**CHAPTER 1**

**INTERCORPORATE ACQUISITIONS AND INVESTMENTS IN OTHER ENTITIES**

**ANSWERS TO QUESTIONS**

**Q1-1**Complex organizational structures often result when companies do business in a complex business environment. New subsidiaries or other entities may be formed for purposes such as extending operations into foreign countries, seeking to protect existing assets from risks associated with entry into new product lines, separating activities that fall under regulatory controls, and reducing taxes by separating certain types of operations.

**Q1-2**The split-off and spin-off result in the same reduction of reported assets and liabilities. Only the stockholders’ equity accounts of the company are different. The number of shares outstanding remains unchanged in the case of a spin-off and retained earnings or paid-in capital is reduced. Shares of the parent are exchanged for shares of the subsidiary in a split-off, thereby reducing the outstanding shares of the parent company.

**Q1-3**Enron’s management used special-purpose entities to avoid reporting debt on its balance sheet and to create fictional transactions that resulted in reported income. It also transferred bad loans and investments to special-purpose entities to avoid recognizing losses in its income statement.

**Q1-4**(a)  A **statutory merger** occurs when one company acquires another company and the assets and liabilities of the acquired company are transferred to the acquiring company; the acquired company is liquidated, and only the acquiring company remains. The acquiring company can give cash or other assets in addition to stock.

(b)  A **statutory consolidation** occurs when a new company is formed to acquire the assets and liabilities of two combining companies. The combining companies dissolve, and the new company is the only surviving entity.

(c)  A **stock acquisition** occurs when one company acquires a majority of the common stock of another company and the acquired company is not liquidated; both companies remain as separate but related corporations.

**Q1-5**A noncontrolling interest exists when the acquiring company gains control but does not own all the shares of the acquired company. The non-controlling interest is made up of the shares not owned by the acquiring company.

**Q1-6**Goodwill is the excess of the sum of (1) the fair value given by the acquiring company, (2) the fair value of any shares already owned by the parent and (3) the acquisition-date fair value of any noncontrolling interest over the acquisition-date fair value of the net identifiable assets acquired in the business combination.

**Q1-7** A differential isthe total difference at the acquisition date between the sum of (1) the fair value given by the acquiring company, (2) the fair value of any shares already owned by the parent and (3) the acquisition-date fair value of any noncontrolling interest and the book value of the net identifiable assets acquired is referred to as the differential.

**Q1-8**The purchase of a company is viewed in the same way as any other purchase of assets. The acquired company is owned by the acquiring company only for the portion of the year subsequent to the combination. Therefore, earnings are accrued only from the date of purchase forward.

**Q1-9**None of the retained earnings of the subsidiary should be carried forward under the acquisition method. Thus, consolidated retained earnings immediately following an acquisition is limited to the balance reported by the acquiring company.

**Q1-10**Additional paid-in capital reported following a business combination is the amount previously reported on the acquiring company's books plus the excess of the fair value over the par or stated value of any shares issued by the acquiring company in completing the acquisition less any sock issue costs.

**Q1-11**When the acquisition method is used, all costs incurred in bringing about the combination are expensed as incurred. None are capitalized. However, costs associated with the issuance of stock are recorded as a reduction of additional paid-in capital.

**Q1-12**When the acquiring company issues shares of stock to complete a business combination, the excess of the fair value of the stock issued over its par value is recorded as additional paid-in capital. All costs incurred by the acquiring company in issuing the securities should be treated as a reduction in the additional paid-in capital. Items such as audit fees associated with the registration of the new securities, listing fees, and brokers' commissions should be treated as reductions of additional paid-in capital when stock is issued.

**Q1-13**If the fair value of a reporting unit acquired in a business combination 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, impairment of goodwill is implied. An impairment must be recognized if the carrying amount of the goodwill assigned to the reporting unit is greater than the implied value of the carrying unit’s goodwill. The implied value of the reporting unit’s goodwill is determined as the excess of the fair value of the reporting unit over the fair value of its net identifiable assets.

**Q1-14** A bargain purchase occurswhen the fair value of the consideration given in a business combination, along with the fair value of any equity interest in the acquiree already held and the fair value of any noncontrolling interest in the acquiree, is less than the fair value of the acquiree’s net identifiable assets.

**Q1-15** The acquirer should record the clarification of the acquisition-date fair value of buildings as a reduction to buildings and addition to goodwill.

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**Q1-16** The acquirer must revalue the equity position to its fair value at the acquisition date and recognize a gain. A total of $250,000 ($25 x 10,000 shares) would be recognized in this case assuming that the $65 per share price is the appropriate fair value for all shares (i.e. there is no control premium for the new shares purchased).

**SOLUTIONS TO CASES**

**C1-1 Assignment of Acquisition Costs**

MEMO

To:    Vice-President of Finance

         Troy Company

From:                          , CPA

Re:      Recording Acquisition Costs of Business Combination

Troy Company incurred a variety of costs in acquiring the ownership of Kline Company and transferring the assets and liabilities of Kline to Troy Company. I was asked to review the relevant accounting literature and provide my recommendations as to what was the appropriate treatment of the costs incurred in the Kline Company acquisition.

Current accounting standards require that acquired companies be valued under **ASC 805** at the fair value of the consideration given in the exchange, plus the fair value of any shares of the acquiree already held by the acquirer, plus the fair value of any noncontrolling interest in the acquiree at the combination date [ASC 805]. All other acquisition-related costs directly traceable to an acquisition should be accounted for as expenses in the period incurred [ASC 805]. The costs incurred in issuing common or preferred stock in a business combination are required to be treated as a reduction of the recorded amount of the securities (which would be a reduction to additonal paid-in capital if the stock has a par value or a reduction to common stock for no par stock).

A total of $720,000 was paid in completing the Kline acquisition. Kline should record the $200,000 finders’ fee and $90,000 legal fees for transferring Kline’s assets and liabilities to Troy as acquisition expense in 20X7. The $60,000 payment for stock registration and audit fees should be recorded as a reduction of paid-in capital recorded when the Troy Company shares are issued to acquire the shares of Kline. The only cost potentially at issue is the $370,000 legal fees resulting from the litigation by the shareholders of Kline. If this cost is considered to be a direct acquisition cost, it should be included in acquisition expense. If, on the other hand, it is considered to be related to the issuance of the shares, it should be debited to paid-in capital.

*Primary citation*

ASC 805

**C1-2 Evaluation of Merger**

a. AT&T had a vast cable customer base, but felt that TimeWarner’s content would greatly enhance the demand for its cable services.

b. AT&T provided TimeWarner shareholders with AT&T stock and an equal value of cash.

c. The cash portion of the merger was funded primarily with debt.

d. This would be a statutory merger since (1) the AT&T name survived through the merger and (2) the acquisition was formalized when AT&T gave both stock and cash.

**C1-3 Business Combinations**

It is very difficult to develop a single explanation for any series of events. Merger activity in the United States is impacted by events both within the U.S. economy and those around the world. As a result, there are many potential answers to the questions posed in this case.

a. One factor that may have prompted the greater use of stock in business combinations in the middle and late 1990s is that many of the earlier combinations that had been effected through the use of debt had unraveled. In many cases, the debt burden was so heavy that the combined companies could not meet debt payments. Thus, this approach to financing mergers had somewhat fallen from favor by the mid-nineties. Further, with the spectacular rise in the stock market after 1994, many companies found that their stock was worth much more than previously. Accordingly, fewer shares were needed to acquire other companies.

b. Two of major factors appear to have had a significant influence on the merger movement in the mid-2000s. First, interest rates were very low during that time, and a great amount of unemployed cash was available worldwide. Many business combinations were effected through significant borrowing. Second, private equity funds pooled money from various institutional investors and wealthy individuals and used much of it to acquire companies.

Many of the acquisitions of this time period involved private equity funds or companies that acquired other companies with the goal of making quick changes and selling the companies for a profit. This differed from prior merger periods where acquiring companies were often looking for long-term acquisitions that would result in synergies.

