building has a fair value of $200,000.

Based on the information provided, at the time of the transfer, Regan Company should record:

A. Building at $180,000 and no accumulated depreciation.

B. Building at $162,000 and no accumulated depreciation.

C. Building at $200,000 and accumulated depreciation of $24,000.

D. Building at $180,000 and accumulated depreciation of $18,000.

AACSB: Analytic
AICPA FN: Measurement

1-34

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-03 Make calculations and prepare journal entries for the creation and purchase of a business entity.

Learning Objective: 01-04 Understand and explain the differences between different forms of business combinations.

Topic: Accounting for Internal Expansion: Creating Business Entities

Topic: Valuation of Business Entities

6. During its inception, Devon Company purchased land for $100,000 and a building for $180,000. After exactly 3 years, it transferred these assets and cash of $50,000 to a newly created subsidiary, Regan Company, in exchange for 15,000 shares of Regan's $10 par value stock. Devon uses straight-line depreciation. Useful life for the building is 30 years, with zero residual value. An appraisal revealed that the building has a fair value of $200,000.

   Based on the information provided, what amount would be reported by Devon Company as investment in Regan Company common stock?

   A. $312,000
   B. $180,000
   C. $330,000
   D. $150,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-02 Understand the history of the development of standards related to acquisition accounting over time.

Learning Objective: 01-03 Make calculations and prepare journal entries for the creation and purchase of a business entity.

Topic: Accounting for Internal Expansion: Creating Business Entities

Topic: The Development of Accounting for Business Combinations

 1-35

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7. During its inception, Devon Company purchased land for $100,000 and a building for $180,000. After exactly 3 years, it transferred these assets and cash of $50,000 to a newly created subsidiary, Regan Company, in exchange for 15,000 shares of Regan's $10 par value stock. Devon uses straight-line depreciation. Useful life for the building is 30 years, with zero residual value. An appraisal revealed that the building has a fair value of $200,000.

Based on the preceding information, Regan Company will report

A. additional paid-in capital of $0.

B. additional paid-in capital of $150,000.

<u>C.</u> additional paid-in capital of $162,000.

D. additional paid-in capital of $180,000.

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-03 Make calculations and prepare journal entries for the creation and purchase of a business entity.

Topic: Accounting for Internal Expansion: Creating Business Entities

8. Which of the following situations best describes a business combination to be accounted for as a statutory merger?

A. Both companies in a combination continue to operate as separate, but related, legal entities.

<u>B.</u> Only one of the combining companies survives and the other loses its separate identity.

C. Two companies combine to form a new third company, and the original two companies are dissolved.

D. One company transfers assets to another company it has created.

AACSB: Reflective Thinking

AICPA FN: Decision Making

 1-36

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Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-04 Understand and explain the differences between different forms of business combinations.

Topic: Forms of Business Combinations

9. A statutory consolidation is a type of business combination in which:

A. one of the combining companies survives and the other loses its separate identity.

B. one company acquires the voting shares of the other company and the two companies continue to operate as separate legal entities.

C. two publicly traded companies agree to share a board of directors.

<u>D.</u> each of the combining companies is dissolved and the net assets of both companies are transferred to a newly created corporation.

AACSB: Reflective Thinking

AICPA FN: Decision Making

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-04 Understand and explain the differences between different forms of business combinations.

Topic: Forms of Business Combinations

 1-37

38. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, what number of shares of $7 par value stock did Spin issue to Conservative?

A. 10,000

B. 7,000

C. 8,000

D. 25,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Combination Effected through Acquisition of Stock

39. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, what was Conservative's book value of assets transferred to Spin Company?

A. $243,000

B. $263,000

C. $221,000

D. $201,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.

Learning Objective: 01-03 Make calculations and prepare journal entries for the creation and purchase of a business entity.

Topic: Accounting for Internal Expansion: Creating Business Entities

Topic: Internal Expansion: Creating a Business Entity

1-39

40. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, what amount did Conservative report as its investment in Spin after the transfer of assets and liabilities?

A. $181,000

B. $221,000

C. $263,000

D. $243,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-02 Understand the history of the development of standards related to acquisition accounting over time.

Learning Objective: 01-03 Make calculations and prepare journal entries for the creation and purchase of a business entity.

