Intermediate Accounting Volume 2 (Canadian) 13th edition Kieso Test Bank

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CHAPTER 13

NON-FINANCIAL AND CURRENT LIABILITIES

CHAPTER STUDY OBJECTIVES

1. ***Understand the importance of non-financial and current liabilities from a business perspective.*** Cash flow management is a key control factor for most businesses. Taking advantage of supplier discounts for prompt payment is one step companies can take. Control of expenses and related accounts payable can improve the efficiency of a business, and can be particularly important during economic downturns.

2. ***Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.*** Liabilities are defined as an obligation of an entity arising from past transactions or events that are settled through a transfer of economic resources in the future. The entity should have little (or no) ability to avoid the duty or responsibility. Financial liabilities are a subset of liabilities. They are contractual obligations to deliver cash or other financial assets to another party, or to exchange financial assets or liabilities with another party under conditions that are potentially unfavourable. Financial liabilities are initially recognized at fair value, and subsequently either at amortized cost or fair value. ASPE does not specify how non-financial liabilities are measured. However, unearned revenue is generally measured at the fair value of the goods or services to be delivered in the future, while others are measured at the best estimate of the resources needed to settle the obligation. Under IFRS, non-financial liabilities other than unearned revenue are measured at the best estimate of the amount the entity would rationally pay at the date of the SFP to settle the present obligation.

3. ***Define current liabilities and identify and account for common types of current liabilities.*** Current liabilities are obligations that are payable within one year from the date of the SFP or within the operating cycle if the cycle is longer than a year. IFRS also includes liabilities held for trading and any obligation where the entity does not have an unconditional right to defer settlement beyond 12 months after the date of the SFP. There are several types of current liabilities. The most common are accounts and notes payable, and payroll-related obligations.

4. ***Identify and account for the major types of employee-related liabilities.*** Employee-related liabilities include (1) payroll deductions, (2) compensated absences, and (3) profit-sharing and bonus agreements. Payroll deductions are amounts that are withheld from employees and result in an obligation to the government or another party. The employer's matching contributions are also included in this obligation. Compensated absences earned by employees are company obligations that are recognized as employees earn an entitlement to them, as long as they can be reasonably measured. Bonuses based on income are accrued as an expense and liability as the income is earned.

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5. ***Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.*** A decommissioning, restoration, or asset retirement obligation (ARO) is an estimate of the costs a company is obliged to incur when it retires certain assets. It is recorded as a liability and is usually long term in nature. Under ASPE, only legal obligations are recognized. They are measured at the best estimate of the cost to settle them at the date of the SFP, and the associated cost is included as part of the cost of property, plant, and equipment. Under IFRS, both legal and constructive obligations are recognized. They are measured at the amount the entity would rationally pay to be relieved of the obligation, and are capitalized as part of property, plant, and equipment or to inventory, if due to production activities. Over time, the liability is increased for the time value of money and the asset costs are amortized to expense. Entities disclose information about the nature of the obligation and how it is measured, with more disclosures required under IFRS than ASPE.

6. ***Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.*** Historically, an expense approach has been used to account for the outstanding liability, and this type of approach is still used for assurance-type warranties, as initially discussed in Chapter 6. More recently, standards such as IFRS 15 have moved to a revenue approach for warranties that are not included in the sales price of the product (that is, for service-type warranties). Under the expense approach, the outstanding liability is measured at the cost of the economic resources needed to meet the obligation. The assumption is that, along with the liability that is required to be recognized at the reporting date, the associated expense needs to be measured and matched with the revenues of the period. Under the revenue approach, the outstanding liability is measured at the value of the obligation. The proceeds received for any goods or services yet to be delivered or performed are considered to be unearned revenue at the point of sale. Until the revenue is earned, the obligation—the liability—is reported at its sales or fair value. The liability is then reduced as the revenue is earned. More generally, when an entity receives proceeds in advance or for multiple deliverables, unearned revenue is recognized to the extent the entity has not yet performed. This is measured at the fair value of the remaining goods or services that will be delivered. When costs remain to be incurred in revenue transactions where the revenue is considered earned and has been recognized, estimated liabilities and expenses are recognized at the best estimate of the expenditures that will be incurred. This is an application of the matching concept.