In late 2008, a mortgage crisis spilled over into the credit markets in general, and money for acquisitions became hard to get. This in turn caused many planned or possible mergers to be canceled. In addition, the economy in general faltered toward the end of 2008 and into 2009. Since that time, companies have turned their attention to global expansion.

c. Establishing incentives for corporate mergers is a controversial issue. Many people in our society view mergers as not being in the best interests of society because they are seen as lessening competition and often result in many people losing their jobs. On the other hand, many mergers result in companies that are more efficient and can compete better in a global economy; this in turn may result in more jobs and lower prices. Even if corporate mergers are viewed favorably, however, the question arises as to whether the government, and ultimately the taxpayers, should be subsidizing those mergers through tax incentives. Many would argue that the desirability of individual corporate mergers, along with other types of investment opportunities, should be determined on the basis of the merits of the individual situations rather than through tax incentives.

Perhaps the most obvious incentive is to lower capital gains tax rates. Businesses may be more likely to invest in other companies if they can sell their ownership interests when it is convenient and pay lesser tax rates. Another alternative would include exempting certain types of intercorporate income. Favorable tax status might be given to investment in foreign companies through changes in tax treaties. As an alternative, barriers might be raised to discourage foreign investment in United States, thereby increasing the opportunities for domestic firms to acquire ownership of other companies.

d. In an ideal environment, the accounting and reporting for economic events would be accurate and timely and would not influence the economic decisions being reported. Any change in reporting requirements that would increase or decrease management's ability to "manage" earnings could impact management's willingness to enter new or risky business fields and affect the level of business combinations. Greater flexibility in determining which subsidiaries are to be consolidated, the way in which intercorporate income is calculated, the elimination of profits on intercompany transfers, or the process used in calculating earnings per share could impact such decisions. The processes used in translating foreign investment into United States dollars also may impact management's willingness to invest in domestic versus international alternatives.

**C1-4  Determination of Goodwill Impairment**

MEMO

TO:   Chief Accountant

         Plush Corporation

From:                           , CPA

Re:      Determining Impairment of Goodwill

Once goodwill is recorded in a business combination, it must be accounted for in accordance with current accounting literature. Goodwill is carried forward at the original amount without amortization, unless it becomes impaired. The amount determined to be goodwill in a business combination must be assigned to the reporting units of the acquiring entity that are expected to benefit from the synergies of the combination. [ASC 350-20-35-41]

This means the total amount assigned to goodwill may be divided among a number of reporting units. Goodwill assigned to each reporting unit must be tested for impairment annually and between the annual tests in the event circumstances arise that would lead to a possible decrease in the fair value of the reporting unit below its carrying amount [ASC 350-20-35-30, ASU 2017-04].

As long as the fair value of the reporting unit is greater than its carrying value, goodwill is not considered to be impaired. If the fair value is less than the carrying value, an impairment loss must be reported for the amount by which the carrying amount of reporting unit exceeds its fair value. However, the impairment cannot exceed the amount of goodwill originally recognized for that reporting unit [ASC 350-20-35-11, ASU 2017-04]

At the date of acquisition, Plush Corporation recognized goodwill of $20,000 ($450,000 - $430,000) and assigned it to a single reporting unit. Even though the fair value of the reporting unit increased to $485,000 at December 31, 20X5, Plush Corporation must test for impairment of goodwill if the carrying value of Plush’s investment in the reporting unit is above that amount. That would be the case if the carrying value were determined to be $500,000. If the carrying value of the reporting unit’s net assets exceeds the fair value of the reporting unit’s net assets, an impairment is recorded for the amount by which the carrying amount exceeds the fair value (but the impairment is limited to the amount of goodwill reported by that unit). If the carrying amount were $500,000 and the fair value of the reporting unit were $485,000, The impairment would be $15,000 ($500,000 - $485,000). On the other hand, if the fair value were greater than the carrying value, there would be no goodwill impairment. For example, if the carrying value of the reporting unit were determined to be $470,000, there would be no impairment.

With the information provided, we do not know if there has been an impairment of the goodwill involved in the purchase of Common Corporation. However, Plush must follow the procedures outlined here in testing for impairment at December 31, 20X5.

*Primary citations*

ASC 350-20-35-11

ASC 350-20-35-30

ASC 350-20-35-41

ASU 2017-04

**C1-5 Risks Associated with Acquisitions**

Alphabet discloses on pages 9-10 of its 2016 Form 10-K that acquisitions, investments, and divestitures are an important part of its corporate strategy. The company goes on to discuss relevant risks associated with these activities. The specific risk areas identified include:

* The use of management time on acquisitions-related activities may temporarily divert management’s time and focus from normal operations.
* After acquiring companies, there is a risk that Alphabet may not successfully develop the business and technologies of the acquired firms.
* It can be difficult to implement controls, procedures, and policies appropriate for a public company that were not already in place in the acquired company.
* Integrating the accounting, management information, human resources, and other administrative systems can be challenging.
* The company sometimes encounters difficulties in transitioning operations, users, and customers into Alphabet’s existing platforms.
* Government “red tape” in obtaining necessary approvals can reduce the potential strategic benefits of acquisitions.
* There are many difficulties associated with foreign acquisitions due to differences in culture, language, economics, currencies, politic, and regulation.
* Since corporate cultures can vary significantly, there are potential difficulties in integrating the employees of an acquired company into the Google organization.
* It can be difficult to retain employees who worked for companies that Alphabet acquires.
* There may be legal liabilities for activities of acquired companies.
* Litigation of claims against acquired companies or as a result of acquisitions can be problematic.
* Anticipated benefits of acquisitions may not materialize.
* Acquisitions through equity issuances can result in dilution to existing shareholders. Similarly, the issuance of debt can result in other costs. Impairments, restructuring charges, and other unfavorable results can result.

**C1-6 Leveraged Buyouts**

a. A leveraged buyout (LBO) involves acquiring a company in a transaction or series of planned transactions that include using a very high proportion of debt, often secured by the assets of the target company. Normally, the investors acquire all of the stock or assets of the target company. A management buyout (MBO) occurs when the existing management of a company acquires all or most of the stock or assets of the company. Frequently, the investors in LBOs include management, and thus an LBO may also be an MBO

b. The FASB has not dealt with leveraged buyouts in either current pronouncements or exposure drafts of proposed standards. The Emerging Issues Task Force has addressed limited aspects of accounting for LBOs. In EITF 84-23, “Leveraged Buyout Holding Company Debt,” the Task Force did not reach a consensus. In EITF 88-16, “Basis in Leveraged Buyout Transactions,” the Task Force did provide guidance as to the proper basis that should be recognized for an acquiring company’s interest in a target company acquired through a leveraged buyout.

c. Whether an LBO is a type of business combination is not clear and probably depends on the structure of the buyout. The FASB has not taken a position on whether an LBO is a type of business combination. The EITF indicated that LBOs of the type it was considering are similar to business combinations. Most LBOs are effected by establishing a holding company for the purpose of acquiring the assets or stock of the target company. Such a holding company has no substantive operations. Some would argue that a business combination can occur only if the acquiring company has substantive operations. However, neither the FASB nor EITF has established such a requirement. Thus, the question of whether an LBO is a business combination is unresolved.

d. The primary issue in deciding the proper basis for an interest in a company acquired in an LBO, as determined by EITF 88-16, is whether the transaction has resulted in a change in control of the target company (a new controlling shareholder group has been established). If a change in control has not occurred, the transaction is treated as a recapitalization or restructuring, and a change in basis is not appropriate (the previous basis carries over). If a change in control has occurred, a new basis of accounting may be appropriate.

**SOLUTIONS TO EXERCISES**

**E1-1 Multiple-Choice Questions on Complex Organizations**

1. **b** – As companies grow in size and respond to their unique business environment, they often develop complex organizational and ownership structures.