Topic: Accounting for Internal Expansion: Creating Business Entities

Topic: The Development of Accounting for Business Combinations

41. In order to reduce the risk associated with a new line of business, Conservative Corporation established Spin Company as a wholly owned subsidiary. It transferred assets and accounts payable to Spin in exchange for its common stock. Spin recorded the following entry when the transaction occurred:

Cash and receivables	23,000	
Inventory	15,000	
Land	30,000	
Buildings	100,000	
Equipment	95,000	
Accounts Payable		20,000
Accumulated Depreciation—Buildings		32,000
Accumulated Depreciation—Equipment		30,000
Common Stock		56,000
Additional Paid-In Capital		125,000

Based on the preceding information, immediately after the transfer,

A. Conservative's total assets decreased by $23,000.

B. Conservative's total assets decreased by $20,000.

C. Conservative's total assets increased by $56,000.

D. Conservative's total assets remained the same.

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-03 Make calculations and prepare journal entries for the creation and purchase of a business entity.

Topic: Accounting for Internal Expansion: Creating Business Entities

14. Riverdell Corporation and Foster Company merged as of January 1, 20X9. To effect the merger, Riverdell paid finder's fees of $40,000, legal fees of $13,000, audit fees related to the stock issuance of $10,000, stock registration fees of $5,000, and stock listing application fees of $4,000.

Based on the preceding information, under the acquisition method, what amount relating to the business combination would be expensed?

A. $72,000

B. $19,000

<u>C.</u> $53,000

D. $63,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Applying the Acquisition Method

15. Riverdell Corporation and Foster Company merged as of January 1, 20X9. To effect the merger, Riverdell paid finder's fees of $40,000, legal fees of $13,000, audit fees related to the stock issuance of $10,000, stock registration fees of $5,000, and stock listing application fees of $4,000.

Based on the preceding information, under the acquisition method:

A. $72,000 of stock issue costs are treated as goodwill.

<u>B.</u> $19,000 of stock issue costs are treated as a reduction in the issue price.

C. $19,000 of stock issue costs are expensed.

D. $72,000 of stock issue costs are expensed.

AACSB: Analytic
AICPA FN: Measurement
Blooms: Understand
Difficulty: 2 Medium
Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.
Topic: Applying the Acquisition Method

16. Burrough Corporation paid $80,000 to acquire all of Helyar Company's net assets. Helyar reported assets with a book value of $60,000 and fair value of $98,000 and liabilities with a book value and fair value of $23,000 on the date of combination. Burrough also paid $3,000 to a search firm for finder's fees related to the acquisition. What amount will be recorded as goodwill by Burrough Corporation while recording its investment in Helyar?

A. $0

<u>B.</u> $5,000

C. $8,000

D. $13,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

17. Plummet Corporation reported the book value of its net assets at $400,000 when Zenith Corporation acquired 100 percent ownership. The fair value of Plummet's net assets was determined to be $510,000 on that date.

Based on the preceding information, what amount of goodwill will be reported in consolidated financial statements presented immediately following the combination if Zenith paid $550,000 for the acquisition?

A. $0

B. $50,000

C. $150,000

<u>D.</u> $40,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

18. Plummet Corporation reported the book value of its net assets at $400,000 when Zenith Corporation acquired 100 percent ownership. The fair value of Plummet's net assets was determined to be $510,000 on that date.

Based on the preceding information, what amount will be recorded by Zenith as its investment in Plummet, if it paid $500,000 for the acquisition?

A. $610,000

B. $400,000

C. $500,000

<u>D.</u> $510,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-02 Understand the history of the development of standards related to acquisition accounting over time.

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Combination Effected through the Acquisition of Net Assets

Topic: The Development of Accounting for Business Combinations

 1-45

19. Plummet Corporation reported the book value of its net assets at $400,000 when Zenith Corporation acquired 100 percent ownership. The fair value of Plummet's net assets was determined to be $510,000 on that date.

Based on the preceding information, what amount of goodwill will be reported in consolidated financial statements presented immediately following the combination if Zenith paid $500,000 for the acquisition?

A. $0
B. $50,000
C. $150,000
D. $40,000

AACSB: Analytic
AICPA FN: Measurement
Blooms: Understand
Difficulty: 2 Medium
Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.
Topic: Goodwill

20. The fair value of net identifiable assets of a reporting unit of X Company is $300,000. On X Company's books, the carrying value of this reporting unit's net assets is $350,000, including $60,000 goodwill. If the fair value of the reporting unit as a whole is $335,000, what amount of goodwill impairment will be recognized for this unit?