7. ***Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.*** Under existing standards, a loss is accrued and a liability recognized if (1) information that is available before the issuance of the financial statements shows that it is likely (or more likely than not under IFRS) that a liability has been incurred at the date of the financial statements, and (2) the loss amount can be reasonably estimated (under IFRS, it would be a rare situation where this could not be done). Some minor changes are under consideration by the IASB as described in the Looking Ahead section of the chapter. Guarantees in general are accounted for similarly to contingencies. Commitments, or contractual obligations, do not usually result in a liability at the date of the SFP. Information about specific types of outstanding commitments is reported at the date of the SFP.

8. ***Indicate how non-financial and current liabilities are presented and analyzed.*** Current liability

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accounts are commonly presented as the first classification in the liability section of the SFP, although under IFRS, an alternative presentation is to present current assets and liabilities at the bottom of the statement. Within the current liability section, the accounts may be listed in order of their maturity or in order of their liquidation preference. IFRS requires information about and reconciliations of any provisions. Additional information is provided so that there is enough to meet the requirement of full disclosure. Information about unrecognized loss contingencies is reported in notes to the financial statements, including their nature and estimates of possible losses. Commitments at year end that are significant in size, risk, or time are disclosed in the notes to the financial statements, with significantly more information required under IFRS. Three common ratios used to analyze liquidity are the current, acid-test, and days payables outstanding ratios.

9. ***Identify differences in accounting between IFRS and ASPE, and what changes are expected in the near future.*** In June 2015, a Staff Paper on the Research—Provisions, Contingent Liabilities and Contingent Assets (IAS 37) project was published. In 2020, as a follow-up, the IASB limited its study to matters such as aligning the definition of a liability and requirements for identifying liabilities in IAS 37 with updates in the *Conceptual Framework for Financial Reporting*, which became effective in 2020. Other goals are to clarify the costs to include in the measure of a provision and to specify whether the rates used by entities to discount provisions should reflect their own credit risk.

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MULTIPLE CHOICE QUESTIONS

Answer	No.	Description
c	1.	Essential characteristics of liabilities
c	2.	Constructive obligation
b	3.	Recognition and accounting for financial liabilities
b	4.	Non-financial liabilities
a	5.	Classification of notes payable
d	6.	Zero-interest-bearing notes
c	7.	Refinancing of long-term debts
b	8.	Identify item that is not a current liability
c	9.	Identify the current liability.
d	10.	Classification of stock dividends distributable
a	11.	Goods and Services Tax
b	12.	Identify current liability
c	13.	Accounting for GST
a	14.	Provincial sales tax
b	15.	Corporation income tax
a	16.	Knowledge of accounts payable
b	17.	Adjusting entry for zero-interest-bearing note
d	18.	Journal entry for payment of interest-bearing note
b	19.	Determine amount of short-term debt to be reported
d	20.	Determine amount of short-term debt to be reported
b	21.	Calculate accounts receivable including sales taxes
c	22.	Calculate cost of purchase for own use
d	23.	Payment of GST
c	24.	Adjusting entry for corporate income tax
d	25.	Determine amount of short-term debt to be reported
c	26.	Calculate accrued interest payable
c	27.	Calculate HST collected
d	28.	Calculate a zero-interest-bearing note
a	29.	Calculate interest on a zero-interest-bearing note
d	30.	Current liabilities in general – determine false statement
c	31.	Determine employer's payroll costs
b	32.	Recording payroll expenses – ASPE
b	33.	Accumulating rights to benefits
c	34.	Accrual of liability for compensated absences
b	35.	Non-accumulating rights to benefits
d	36.	Methods of calculating employee bonuses
b	37.	Calculate payroll tax expense
b	38.	Calculate vacation pay expense to be reported
c	39.	Calculate accrued vacation pay liability
b	40.	Calculate net pay
a	41.	Calculate accrued salaries payable
b	42.	Accrual of payroll taxes
d	43.	Total source deductions owing