(a) *Incorrect*. The need to avoid legal liability is not a direct result of increased complexity.

(c) *Incorrect.* Part of the reason the business environment is complex is due to the increased number and type of divisions and product lines in companies.

(d) *Incorrect.* This statement is false. There has been an impact on organizational structure and management.

2. **d** – A transfer of product to a subsidiary does not constitute a sale for income purposes and as such would not increase profit for the parent.

(a) *Incorrect*. Shifting risk is a common reason for establishing a subsidiary.

(b) *Incorrect.* Corporations often establish subsidiaries in other regulatory environments so that the parent company is not explicitly affected by the regulatory control.

(c) *Incorrect.* Corporations will often establish subsidiaries to take advantage of tax benefits that exist in different regions.

3. **a** –When a merger occurs, all the assets and liabilities are transferred to the purchasing company and any excess of the purchase price over the fair value of the net assets is recorded as goodwill on the purchaser’s books.

(b) *Incorrect*. This combination results in a parent-subsidiary relationship in which an investment in Penn would be recorded. In the event that goodwill were present in this transaction, it would be reported on the consolidated books and not Randolph’s books.

(c) *Incorrect.* In a spin-off, no change to net assets occurs, and consequently no goodwill is recorded.

(d) *Incorrect.* In a split-off, no change to net assets occurs, and consequently no goodwill is recorded.

4. **b** –In an internal expansion in which the existing company *creates* a new subsidiary, the assets and liabilities are recorded at the carrying values of the original company.

(a) *Incorrect*. This is not in accordance with GAAP; assets are transferred at the parent’s book (carrying) value.

(c) *Incorrect.* Not in accordance with US GAAP; no gain or loss is permitted because the assets are transferred at the parent’s book value.

(d) *Incorrect.* Not in accordance with US GAAP – Goodwill is not created when a company creates a subsidiary through internal expansion.

5. **d** –This is the proper impairment test required under US GAAP, according to FASB 142/ASC 350.

(a) *Incorrect*. This is not the proper test for impairment under US GAAP.

(b) *Incorrect.* This is not the proper test for impairment under US GAAP.

(c) *Incorrect.* This is not the proper test for impairment under US GAAP.

**E1-2 Multiple-Choice Questions on Recording Business Combinations**

**[AICPA Adapted]**

1. **a** – Goodwill equals the excess sum of the consideration given over the sum of the fair value of identifiable assets less liabilities.

(b) *Incorrect*. Assets considered only need be identifiable, not just tangible. For example, patents would be identifiable, but not tangible.

(c) *Incorrect.* Assets considered only have to be identifiable. This includes both tangible and intangible identifiable assets.

(d) *Incorrect.* The calculation of goodwill requires a remeasurement of the assets and liabilities at fair value, not book value.

2. **c** – “Costs of issuing equity securities used to acquire the acquire are treated in the same manner as stock issue costs are normally treated, as a reduction in the paid-in capital associated with the securities” A reduction to the paid-in capital account results in a reduction in the fair value of the securities issued.

(a) *Incorrect*. Stock issue costs are not expensed but are charged as a reduction in paid-in capital.

(b) *Incorrect.* Stock issue costs result in a reduction of stockholder’s equity, not an increase.

(d) *Incorrect.* Stock issue costs result in a reduction of equity, and are not capitalized. They are not added to goodwill.

3. **d** –When a new company is acquired, the assets and liabilities are recorded at fair value.

(a) *Incorrect*. Historical cost is not always reflective of actual value, thus fair values are used.

(b) *Incorrect.* Book value is often different than fair value, thus fair value is the appropriate basis.

(c) *Incorrect.* This method is also unacceptable. Fair value is the appropriate basis.

4. **d** –This combination would result in a bargain purchase.

(a) *Incorrect*. Deferred credits do not arise as a result of fair value of identifiable assets exceeding fair value of the consideration.

(b) *Incorrect.* The fair value is not reduced, and deferred credits do not arise in this situation.

(c) *Incorrect.* The fair value is not reduced, and deferred credits do not arise in this situation.

5. **c** –$875,000 – $800,000 = $75,000. Total consideration given – FV of net assets = Goodwill

**E1-3 Multiple-Choice Questions on Reported Balances [AICPA Adapted]**

1. **d** –$2,900,000. New APIC Balance = existing APIC on Poe’s books + APIC from new stock issuance. (200,000\*($18-$10) + $1,300,000 = $2,900,000)

2. **d** –$600,000. The total balance in the investment account is equal to the total consideration given in the combination. (10,000 \*$60 per share = $600,000)

3. **c** – $150,000. Goodwill = Consideration given – FV of net assets acquired. FV of Net Assets: $80,000 + $190,000 + $560,000 - $180,000 = $650,000. (800,000 – 650,000 = 150,000)

4. **c** – $4,000,000. The increase in net assets is solely attributable to the FV of the consideration given, the nonvoting preferred stock.

(a) *Incorrect*. This answer only reflects the book value of Master’s net assets.

(b) *Incorrect.* This answer only reflects the fair value of Master’s net assets.

(d) *Incorrect.* The additional stock related to the finder’s fee is not capitalized, but rather expensed.

**E1-4 Multiple-Choice Questions Involving Account Balances**

1. **c** –When the parent creates the subsidiary, the equipment is transferred at cost with the accompanying accumulated depreciation (which in effect is the book value). ($100,000/10 = $10,000 per year \* 4 = $40,000.)

(a) *Incorrect*. When a subsidiary is created internally, the assets are transferred as they were on the parent’s books (carrying value). Fair value is not considered.

(b) *Incorrect.* This is the proper carrying value of the asset, but it should be recorded at cost with the accompanying accumulated depreciation.

(d) *Incorrect.* When a subsidiary is created internally, the assets are transferred as they were on the parent’s books (carrying value).

2. **c** –The assets are transferred at the carrying value on Pead’s books, and thus no change in reported net assets occurs.

(a) *Incorrect*. No change occurs.

(b) *Incorrect.* No change occurs.

(d) *Incorrect.* No change occurs.

3. **b** –APIC = $140,000 (BV) – 7,000 \* $8 = $84,000.

4. **b** –$35,000. Since the carrying value of the reporting unit ($330,000) is lower than the fair value of the reporting unit’s net assets ($350,000), the goodwill of the reporting unit is not impaired and will remain at its carrying value of $35,000

5. **c** –$15,000. The carrying value of the reporting unit’s net assets ($575,000) exceeds the estimated fair value of the reporting unit ($560,000). The goodwill should be impaired by the amount by which the carrying value of the unit’s net assets exceeds the estimated fair value of the reporting unit, $15,000 ($575,000 - $560,000).

**E1-5 Asset Transfer to Subsidiary**

a. Journal entry recorded by Pale Company for transfer of assets to Sight Company:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Sight Company Common Stock | 408,000 |  |
|  | Accumulated Depreciation – Buildings | 24,000 |  |
|  | Accumulated Depreciation – Equipment | 36,000 |  |
|  | Cash |  | 21,000 |
|  | Inventory |  | 37,000 |
|  | Land |  | 80,000 |
|  | Buildings |  | 240,000 |
|  | Equipment |  | 90,000 |

b. Journal entry recorded by Sight Company for receipt of assets from Pale Company:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 21,000 |  |
|  | Inventory | 37,000 |  |
|  | Land | 80,000 |  |
|  | Buildings | 240,000 |  |
|  | Equipment | 90,000 |  |
|  | Accumulated Depreciation – Buildings |  | 24,000 |
|  | Accumulated Depreciation – Equipment |  | 36,000 |
|  | Common Stock |  | 60,000 |
|  | Additional Paid-In Capital |  | 348,000 |