A. $0
B. $10,000
C. $25,000
D. $35,000

AACSB: Analytic

1-46

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

21. The fair value of net identifiable assets of a reporting unit of Y Company is $270,000. The carrying value of the reporting unit's net assets on Y Company's books is $320,000, including $50,000 goodwill. If the reported goodwill impairment for the unit is $10,000, what would be the fair value of the reporting unit?

A. $320,000

<u>B.</u> $310,000

C. $270,000

D. $290,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Fair Value Measurements

Topic: Goodwill

22. Following its acquisition of the net assets of Dan Company, Empire Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

	Carrying Amount	Fair Value
Cash	$20,000	$20,000
Inventory	35,000	40,000
Equipment	125,000	160,000
Goodwill	60,000	
Accounts Payable	30,000	30,000

Based on the preceding information, what amount of goodwill (after any impairment) will be reported for this division if its fair value is determined to be $200,000?

A. $0

B. $60,000

C. $30,000

<u>D.</u> $10,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

 1-22

23. Following its acquisition of the net assets of Dan Company, Empire Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

	Carrying Amount	Fair Value
Cash	$20,000	$20,000
Inventory	35,000	40,000
Equipment	125,000	160,000
Goodwill	60,000	
Accounts Payable	30,000	30,000

Based on the preceding information, what amount of goodwill impairment will be recognized for this division if its fair value is determined to be $195,000?

A. $5,000

B. $30,000

C. $60,000

D. $55,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

50. Following its acquisition of the net assets of Dan Company, Empire Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

50. Public Equity Corporation acquired all of Leo Corp's assets and liabilities through an exchange of common shares. All of Leo's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available:

	Carrying Amount	Fair Value
Cash	$20,000	$20,000

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what amount of amount of goodwill impairment will be recognized for this division if its fair value is determined to be $245,000?

A. $0

B. $5,000

C. $60,000

D. $55,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

51. Public Equity Corporation acquired Lemon Corporation through an exchange of common shares. All of Lemon's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available:

51. Following its acquisition of the net assets of Dan Company, Empire Company assigned goodwill of $60,000 to one of the reporting divisions. Information for this division follows:

	Carrying Amount	Fair Value
Cash	$20,000	$20,000

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what number of shares was issued at the time of the exchange?

A. 5,000

B. 17,500

C. 12,500

D. 10,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 1 Easy

Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Combination Effected through Acquisition of Stock

Topic: External Expansion: Business Combinations

1-51

26. Public Equity Corporation acquired Lenore Company through an exchange of common shares. All of Lenore's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available.

All of Lenore's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available.

Public Equity

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what is the par value of Public's common stock?

A. $10

B. $1

C. $5

D. $4

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 1 Easy

Learning Objective: 01-01 Understand and explain the reasons for and different methods of business expansion; the types of organizational structures; and the types of acquisitions.

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Combination Effected through Acquisition of Stock

Topic: External Expansion: Business Combinations

27. Public Equity Corporation acquired Lenore Company through an exchange of common shares. All of Lenore's assets and liabilities were immediately transferred to Public Equity. Public's common stock was trading at $20 per share at the time of exchange. Following selected information is also available.

	Public Equity	
	Before acquisition	After acquisition
Par value of shares outstanding	$200,000	$250,000
Additional paid-in capital	$350,000	$550,000

Based on the preceding information, what is the fair value of Lenore's net assets, if goodwill of $56,000 is recorded?

A. $306,000

B. $244,000

C. $194,000

D. $300,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 2 Medium

Learning Objective: 01-02 Understand the history of the development of standards related to acquisition accounting over time.

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Combination Effected through Acquisition of Stock

Topic: Fair Value Measurements

Topic: The Development of Accounting for Business Combinations

28. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta
Carrying value	$200,000	$320,000	$370,000	$300,000
Goodwill included in carrying value	20,000	34,000	50,000	30,000
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000

Based on the preceding information, what amount of goodwill will be reported for Alpha at year-end?

A. $0

B. $20,000

C. $30,000

D. $10,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

29. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta
Carrying value	$200,000	$320,000	$370,000	$300,000
Goodwill included in carrying value	20,000	34,000	50,000	30,000
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000

Based on the preceding information, what amount of goodwill will be reported for Beta at year-end?