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Answer	No.	Description
c	44.	Definition of a provision
d	45.	Recognition of an asset retirement obligation
c	46.	Recognition of an asset retirement obligation
a	47.	Recording accretion expense for ARO
d	48.	Entry for asset retirement obligation
b	49.	Entry for asset retirement obligation accretion
b	50.	Calculate asset retirement obligation
a	51.	Accounting for asset retirement obligations – IFRS
b	52.	Accounting for asset retirement obligations – ASPE
c	53.	Revenue approach for product guarantees
d	54.	Determine false statement regarding warranties
b	55.	Accounting for premiums and coupons
d	56.	IFRS re customer loyalty programs
c	57.	Adjusting entry for unearned revenue
b	58.	Determine current and long-term portions of debt
a	59.	Expense approach to warranty
a	60.	Revenue approach to warranty
c	61.	Calculate warranty liability (expense approach)
a	62.	Calculate liability for unredeemed coupons
b	63.	Calculate unearned service contract revenue
c	64.	Calculate liability from unredeemed trading stamps
b	65.	Service-type warranty liability
a	66.	Account for warranty liability
c	67.	Recognition of contingencies (ASPE)
a	68.	Recognition of contingencies (IFRS)
d	69.	Accrual of contingent liability
c	70.	Disclosure of commitments
d	71.	Determine range of loss accrual
b	72.	Determine amount to accrue as a loss contingency
d	73.	Determine amount to accrue as a gain contingency
d	74.	Determine uncertain liabilities
d	75.	Contingent gains
d	76.	Acid-test ratio elements
c	77.	Days payable outstanding elements
c	78.	Calculate quick (acid-test) ratio
d	79.	Calculate current ratio
c	80.	Calculate quick ratio
a	81.	Calculate days payables outstanding
b	82.	Essential characteristics of liabilities

EXERCISES

Item	Description
E13-85	Non-financial versus financial liabilities
E13-86	Interest-bearing note
E13-87	Zero-interest-bearing note

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E13-88	Notes payable
E13-89	Sales taxes
E13-90	Income taxes payable
E13-91	Payroll entries
E13-92	Compensated absences
E13-93	Compensated absences
E13-94	Asset retirement obligation – ASPE
E13-95	Asset retirement obligation – IFRS
E13-96	Product guarantee and expense approach
E13-97	Product guarantee and cash basis method
E13-98	Premiums
E13-99	Premiums
E13-100	Contingent liabilities

PROBLEMS

Item	Description
P13-101	Common types of current liabilities
P13-102	Accounts and notes payable
P13-103	Presentation of short-term debt
P13-104	Refinancing of short-term debt
P13-105	Payroll deduction entries
P13-106	Employee-related liabilities
P13-107	Asset retirement obligation – IFRS
P13-108	Asset retirement obligation – ASPE
P13-109	Premiums: expense versus revenue approach
P13-110	Premiums: multi-years
P13-111	Warranties
P13-112	Unredeemed coupons
P13-113	Contingencies

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MULTIPLE CHOICE QUESTIONS

1. According to the new Conceptual Framework and under ASPE in the CPA Canada Handbook Part II, which of the following is NOT an essential characteristic of a liability?
a) It embodies a duty or responsibility.
b) The transaction or event that obliges the entity has occurred.
c) The obligation is enforceable on the other party.
d) The entity has little or no discretion to avoid the duty.

Answer: c

Difficulty: Easy
Learning Objective: Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.
Section Reference: Recognition and Measurement
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

2. A constructive obligation arises when
a) the entity is legally obligated to honour the obligation.
b) the entity makes an unconditional promise to pay money in the future.
c) past or present company practice reveals the entity acknowledges a potential economic burden.
d) the entity has a conditional obligation which becomes unconditional if an uncertain future event occurs.