**E1-6 Creation of New Subsidiary**

a. Journal entry recorded by Pester Company for transfer of assets to Shumby Corporation:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Shumby Corporation Common Stock | 498,000 |  |
|  | Allowance for Uncollectible Accounts Receivable | 7,000 |  |
|  | Accumulated Depreciation – Buildings | 35,000 |  |
|  | Accumulated Depreciation – Equipment | 60,000 |  |
|  | Cash |  | 40,000 |
|  | Accounts Receivable |  | 75,000 |
|  | Inventory |  | 50,000 |
|  | Land |  | 35,000 |
|  | Buildings |  | 160,000 |
|  | Equipment |  | 240,000 |

b. Journal entry recorded by Shumby Corporation for receipt of assets from Pester Company:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 40,000 |  |
|  | Accounts Receivable | 75,000 |  |
|  | Inventory | 50,000 |  |
|  | Land | 35,000 |  |
|  | Buildings | 160,000 |  |
|  | Equipment | 240,000 |  |
|  | Allowance for Uncollectible  Accounts Receivable |  | 7,000 |
|  | Accumulated Depreciation – Buildings |  | 35,000 |
|  | Accumulated Depreciation – Equipment |  | 60,000 |
|  | Common Stock |  | 120,000 |
|  | Additional Paid-In Capital |  | 378,000 |

**E1-7 Balance Sheet Totals of Parent Company**

a. Journal entry recorded by Phoster Corporation for transfer of assets and accounts payable to Skine Company:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Skine Company Common Stock | 66,000 |  |
|  | Accumulated Depreciation | 28,000 |  |
|  | Accounts Payable | 22,000 |  |
|  | Cash |  | 15,000 |
|  | Accounts Receivable |  | 24,000 |
|  | Inventory |  | 9,000 |
|  | Land |  | 3,000 |
|  | Depreciable Assets |  | 65,000 |

b. Journal entry recorded by Skine Company for receipt of assets and accounts payable from Phoster Corporation:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 15,000 |  |
|  | Accounts Receivable | 24,000 |  |
|  | Inventory | 9,000 |  |
|  | Land | 3,000 |  |
|  | Depreciable Assets | 65,000 |  |
|  | Accumulated Depreciation |  | 28,000 |
|  | Accounts Payable |  | 22,000 |
|  | Common Stock |  | 48,000 |
|  | Additional Paid-In Capital |  | 18,000 |

**E1-8 Acquisition of Net Assets**

|  |
| --- |
| Pun Corporation will record the following journal entries: |

|  |  |  |  |
| --- | --- | --- | --- |
| (1) | Assets | 71,000 |  |
|  | Goodwill | 9,000 |  |
|  | Liabilities |  | 20,000 |
|  | Cash |  | 60,000 |
|  |  |  |  |
| (2) | Merger Expense | 4,000 |  |
|  | Cash |  | 4,000 |

**E1-9 Reporting Goodwill**

a. Goodwill: $120,000 = $310,000 - $190,000

Investment: $310,000

b. Goodwill: $6,000 = $196,000 - $190,000

Investment: $196,000

c. Goodwill: $0; no goodwill is recorded when the purchase price is below the fair

value of the net identifiable assets.

Investment: $190,000; recorded at the fair value of the net identifiable assets.

**E1-10 Stock Acquisition**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | Journal entry to record the purchase of Sippy Inc., shares: | | | |
|  | |  |  |  | |
|  | | Investment in Sippy Inc., Common Stock | 986,000 |  | |
|  | | Common Stock |  | 425,000 | |
|  | | Additional Paid-In Capital |  | 561,000 | |
|  | |  |  |  | |
|  | | $986,000 = $58 x 17,000 shares |  |  | |
|  | | $425,000 = $25 x 17,000 shares |  |  | |
|  | | $561,000 = ($58 - $25) x 17,000 shares |  |  | |

**E1-11 Balances Reported Following Combination**

|  |  |  |
| --- | --- | --- |
| a. | Stock Outstanding: $200,000 + ($10 x 8,000 shares) | $280,000 |
|  |  |  |
| b. | Cash and Receivables: $150,000 + $40,000 | 190,000 |
|  |  |  |
| c. | Land: $100,000 + $85,000 | 185,000 |
|  |  |  |
| d. | Buildings and Equipment (net): $300,000 + $230,000 | 530,000 |
|  |  |  |
| e. | Goodwill: ($50 x 8,000) - $355,000 | 45,000 |
|  |  |  |
| f. | Additional Paid-In Capital:  $20,000 + [($50 - $10) x 8,000] | 340,000 |
|  |  |  |
| g. | Retained Earnings | 330,000 |

**E1-12 Goodwill Recognition**

Journal entry to record acquisition of Spur Corporation net assets:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash and Receivables | 40,000 |  |
|  | Inventory | 150,000 |  |
|  | Land | 30,000 |  |
|  | Plant and Equipment | 350,000 |  |
|  | Patent | 130,000 |  |
|  | Goodwill | 55,000 |  |
|  | Accounts Payable |  | 85,000 |
|  | Cash |  | 670,000 |

Computation of goodwill

|  |  |  |  |
| --- | --- | --- | --- |
|  | Fair value of consideration given |  | $670,000 |
|  | Fair value of assets acquired | $700,000 |  |
|  | Fair value of liabilities assumed | (85,000) |  |
|  | Fair value of net assets acquired |  | 615,000 |
|  | Goodwill |  | $ 55,000 |
|  |  |  |  |

**E1-13 Acquisition Using Debentures**

Journal entry to record acquisition of Sorden Company net assets:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash and Receivables | 50,000 |  |
|  | Inventory | 200,000 |  |
|  | Land | 100,000 |  |
|  | Plant and Equipment | 300,000 |  |
|  | Discount on Bonds Payable | 17,000 |  |
|  | Goodwill | 8,000 |  |
|  | Accounts Payable |  | 50,000 |
|  | Bonds Payable |  | 625,000 |

Computation of goodwill

|  |  |  |  |
| --- | --- | --- | --- |
|  | Fair value of consideration given |  | $608,000 |
|  | Fair value of assets acquired | $650,000 |  |
|  | Fair value of liabilities assumed | (50,000) |  |
|  | Fair value of net assets acquired |  | 600,000 |
|  | Goodwill |  | $ 8,000 |
|  |  |  |  |

**E1-14 Bargain Purchase**

|  |
| --- |
| Journal entry to record acquisition of Sorden Company net assets: |

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash and Receivables | 50,000 |  |
|  | Inventory | 200,000 |  |
|  | Land | 100,000 |  |
|  | Plant and Equipment | 300,000 |  |
|  | Discount on Bonds Payable | 16,000 |  |
|  | Accounts Payable |  | 50,000 |
|  | Bonds Payable |  | 580,000 |
|  | Gain on Bargain Purchase of Subsidiary |  | 36,000 |
|  |  |  |  |
|  |  |  |  |

Computation of Bargain Purchase Gain

|  |  |  |  |
| --- | --- | --- | --- |
|  | Fair value of consideration given |  | $564,000 |
|  | Fair value of assets acquired | $650,000 |  |
|  | Fair value of liabilities assumed | (50,000) |  |
|  | Fair value of net assets acquired |  | 600,000 |
|  | Bargain Purchase Gain |  | $ 36,000 |

**E1-15 Goodwill Impairment**

a. Goodwill of $80,000 will be reported. The fair value of the reporting unit ($340,000) is greater than the carrying amount of the reporting unit ($290,000). As a result, no impairment loss will be recorded.

b. An impairment loss of $10,000 ($290,000 - $280,000) will be recognized. Therefore, goodwill of $70,000 will be reported (80,000 – 10,000 impairment loss).

c. An impairment loss of $30,000 ($290,000 - $260,000) will be recognized. Therefore, goodwill of $50,000 will be reported (80,000 – 30,000 impairment loss).