A. $0

B. $14,000

C. $34,000

D. $50,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

30. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta
Carrying value	$200,000	$320,000	$370,000	$300,000
Goodwill included in carrying value	20,000	34,000	50,000	30,000
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000

Based on the preceding information, for Gamma:

A. no goodwill should be reported at year-end.

B. goodwill impairment of $30,000 should be recognized at year-end.

C. goodwill impairment of $20,000 should be recognized at year-end.

D. goodwill of $30,000 should be reported at year-end.

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

31. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta
Carrying value	$200,000	$320,000	$370,000	$300,000
Goodwill included in carrying value	20,000	34,000	50,000	30,000
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000

Based on the preceding information, for Delta:

A. no goodwill should be reported at year-end.

B. goodwill impairment of $15,000 should be recognized at year-end.

C. goodwill impairment of $20,000 should be recognized at year-end.

D. goodwill of $30,000 should be reported at year-end.

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

1-31

32. Pursuing an inorganic growth strategy, Wilson Company acquired Venus Company's net assets and assigned them to four separate reporting divisions. Wilson assigned total goodwill of $134,000 to the four reporting divisions as given below:

	Alpha	Beta	Gamma	Delta
Carrying value	$200,000	$320,000	$370,000	$300,000
Goodwill included in carrying value	20,000	34,000	50,000	30,000
Fair value of net identifiable assets at year-end	150,000	300,000	390,000	280,000
Fair value of reporting unit at year-end	180,000	350,000	360,000	295,000

Based on the preceding information, what would be the total amount of goodwill that Wilson should report at year-end?

A. $0

B. $69,000

C. $79,000

D. $94,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

33. Which of the following observations is (are) consistent with the acquisition method of accounting for business combinations?

I. Expenses related to the business combination are expensed.

II. Stock issue costs are treated as a reduction in the issue price.

III. All merger and stock issue costs are expensed.

IV. No goodwill is ever recorded.

A. III

B. IV

C. I and II

D. I, II, and IV

AACSB: Reflective Thinking

AICPA FN: Reporting

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Applying the Acquisition Method

34. Which of the following observations refers to the term differential?

A. Excess of consideration exchanged over fair value of net identifiable assets.

B. Excess of fair value over book value of net identifiable assets.

C. Excess of consideration exchanged over book value of net identifiable assets.

D. Excess of fair value over historical cost of net identifiable assets.

AACSB: Reflective Thinking

AICPA FN: Reporting

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential;

 1-33

goodwill; or a bargain purchase element.

Topic: Applying the Acquisition Method

35. Which of the following observations concerning "goodwill" is NOT correct?

A. Once written down, it may be written up for recoveries.

B. It must be tested for impairment at least annually.

C. Goodwill impairment losses are recognized in income from continuing operations or income before extraordinary gains and losses.

D. It must be reported as a separate line item in the balance sheet.

AACSB: Reflective Thinking

AICPA FN: Reporting

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

1-60

36. Big Company acquired the following assets and liabilities of Little Company (fair values listed below) for $470,000 cash.

Inventory	$70,000
Land	100,000
Buildings and Equipment	320,000
Current Liabilities	50,000

Assuming these items are all recorded at their acquisition date fair values, what additional item needs to be recorded and how will it be accounted for in the future?

A. $30,000 Goodwill, capitalized and tested for impairment
B. $30,000 Bargain purchase, recognized in current earnings
C. $30,000 Bargain purchase, capitalized and recognized over time
D. $30,000 Goodwill, capitalized and amortized over time

AACSB: Analytic
AICPA FN: Measurement
Blooms: Understand
Difficulty: 2 Medium
Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.
Topic: Bargain Purchase

 1-61

37. Paul Corp. acquired 100 percent of Sam Inc.'s voting stock on July 1, 20X1. The following information was available as of December 31, 20X1:

	Net Income Jan 1 – June 30, 20X1	Net Income July 1, 20X1 – Dec 31, 20X1
Paul Corp.	$300,000	$420,000
Sam Inc.	$150,000	$220,000

How much net income should be reported in Paul Corp's income statement for 20X1?