Answer: c

Difficulty: Easy
Learning Objective: Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.
Section Reference: Recognition and Measurement
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

3. Which of the following statements is NOT true about recognition and subsequent accounting for financial liabilities?
a) They are initially recognized at their fair value.
b) After acquisition, they continue to be accounted for at fair value.
c) After acquisition, they are generally accounted for at amortized cost.
d) Short-term liabilities, such as accounts payable, are usually recorded at their maturity value.

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Answer: b

Difficulty: Easy
Learning Objective: Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.
Section Reference: Recognition and Measurement
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

4. Which of the following characteristics of non-financial liabilities is NOT correct?
a) The exact timing of these obligations is generally not known.
b) Non-financial obligations are generally easier to measure.
c) Non-financial obligations are subject to different measurement standards than financial obligations.
d) Non-financial obligations are satisfied with goods and services.

Answer: b

Difficulty: Easy
Learning Objective: Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.
Section Reference: Recognition and Measurement
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

5. Among Oslo Corp.'s short-term obligations, on its most recent statement of financial position date, are notes payable totaling $250,000 with the Provincial Bank. These are 90-day notes, renewable for another 90-day period. These notes should be classified on Oslo's statement of financial position as
a) current liabilities.
b) deferred charges.
c) long-term liabilities.
d) shareholders' equity.

Answer: a

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

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6. Regarding zero-interest-bearing notes,
a) they do not have an interest component.
b) the debtor receives the future value of the note and pays back the present value.
c) any interest is never recognized until the note is repaid.
d) the debtor receives the present value of the note and pays back the future value.

Answer: d

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

7. Under IFRS, even if the entity plans to refinance long-term debt, the current portion must be reported as a current liability UNLESS
a) long-term financing has been completed after the statement of financial position date, but before the financial statements are released.
b) management intends to refinance the debt on a long-term basis.
c) at the statement of financial position date, the entity expects to refinance under an existing agreement for at least a year, and the decision is solely at its discretion.
d) management intends to discharge the debt by issuing shares.

Answer: c

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

8. Which of the following should NOT be included in the current liabilities section of the statement of financial position?
a) trade accounts payable
b) current portion of long-term debt to be retired by non-current assets
c) short-term zero-interest-bearing notes payable
d) a liability due on demand (callable debt)

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Answer: b

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

9. Which of the following is a current liability?
a) preferred dividends in arrears
b) stock dividends distributable
c) preferred cash dividends payable
d) stock splits

Answer: c

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

10. Stock dividends distributable should be classified on the
a) income statement as an expense.
b) statement of financial position as an asset.
c) statement of financial position as a liability.
d) statement of financial position as an item of shareholders' equity.

Answer: d

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
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11. Goods and Services Tax (GST)

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a) is a value added tax.
b) is a sales tax charged by each province on all taxable goods.
c) in some provinces, is an income tax.
d) must be collected by all businesses in Canada.

Answer: a

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

12. Which of the following may be classified as a current liability?
a) stock dividends distributable
b) accounts receivable credit balances
c) losses expected to be incurred within the next 12 months in excess of the company's insurance coverage
d) tenant’s rent deposit not returnable until the end of a long-term lease

Answer: b

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

13. Accounting for GST includes
a) crediting GST Payable to record GST paid on inventory for resale.
b) crediting GST Receivable to record GST collected from customers.
c) debiting GST Receivable to record GST paid to suppliers.
d) debiting GST Payable to record GST collected from customers.

Answer: c

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities

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CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

14. Regarding Provincial Sales Tax (PST),
a) the purchaser includes any PST paid in the cost of the goods or services.
b) all PST paid is recorded in a "PST Expense" account.
c) all PST paid is recorded in a "PST Recoverable" account.
d) for statement of financial position presentation, a PST registrant "nets" any PST paid against any PST collected from customers.