**E1-16 Goodwill Impairment**

a. No impairment loss will be recognized. The estimated fair value of the reporting unit ($530,000) is greater than the carrying value of the reporting unit’s net assets ($500,000).

b. A goodwill impairment of $15,000 will be recognized ($500,000 - $485,000).

c. A goodwill impairment of $50,000 will be recognized ($500,000 - $450,000).

**E1-17 Goodwill Assigned to Reporting Units**

Goodwill of $146,000 ($50,000 + $48,000 + $8,000 + $40,000) should be reported, computed as follows:

Reporting Unit A: A goodwill impairment of $10,000 should be recognized ($700,000 - $690,000). Thus, goodwill of $50,000 ($60,000 - $10,000 impairment) should be reported on December 31, 20X7..

Reporting Unit B: There is no goodwill impairment because the fair value of the reporting unit exceeds the carrying value. Goodwill of $48,000 should be reported on December 31, 20X7.

Reporting Unit C: A goodwill impairment of $20,000 should be recognized ($380,000 - $370,000). Thus, goodwill of $8,000 ($28,000 - $20,000 impairment) should be reported on December 31, 20X7.

Reporting Unit D: There is no goodwill impairment because the fair value of the reporting unit exceeds the carrying value. Goodwill of $40,000 should be reported.

**E1-18 Goodwill Measurement**

a. The fair value of the reporting unit ($580,000) is greater than the carrying value of the investment ($550,000). Thus, goodwill is not impaired Goodwill of $150,000 will be reported.

b. The carrying value of the reporting unit ($550,000) exceeds the fair value of the reporting unit ($540,000). Thus, an impairment of goodwill of $10,000 ($550,000 - $540,000) must be recognized. Goodwill of $140,000 will be reported.

c. The carrying value of the reporting unit ($550,000) exceeds the fair value of the reporting unit ($500,000). Thus, an impairment loss of $50,000 ($550,000 - $500,000) must be recognized. Goodwill of $100,000 will be reported.

d. The carrying value of the reporting unit ($550,000) exceeds the fair value of the reporting unit ($460,000). Thus, an impairment loss of $90,000 ($550,000 - $460,000) must be recognized. Goodwill of $60,000 will be reported.

**E1-19 Computation of Fair Value**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Amount paid |  | $517,000 |
|  | Book value of assets | $624,000 |  |
|  | Book value of liabilities | (356,000) |  |
|  | Book value of net assets | $268,000 |  |
|  | Adjustment for research and development costs | (40,000) |  |
|  | Adjusted book value | $228,000 |  |
|  | Fair value of patent rights | 120,000 |  |
|  | Goodwill recorded | 93,000 | (441,000) |
|  | Fair value increment of buildings and equipment |  | $ 76,000 |
|  | Book value of buildings and equipment |  | 341,000 |
|  | Fair value of buildings and equipment |  | $417,000 |

**E1-20 Computation of Shares Issued and Goodwill**

|  |  |  |  |
| --- | --- | --- | --- |
| a. | 15,600 shares were issued, computed as follows: | | |
|  |  |  |  |
|  | Par value of shares outstanding following merger |  | $327,600 |
|  | Paid-in capital following merger |  | 650,800 |
|  | Total par value and paid-in capital |  | $978,400 |
|  | Par value of shares outstanding before merger | $218,400 |  |
|  | Paid-in capital before merger | 370,000 |  |
|  |  |  | (588,400) |
|  | Increase in par value and paid-in capital |  | $390,000 |
|  | Divide by price per share |  | ÷    $25 |
|  | Number of shares issued |  | 15,600 |
|  |  |  |  |
| b. | The par value is $7, computed as follows: |  |  |
|  |  |  |  |
|  | Increase in par value of shares outstanding ($327,600 - $218,400) |  |  |
|  | Divide by number of shares issued |  | $109,200 |
|  | Par value |  | ÷  15,600 |
|  |  |  | $ 7.00 |
|  |  |  |  |
| c. | Goodwill of $34,000 was recorded, computed as follows: | | |
|  |  |  |  |
|  | Increase in par value and paid-in capital |  | $390,000 |
|  | Fair value of net assets ($476,000 - $120,000) |  | (356,000) |
|  | Goodwill |  | $ 34,000 |

**E1-21 Combined Balance Sheet**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Pam Corporation and Slest Company  Combined Balance Sheet  January 1, 20X2 | | | | | |
|  |  |  | | |  |
| Cash and Receivables | $ 240,000 | Accounts Payable | | | $ 125,000 |
| Inventory | 460,000 | Notes Payable | | | 235,000 |
| Buildings and Equipment | 840,000 | Common Stock | | | 244,000 |
| Less: Accumulated Depreciation | (250,000) | Additional Paid-In Capital | | | 556,000 |
| Goodwill | 75,000 | Retained Earnings | | | 205,000 |
|  | $1,365,000 |  | | | $1,365,000 |
| Computation of goodwill | | |  |
|  | | |  |
| Fair value of compensation given | | | $480,000 |
| Fair value of net identifiable assets  ($490,000 - $85,000) | | | (405,000) |
| Goodwill | | | $  75,000 |

Computation of APIC

|  |  |
| --- | --- |
| Fair value of compensation given ($60 x 8,000 shares)  Less par value of shares issued ($8 x 8,000) | $480,000  (64,000) |
| Plus existing APIC from Pam’s books | 140,000 |
| Additional Paid-In Capital | $  556,000 |

**E1-22 Recording a Business Combination**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Merger Expense | 54,000 |  |
|  | Deferred Stock Issue Costs | 29,000 |  |
|  | Cash |  | 83,000 |
|  |  |  |  |
|  | Cash | 70,000 |  |
|  | Accounts Receivable | 110,000 |  |
|  | Inventory | 200,000 |  |
|  | Land | 100,000 |  |
|  | Buildings and Equipment | 350,000 |  |
|  | Goodwill (1) | 30,000 |  |
|  | Accounts Payable |  | 195,000 |
|  | Bonds Payable |  | 100,000 |
|  | Bond Premium |  | 5,000 |
|  | Common Stock |  | 320,000 |
|  | Additional Paid-In Capital (2) |  | 211,000 |
|  | Deferred Stock Issue Costs |  | 29,000 |

Computation of goodwill

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Fair value of consideration given (40,000 x $14) | | $560,000 | | |
|  | Fair value of assets acquired | $830,000 | |  |
|  | Fair value of liabilities assumed | (300,000) | |  |
|  | Fair value of net assets acquired | | (530,000) | | |
|  | Goodwill | | $ 30,000 | | |

Computation of additional paid-in capital

|  |  |  |
| --- | --- | --- |
|  | Number of shares issued | 40,000 |
|  | Issue price in excess of par value ($14 - $8) | x       $6 |
|  | Total | $240,000 |
|  | Less: Deferred stock issue costs | (29,000) |
|  | Increase in additional paid-in capital | $211,000 |

**E1-23 Reporting Income**

|  |  |  |  |
| --- | --- | --- | --- |
|  |  |  |  |
| 20X2: | Net income | = | $6,028,000 [$2,500,000 + $3,528,000] |
|  | Earnings per share | = | $5.48 [$6,028,000 / (1,000,000 + 100,000\*)] |
|  |  |  |  |
| 20X1: | Net income | = | $4,460,000 [previously reported] |
|  | Earnings per share | = | $4.46 [$4,460,000 / 1,000,000] |
|  |  |  |  |
|  | \* 100,000 = 200,000 shares x ½ year | | |