A. $370,000

B. $720,000

C. $940,000

D. $1,090,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 2 Medium

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Financial Reporting Subsequent to a Business Combination

 1-62

38. Note: This is a Kaplan CPA Review Question

On August 31, 20X1, Wood Corp. issued 100,000 shares of its $20 par value common stock for the net assets of Pine, Inc. in a business combination accounted for by the acquisition method. The market value of Wood's common stock on August 31 was $36 per share. Wood paid a fee of $160,000 to the consultant who arranged this acquisition. Costs of registering and issuing the equity securities amounted to $80,000. No goodwill was involved in the purchase. What amount should Wood capitalize as the cost of acquiring Pine's net assets?

A. $3,680,000

B. $3,600,000

C. $3,760,000

D. $3,840,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Understand

Difficulty: 1 Easy

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Applying the Acquisition Method

39. Note: This is a Kaplan CPA Review Question

Company X acquired for cash all of the outstanding common stock of Company Y. How should Company X determine in general the amounts to be reported for the inventories and long-term debt acquired from Company Y?

Inventories	Long-term debt
A. Fair value	Fair value
B. Fair value	Recorded value
C. Recorded value	Fair value
D. Recorded value	Recorded value

<u>A.</u> Option A

B. Option B

C. Option C

D. Option D

AACSB: Reflective Thinking

AICPA FN: Reporting

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Applying the Acquisition Method

 1-64

40. Point Co. purchased 90% of Sharpe Corp.'s voting stock on January 1, 20X2 for $5,580,000. Prior to the acquisition, Point held a 10% equity position in Sharpe Company. On January 1, 20X2 Pointe's 10% investment in Sharpe has a book value of $340,000 and a fair value of $620,000. On January 1, 20X2 Point records the following:

A. Debit Gain on revaluation of Sharpe's stock $280,000

B. Credit Gain on revaluation of Sharpe's stock $280,000

C. Credit Investment in Sharpe stock $5,860,000

D. Debit Investment in Sharpe stock $6,200,000

AACSB: Reflective Thinking
AICPA FN: Measurement
Blooms: Understand
Difficulty: 2 Medium
Learning Objective: 01-06 Understand additional considerations associated with business combinations.
Topic: Noncontrolling Equity Held Prior to Combination

41. The length of the measurement period allowed to value the assets and liabilities in an acquired business combination starts on the date of acquisition and lasts until:

A. All necessary information about the facts of the acquisition is obtained

B. All necessary information about the facts of the acquisition is obtained, not to exceed one month

C. All necessary information about the facts of the acquisition is obtained, not to exceed one reporting period

D. All necessary information about the facts of the acquisition is obtained, not to exceed one year

AACSB: Reflective Thinking
AICPA FN: Decision Making
Blooms: Remember
Difficulty: 1 Easy

Learning Objective: 01-06 Understand additional considerations associated with business combinations.

Topic: Uncertainty in Business Combinations-Measurement Period

42. ASC 805 requires contingent consideration in a business combination to be classified as:

A. An asset

B. A liability or equity

C. An asset or equity

D. An asset or a liability

AACSB: Reflective Thinking

AICPA FN: Reporting

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-06 Understand additional considerations associated with business combinations.

Topic: Uncertainty in Business Combinations-Contingent Consideration

43. For all acquired contingencies, the acquirer should do all of the following except:

A. Provide documentation from the acquirer's attorney regarding pending lawsuits and loan guarantees

B. Provide a description of each contingency

C. Disclose the amount recognized at the acquisition date

D. Describe the estimated range of possible undiscounted outcomes of the contingency

AACSB: Reflective Thinking

AICPA FN: Decision Making

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-06 Understand additional considerations associated with business combinations.

Topic: Uncertainty in Business Combinations-Acquiree Contingencies

44. ASC 805 requires that ongoing research and development projects be treated in all of the following ways except:

A. Recorded at acquisition-date fair values

B. Classified as intangible assets having indefinite lives

C. Expensed immediately

D. Tested for impairment periodically

AACSB: Reflective Thinking

AICPA FN: Reporting

Blooms: Remember

Difficulty: 1 Easy

Learning Objective: 01-06 Understand additional considerations associated with business combinations.