**SOLUTIONS TO PROBLEMS**

**P1-24 Assets and Accounts Payable Transferred to Subsidiary**

a. Journal entry recorded by Pab Corporation for its transfer of

assets and accounts payable to Sollon Company:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Sollon Company Common Stock | 320,000 |  |
|  | Accounts Payable | 45,000 |  |
|  | Accumulated Depreciation – Buildings | 40,000 |  |
|  | Accumulated Depreciation – Equipment | 10,000 |  |
|  | Cash |  | 25,000 |
|  | Inventory |  | 70,000 |
|  | Land |  | 60,000 |
|  | Buildings |  | 170,000 |
|  | Equipment |  | 90,000 |

b. Journal entry recorded by Sollon Company for receipt of assets

and accounts payable from Pab Corporation:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 25,000 |  |
|  | Inventory | 70,000 |  |
|  | Land | 60,000 |  |
|  | Buildings | 170,000 |  |
|  | Equipment | 90,000 |  |
|  | Accounts Payable |  | 45,000 |
|  | Accumulated Depreciation – Buildings |  | 40,000 |
|  | Accumulated Depreciation – Equipment |  | 10,000 |
|  | Common Stock |  | 180,000 |
|  | Additional Paid-In Capital |  | 140,000 |

**P1-25 Creation of New Subsidiary**

a. Journal entry recorded by Pagle Corporation for transfer of assets

and accounts payable to Sand Corporation:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Sand Corporation Common Stock | 400,000 |  |
|  | Allowance for Uncollectible Accounts Receivable | 5,000 |  |
|  | Accumulated Depreciation | 40,000 |  |
|  | Accounts Payable | 10,000 |  |
|  | Cash |  | 30,000 |
|  | Accounts Receivable |  | 45,000 |
|  | Inventory |  | 60,000 |
|  | Land |  | 20,000 |
|  | Buildings and Equipment |  | 300,000 |

b. Journal entry recorded by Sand Corporation for receipt of assets and

accounts payable from Pagle Corporation:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 30,000 |  |
|  | Accounts Receivable | 45,000 |  |
|  | Inventory | 60,000 |  |
|  | Land | 20,000 |  |
|  | Buildings and Equipment | 300,000 |  |
|  | Allowance for Uncollectible Accounts Receivable |  | 5,000 |
|  | Accumulated Depreciation |  | 40,000 |
|  | Accounts Payable |  | 10,000 |
|  | Common Stock |  | 50,000 |
|  | Additional Paid-In Capital |  | 350,000 |

**P1-26 Incomplete Data on Creation of Subsidiary**

a. The book value of assets transferred was $152,000 ($3,000 + $16,000 + $27,000 + $9,000 + $70,000 + $60,000 - $21,000 - $12,000).

b. Plumb Company would report its investment in Stew Company equal to the book value of net assets transferred of $138,000 ($152,000 - $14,000).

c. 8,000 shares ($40,000/$5).

d. Total assets declined by $14,000 (book value of assets transferred of $152,000 - investment in Stew Company of $138,000).

e. No effect. The shares outstanding reported by Plumb Company are not affected by the creation of Stew Company.

**P1-27 Acquisition in Multiple Steps**

|  |
| --- |
| Peal Corporation will record the following entries: |

|  |  |  |  |
| --- | --- | --- | --- |
| (1) | Investment in Seed Company Stock | 85,000 |  |
|  | Common Stock - $10 Par Value |  | 40,000 |
|  | Additional Paid-In Capital |  | 45,000 |
|  |  |  |  |
| (2) | Merger Expense | 3,500 |  |
|  | Additional Paid-In Capital | 2,000 |  |
|  | Cash |  | 5,500 |
|  |  |  |  |

**P1-28 Journal Entries to Record a Business Combination**

Journal entries to record acquisition of SKK net assets:

|  |  |  |  |
| --- | --- | --- | --- |
| (1) | Merger Expense | 14,000 |  |
|  | Cash |  | 14,000 |
|  | Record payment of legal fees. |  |  |
|  |  |  |  |
| (2) | Deferred Stock Issue Costs | 28,000 |  |
|  | Cash |  | 28,000 |
|  | Record costs of issuing stock. |  |  |
|  |  |  |  |
| (3) | Cash and Receivables | 28,000 |  |
|  | Inventory | 122,000 |  |
|  | Buildings and Equipment | 470,000 |  |
|  | Goodwill | 12,000 |  |
|  | Accounts Payable |  | 41,000 |
|  | Notes Payable |  | 63,000 |
|  | Common Stock |  | 96,000 |
|  | Additional Paid-In Capital |  | 404,000 |
|  | Deferred Stock Issue Costs |  | 28,000 |
|  | Record purchase of SKK Corporation. |  |  |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given (24,000 x $22) | $528,000 |
|  | Fair value of net assets acquired ($620,000 - $104,000) | (516,000) |
|  | Goodwill | $ 12,000 |

Computation of additional paid-in capital

|  |  |  |
| --- | --- | --- |
|  | Number of shares issued | 24,000 |
|  | Issue price in excess of par value ($22 - $4) | x       $18 |
|  | Total | $432,000 |
|  | Less: Deferred stock issue costs | (28,000) |
|  | Increase in additional paid-in capital | $404,000 |

**P1-29 Recording Business Combinations**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Merger Expense | 38,000 |  |
|  | Deferred Stock Issue Costs | 22,000 |  |
|  | Cash |  | 60,000 |
|  |  |  |  |
|  | Cash and Equivalents | 41,000 |  |
|  | Accounts Receivable | 73,000 |  |
|  | Inventory | 144,000 |  |
|  | Land | 200,000 |  |
|  | Buildings | 1,500,000 |  |
|  | Equipment | 300,000 |  |
|  | Goodwill | 127,000 |  |
|  | Accounts Payable |  | 35,000 |
|  | Short-Term Notes Payable |  | 50,000 |
|  | Bonds Payable |  | 500,000 |
|  | Common Stock $2 Par |  | 900,000 |
|  | Additional Paid-In Capital |  | 878,000 |
|  | Deferred Stock Issue Costs |  | 22,000 |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given (450,000 x $4) | $1,800,000 |
|  | Fair value of net assets acquired ($41,000  + $73,000 + $144,000 + $200,000 + $1,500,000  + $300,000 - $35,000 - $50,000 - $500,000) | (1,673,000) |
|  | Goodwill | $ 127,000 |

Computation of additional paid-in capital

|  |  |  |
| --- | --- | --- |
|  | Number of shares issued | 450,000 |
|  | Issue price in excess of par value ($4 - $2) | x       $2 |
|  | Total | $900,000 |
|  | Less: Deferred stock issue costs | (22,000) |
|  | Increase in additional paid-in capital | $878,000 |

**P1-30 Business Combination with Goodwill**

a. Journal entry to record acquisition of Sink Company net assets:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 20,000 |  |
|  | Accounts Receivable | 35,000 |  |
|  | Inventory | 50,000 |  |
|  | Patents | 60,000 |  |
|  | Buildings and Equipment | 150,000 |  |
|  | Goodwill | 38,000 |  |
|  | Accounts Payable |  | 55,000 |
|  | Notes Payable |  | 120,000 |
|  | Cash |  | 178,000 |

b. Balance sheet immediately following acquisition:

|  |  |  |  |
| --- | --- | --- | --- |
| Pancor Corporation and Sink Company  Combined Balance Sheet  February 1, 20X3 | | | |
| Cash | $ 82,000 | Accounts Payable | $140,000 |
| Accounts Receivable | 175,000 | Notes Payable | 270,000 |
| Inventory | 220,000 | Common Stock | 200,000 |
| Patents | 140,000 | Additional Paid-In |  |
| Buildings and Equipment | 530,000 | Capital | 160,000 |
| Less: Accumulated |  | Retained Earnings | 225,000 |
| Depreciation | (190,000) |  |  |
| Goodwill | 38,000 |  |  |
|  | $995,000 |  | $995,000 |

c. Journal entry to record acquisition of Sink Company stock:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Sink Company Common Stock | 178,000 |  |
|  | Cash |  | 178,000 |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given | $178,000 |
|  | Fair value of net assets acquired  ($20,000 + $35,000 + $50,000 + $60,000  + $150,000 - $55,000 -$120,000) | (140,000) |
|  | Goodwill | $ 38,000 |

**P1-31 Bargain Purchase**

Journal entries to record acquisition of Sark Corporation net assets:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Merger Expense | 5,000 |  |
|  | Cash |  | 5,000 |
|  |  |  |  |
|  | Cash and Receivables | 50,000 |  |
|  | Inventory | 150,000 |  |
|  | Buildings and Equipment (net) | 300,000 |  |
|  | Patent | 200,000 |  |
|  | Accounts Payable |  | 30,000 |
|  | Cash |  | 625,000 |
|  | Gain on Bargain Purchase of Sark Corporation |  | 45,000 |

Computation of gain

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given | $625,000 |
|  | Fair value of net assets acquired ($700,000 - $30,000) | (670,000) |
|  | Gain on bargain purchase | $ 45,000 |

**P1-32 Computation of Account Balances**

|  |  |  |  |
| --- | --- | --- | --- |
| a. | Acquisition price of reporting unit  ($7.60 x 100,000) | $760,000 |  |
|  | Fair value of net assets at acquisition ($810,000 - $190,000) | (620,000) |  |
|  | Goodwill at acquisition | $140,000 |  |

|  |  |  |
| --- | --- | --- |
| b. | Maximum carrying value of reporting unit’s assets: |  |
|  | Carrying value of assets at year-end | $ X |
|  | Less: Carrying value of liabilities at year-end (given) | (70,000) |
|  | Carrying value of net assets at year-end | $ X - $70,000 |
|  | Less: Fair value of the reporting unit’s net assets | $ (930,000) |
|  | Maximum carrying value of assets | $0  X - $70,00 = $930,000  X = $1,000,000 |

**P1-33 Goodwill Assigned to Multiple Reporting Units**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| a. | A goodwill impairment of $95,000 ($20,000 + $50,000 + $25,000) must be reported in the current period for Prover Company: | | | |
|  | | Computation of goodwill impairment: |  |  |
|  | | Reporting unit A |  |  |
|  | | Carrying value of reporting unit |  | $420,000 |
|  | | Less: Fair value of reporting unit |  | (400,000) |
|  | | Goodwill impairment at year-end |  | $ 20,000 |

|  |  |  |  |
| --- | --- | --- | --- |
|  | Reporting unit B |  |  |
|  | Carrying value of reporting unit |  | $500,000 |
|  | Less: Fair value of reporting unit |  | (440,000) |
|  | Goodwill impairment at year-end |  | $ 60,000\* |
|  |  |  |  |
| \* Limited to the amount of goodwill on the reporting unit’s books ($50,000). | | | |

|  |  |  |  |
| --- | --- | --- | --- |
|  | Reporting unit C |  |  |
|  | Carrying value of reporting unit |  | $290,000 |
|  | Less: Fair value of reporting unit |  | (265,000) |
|  | Goodwill impairment at year-end |  | $ 25,000 |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| b. | Goodwill to be reported by Prover Company: | | | |
|  |  |  | | |
|  |  | Reporting Unit | | |
|  |  | A | B | C |
|  | Carrying value of goodwill | $70,000 | $50,000)\* | $40,000 |
|  | Less: Impairment | (20,000) | (50,000)\* | (25,000) |
|  | Goodwill to be reported at year-end | 50,000 | 0)\* | 15,000 |

\* Limited to the amount of goodwill on the reporting unit’s books.

|  |  |  |
| --- | --- | --- |
|  | Total goodwill to be reported at year-end: |  |
|  | Reporting unit A | $  50,000 |
|  | Reporting unit B | 0 |
|  | Reporting unit C | 15,000 |
|  | Total goodwill to be reported | $65,000 |

**P1-34 Journal Entries**

Journal entries to record acquisition of Steel net assets:

|  |  |  |  |
| --- | --- | --- | --- |
| (1) | Merger Expense | 19,000 |  |
|  | Cash |  | 19,000 |
|  | Record finder's fee and transfer costs. |  |  |
|  |  |  |  |
| (2) | Deferred Stock Issue Costs | 9,000 |  |
|  | Cash |  | 9,000 |
|  | Record audit fees and stock registration fees. | |  |
|  |  |  |  |
| (3) | Cash | 60,000 |  |
|  | Accounts Receivable | 100,000 |  |
|  | Inventory | 115,000 |  |
|  | Land | 70,000 |  |
|  | Buildings and Equipment | 350,000 |  |
|  | Bond Discount | 20,000 |  |
|  | Goodwill | 95,000 |  |
|  | Accounts Payable |  | 10,000 |
|  | Bonds Payable |  | 200,000 |
|  | Common Stock |  | 120,000 |
|  | Additional Paid-In Capital |  | 471,000 |
|  | Deferred Stock Issue Costs |  | 9,000 |
|  | Record merger with Steel Company. | | |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given (12,000 x $50) | $600,000 |
|  | Fair value of net assets acquired ($695,000 - $10,000   - $180,000) | (505,000) |
|  | Goodwill | $ 95,000 |

Computation of additional paid-in capital

|  |  |  |
| --- | --- | --- |
|  | Number of shares issued | 12,000 |
|  | Issue price in excess of par value ($50 - $10) | x       $40 |
|  | Total | $480,000 |
|  | Less: Deferred stock issue costs | (9,000) |
|  | Increase in additional paid-in capital | $471,000 |

**P1-35 Purchase at More than Book Value**

a. Journal entry to record acquisition of Stafford Industries net assets:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 30,000 |  |
|  | Accounts Receivable | 60,000 |  |
|  | Inventory | 160,000 |  |
|  | Land | 30,000 |  |
|  | Buildings and Equipment | 350,000 |  |
|  | Bond Discount | 5,000 |  |
|  | Goodwill | 125,000 |  |
|  | Accounts Payable |  | 10,000 |
|  | Bonds Payable |  | 150,000 |
|  | Common Stock |  | 80,000 |
|  | Additional Paid-In Capital |  | 520,000 |

b. Balance sheet immediately following acquisition:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Pamrod Manufacturing and Stafford Industries  Combined Balance Sheet  January 1, 20X2 | | | | |
| Cash | $  100,000 | Accounts Payable |  | $ 60,000 |
| Accounts Receivable | 160,000 | Bonds Payable | $450,000 |  |
| Inventory | 360,000 | Less: Discount | (5,000) | 445,000 |
| Land | 80,000 | Common Stock |  | 280,000 |
| Buildings and Equipment | 950,000 | Additional | |  |
| Less: Accumulated |  | Paid-In Capital |  | 560,000 |
| Depreciation | (250,000) | Retained Earnings |  | 180,000 |
| Goodwill | 125,000 |  |  |  |
|  | $1,525,000 |  |  | $1,525,000 |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given (4,000 x $150) | $600,000 |
|  | Fair value of net assets acquired ($630,000 - $10,000   - $145,000) | (475,000) |
|  | Goodwill | $125,000 |

**P1-36 Business Combination**

Journal entry to record acquisition of Shoot-Toot Tuba net assets:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Cash | 300 |  |
|  | Accounts Receivable | 17,000 |  |
|  | Inventory | 35,000 |  |
|  | Plant and Equipment | 500,000 |  |
|  | Other Assets | 25,800 |  |
|  | Goodwill | 86,500 |  |
|  | Allowance for Uncollectibles |  | 1,400 |
|  | Accounts Payable |  | 8,200 |
|  | Notes Payable |  | 10,000 |
|  | Mortgage Payable |  | 50,000 |
|  | Bonds Payable |  | 100,000 |
|  | Capital Stock ($10 par) |  | 90,000 |
|  | Premium on Capital Stock |  | 405,000 |

Computation of fair value of net assets acquired

|  |  |  |
| --- | --- | --- |
|  | Cash | $300 |
|  | Accounts Receivable | 17,000 |
|  | Allowance for Uncollectible Accounts | (1,400) |
|  | Inventory | 35,000 |
|  | Plant and Equipment | 500,000 |
|  | Other Assets | 25,800 |
|  | Accounts Payable | (8,200) |
|  | Notes Payable | (10,000) |
|  | Mortgage Payable | (50,000) |
|  | Bonds Payable | (100,000) |
|  | Fair value of net assets acquired | $408,500 |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given (9,000 x $55) | $495,000 |
|  | Fair value of net assets acquired | (408,500) |
|  | Goodwill | $86,500 |