Topic: In-Process Research and Development

Essay Questions

 1-67

45. On January 1, 20X8, Alaska Corporation acquired Mercantile Corporation's net assets by paying $160,000 cash. Balance sheet data for the two companies and fair value information for Mercantile Corporation immediately before the business combination are given below:

	Alaska	Mercantile	
	Book Value	Book Value	Fair Value
Cash	$200,000	$30,000	$30,000
Accounts Receivable	40,000	22,000	22,000
Inventory	120,000	25,000	36,000
Patents	50,000	20,000	40,000
Buildings and Equipment	330,000	250,000	150,000
Less: Accumulated Depreciation	-140,000	-150,000	
Total Assets	$600,000	$197,000	$278,000
Accounts Payable	$85,000	$55,000	$55,000
Notes Payable	100,000	80,000	80,000
Common Stock:			
$5 par value	120,000		
$2 par value		20,000	
Additional Paid-In Capital	140,000	25,000	
Retained Earnings	155,000	17,000	
Total Liabilities and Equities	$600,000	$197,000	

Required:

Prepare the journal entry to record the acquisition of Mercantile Corporation.

Cash	30,000	
Accounts Receivable	22,000	
Inventory	36,000	
Patents	40,000	
Buildings and Equipment	150,000	
Goodwill	17,000	
Accounts Payable		55,000
Notes Payable		80,000
Cash		160,000

Or if the cash paid is reported net of cash received:

Accounts Receivable	22,000	
Inventory	36,000	
Patents	40,000	
Buildings and Equipment	150,000	
Goodwill	17,000	
Accounts Payable		55,000
Notes Payable		80,000
Cash		130,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 2 Medium

Learning Objective: 01-02 Understand the history of the development of standards related to acquisition accounting over time.

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

Topic: The Development of Accounting for Business Combinations

1-69

46. On January 1, 20X8, Line Corporation acquired all of the common stock of Staff Company for $300,000. On that date, Staff's identifiable net assets had a fair value of $250,000. The assets acquired in the purchase of Staff are considered to be a separate reporting unit of Line Corporation. The carrying value of Staff's investment at December 31, 20X8, is $310,000. The fair value of the net assets (excluding goodwill) at that date is $220,000 and the fair value of the reporting unit is determined to be 260,000.

Required:

1) Explain how goodwill is tested for impairment for a reporting unit.
2) Determine the amount, if any, of impairment loss to be recognized at December 31, 20X8.

1) To test for the impairment of goodwill, the fair value of the reporting unit is compared with its carrying amount. If the fair value of the reporting unit exceeds its carrying amount, the goodwill of that reporting unit is considered unimpaired. On the other hand, if the carrying amount of the reporting unit exceeds its fair value, an impairment of the reporting unit's goodwill is implied. The amount of the reporting unit's goodwill impairment is measured as the excess of the carrying amount of the unit's goodwill over the implied value of its goodwill. The implied value of its goodwill is determined as the excess of the fair value of the reporting unit over the fair value of its net assets excluding goodwill.
2) The $310,000 carrying value exceeds the $260,000 fair value, implying impairment. Implied goodwill = $260,000 - $220,000 = $40,000.
Impairment loss = $50,000 - $40,000 = $10,000.

AACSB: Analytic
AACSB: Communication
AICPA FN: Measurement
Blooms: Apply
Difficulty: 3 Hard
Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.
Topic: Goodwill

 1-70

47. SeaLine Corporation is involved in the distribution of processed marine products. The fair values of assets and liabilities held by three reporting units and other information related to the reporting units owned by SeaLine are as follows:

	Unit X	Unit Y	Unit Z
Cash	$15,000	$45,000	$35,000
Accounts Receivables	15,000	18,000	10,000
Inventory	35,000	60,000	35,000
Land	30,000	45,000	20,000
Buildings	120,000	80,000	50,000
Equipment	140,000	45,000	50,000
Accounts Payable	25,000	45,000	25,000
Fair Value of Reporting Unit	360,000	230,000	220,000
Carrying Value of Investment	375,000	240,000	240,000
Goodwill Included in Carrying Value	50,000	25,000	40,000

Required: Determine the amount of goodwill that SeaLine should report in its current financial statements.

	Unit X	Unit Y	Unit Z
Goodwill Included in Carrying Value	$50,000	$25,000	$40,000
Implied Goodwill at year-end	30,000	0	45,000
Goodwill to be reported at year-end	30,000	0	40,000

Total Goodwill reported = $70,000

AACSB: Analytic

AICPA FN: Measurement

Blooms: Apply

Difficulty: 3 Hard

Learning Objective: 01-05 Make calculations and business combination journal entries in the presence of a differential; goodwill; or a bargain purchase element.

Topic: Goodwill

 1-71