**P1-37 Combined Balance Sheet**

a. Balance sheet:

|  |  |  |  |
| --- | --- | --- | --- |
| Pumpworks and Seaworthy Rope Company  Combined Balance Sheet  January 1, 20X3 | | | |
| Cash and Receivables | $110,000 | Current Liabilities | $     100,000 |
| Inventory | 142,000 | Capital Stock | 214,000 |
| Land | 115,000 | Capital in Excess |  |
| Plant and Equipment | 540,000 | of Par Value | 216,000 |
| Less: Accumulated |  | Retained Earnings | 240,000 |
| Depreciation | (150,000) |  |  |
| Goodwill | 13,000 |  |  |
|  | $770,000 |  | $    770,000 |

Computation of goodwill

|  |  |  |
| --- | --- | --- |
|  | Fair value of consideration given (700 x $300) | $210,000 |
|  | Fair value of net assets acquired ($217,000 – $20,000) | (197,000) |
|  | Goodwill | $13,000 |

|  |  |  |
| --- | --- | --- |
| b. | (1) Stockholders' equity with 1,100 shares issued: |  |
|  |  |  |
|  | Capital Stock [$200,000 + ($20 x 1,100 shares)] | $    222,000 |
|  | Capital in Excess of Par Value [$20,000 + ($300 - $20) x 1,100 shares] | 328,000 |
|  | Retained Earnings | 240,000 |
|  |  | $    790,000 |
|  |  |  |

|  |  |  |
| --- | --- | --- |
|  | (2) Stockholders' equity with 1,800 shares issued: |  |
|  |  |  |
|  | Capital Stock [$200,000 + ($20 x 1,800 shares)] | $ 236,000 |
|  | Capital in Excess of Par Value [$20,000 + ($300 - $20) x 1,800 shares] | 524,000 |
|  | Retained Earnings | 240,000 |
|  |  | $1,000,000 |
|  |  |  |

|  |  |  |
| --- | --- | --- |
|  | (3) Stockholders' equity with 3,000 shares issued: |  |
|  |  |  |
|  | Capital Stock [$200,000 + ($20 x 3,000 shares)] | $ 260,000 |
|  | Capital in Excess of Par Value [$20,000 + ($300 - $20) x 3,000 shares] | 860,000 |
|  | Retained Earnings | 240,000 |
|  |  | $1,360,000 |
|  |  |  |

**P1-38 Incomplete Data Problem**

a. 5,200 = ($126,000 - $100,000)/$5

b. $208,000 = ($126,000 + $247,000) - ($100,000 + $65,000)

c. $46,000 = $96,000 - $50,000

d. $130,000 = ($50,000 + $88,000 + $96,000 + $430,000 - $46,000 -

$220,000 - $6,000) - ($40,000 + $60,000 + $50,000 + $300,000 -

$32,000 - $150,000 - $6,000)

e. $78,000 = $208,000 - $130,000

f. $97,000 (as reported by Plend Corporation)

g. $13,000 = ($430,000 - $300,000)/10 years

**P1-39 Incomplete Data Following Purchase**

a. 14,000 = $70,000/$5

b. $8.00 = ($70,000 + $42,000)/14,000

c. 7,000 = ($117,000 - $96,000)/$3

d. $24,000 = $65,000 + $15,000 - $56,000

e. $364,000 = ($117,000 + $553,000 + $24,000) – ($96,000 + $234,000)

f. $110,000 = $320,000 - $210,000

g. $306,000 = ($15,000 + $30,000 + $110,000 + $293,000) -

($22,000 + $120,000)

h. $58,000 = $364,000 - $306,000

**P1-40 Comprehensive Business Combination Problem**

a. Journal entries on the books of Pintime Industries to record the combination:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Merger Expense | 135,000 |  |
|  | Cash |  | 135,000 |
|  |  |  |  |
|  | Deferred Stock Issue Costs | 42,000 |  |
|  | Cash |  | 42,000 |
|  |  |  |  |
|  | Cash | 28,000 |  |
|  | Accounts Receivable | 251,500 |  |
|  | Inventory | 395,000 |  |
|  | Long-Term Investments | 175,000 |  |
|  | Land | 100,000 |  |
|  | Rolling Stock | 63,000 |  |
|  | Plant and Equipment | 2,500,000 |  |
|  | Patents | 500,000 |  |
|  | Special Licenses | 100,000 |  |
|  | Discount on Equipment Trust Notes | 5,000 |  |
|  | Discount on Debentures | 50,000 |  |
|  | Goodwill | 109,700 |  |
|  | Current Payables |  | 137,200 |
|  | Mortgages Payable |  | 500,000 |
|  | Premium on Mortgages Payable |  | 20,000 |
|  | Equipment Trust Notes |  | 100,000 |
|  | Debentures Payable |  | 1,000,000 |
|  | Common Stock |  | 180,000 |
|  | Additional Paid-In Capital — Common |  | 2,298,000 |
|  | Deferred Stock Issue Costs |  | 42,000 |

Computation of goodwill

|  |  |  |  |
| --- | --- | --- | --- |
|  |  |  |  |
|  | Value of stock issued ($14 x 180,000) |  | $2,520,000 |
|  | Fair value of assets acquired | $4,112,500 |  |
|  | Fair value of liabilities assumed | (1,702,200) |  |
|  | Fair value of net identifiable assets |  | (2,410,300) |
|  | Goodwill |  | $ 109,700 |

**P1-40** (continued)

b. Journal entries on the books of SCC to record the combination:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Investment in Pintime Industries Stock | 2,520,000 |  |
|  | Allowance for Bad Debts | 6,500 |  |
|  | Accumulated Depreciation | 614,000 |  |
|  | Current Payables | 137,200 |  |
|  | Mortgages Payable | 500,000 |  |
|  | Equipment Trust Notes | 100,000 |  |
|  | Debentures Payable | 1,000,000 |  |
|  | Discount on Debentures Payable |  | 40,000 |
|  | Cash |  | 28,000 |
|  | Accounts Receivable |  | 258,000 |
|  | Inventory |  | 381,000 |
|  | Long-Term Investments |  | 150,000 |
|  | Land |  | 55,000 |
|  | Rolling Stock |  | 130,000 |
|  | Plant and Equipment |  | 2,425,000 |
|  | Patents |  | 125,000 |
|  | Special Licenses |  | 95,800 |
|  | Gain on Sale of Assets and Liabilities |  | 1,189,900 |
|  | Record sale of assets and liabilities. |  |  |
|  |  |  |  |
|  | Common Stock | 7,500 |  |
|  | Additional Paid-In Capital — Common Stock | 4,500 |  |
|  | Treasury Stock |  | 12,000 |
|  | Record retirement of Treasury Stock:\* |  |  |
|  | $7,500 = $5 x 1,500 shares |  |  |
|  | $4,500 = $12,000 - $7,500 |  |  |
|  |  |  |  |
|  | Common Stock | 592,500 |  |
|  | Additional Paid-In Capital — Common | 495,500 |  |
|  | Additional Paid-In Capital — Retirement of Preferred | 22,000 |  |
|  | Retained Earnings | 1,410,000 |  |
|  | Investment in Pintime Industries Stock |  | 2,520,000 |
|  | Record retirement of SCC stock and distribution of Integrated Industries stock: |  |  |
|  | $592,500 = $600,000 - $7,500 |  |  |
|  | $495,500 = $500,000 - $4,500 |  |  |
|  | 1,410,000 = $220,100 + $1,189,900 |  |  |
|  |  |  |  |
|  | \*Alternative approaches exist. |  |  |