Answer: a

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

15. Corporation income taxes payable
a) must always be approved by an external auditor.
b) are reviewed and approved by Canada Revenue Agency (CRA).
c) also apply to proprietorships and partnerships.
d) are always the same under GAAP and Canadian tax laws.

Answer: b

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

16. Which of the following is generally associated with current liabilities classified as accounts payable?

	Periodic Payment of Interest	**Secured by Collateral**
a)	No	No
b)	No	Yes

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c)	Yes	No
d)	Yes	Yes

Answer: a

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic
Feedback: Accounts payable generally are zero-interest-bearing and unsecured.

17. On November 1, 2023, France Corp. signed a three-month, zero-interest-bearing note for the purchase of $60,000 of inventory. The maturity value of the note was $60,600, based on the bank's discount rate of 4%. The adjusting entry prepared on December 31, 2023 in connection with this note will include a
a) debit to Note Payable for $400.
b) credit to Note Payable for $400.
c) debit to Interest Expense for $600.
d) credit to Interest Expense for $200.

Answer: b

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $60,000 x 4% x 2 ÷ 12 = $400

18. On December 1, 2023, Ruby Ltd. borrowed $180,000 from its bank, by signing a four-month, 5% interest-bearing note. Assuming Ruby has a December 31, year end and does NOT use reversing entries, the journal entry to record payment of this note on April 1, 2024 will include a
a) credit to Note Payable of $180,000.
b) debit to Interest Expense of $3,000.
c) debit to Interest Payable of $2,250.
d) debit to Interest Payable of $750.

Answer: d

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Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: Interest payable that would have been recorded at Dec 31/20
$180,000 x 5% x 1 ÷ 12 = $750.

19. On February 10, 2024, after issuance of its financial statements for calendar 2023, Mantack Corp. entered into a financing agreement with Friedman Bank, allowing Mantack Corp. to borrow up to $4,000,000 at any time through 2025. Amounts borrowed under the agreement bear interest at 3% above the bank's prime interest rate and mature two years from the date of the loan. Mantack presently has $1,500,000 of notes payable with Bringham Bank maturing March 15, 2024. The company intends to borrow $2,500,000 under the agreement with Friedman and pay off the notes payable to Bringham. The agreement with Friedman also requires Mantack to maintain a working capital level of $9,000,000 and prohibits the payment of dividends on common shares without prior approval by Friedman. From the above information only, the total short-term debt of Mantack Corp. on the December 31, 2023 statement of financial position is
a) $0.
b) $1,500,000.
c) $2,500,000.
d) $4,000,000.

Answer: b

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic
Feedback: $1,500,000 (No agreement in place at year end.)

20. On December 31, 2023, Gumble Ltd. has $3,150,000 in short-term notes payable due on February 14, 2024. On January 10, 2024, Gumble arranged a line of credit with Caldi Bank, which allows Gumble to borrow up to $2,000,000 at 2% above the prime rate for three years. On February 2, 2024, Gumble borrowed $1,400,000 from Caldi Bank and used $600,000 additional cash to liquidate $2,000,000 of the short-term notes payable. Assuming Gumble adheres to IFRS, the amount of the short-term notes payable that should be reported as current liabilities on Gumble’s December 31, 2023 statement of financial position (to be issued on March 5, 2024) is
a) $0.

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b) $600,000.
c) $1,400,000.
d) $3,150,000.

Answer: d

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic
Feedback: $3,150,000 (No agreement in place at year end.)

21. Mason Corp. operates in a province with 8% PST. The store must also collect 5% GST on all sales. For the month of May, Mason sold $120,000 worth of goods to customers, 40% of which were cash sales and the balance being on account. Based on the above information, what is the total debit to accounts receivable for the month of May?
a) $72,000
b) $81,360
c) $54,240
d) $35,600

Answer: b

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $120,000 x 60% x 1.13 = $81,360

22. Xylex Ltd., a GST registrant, buys $6,200 worth of Supplies for their own use. The purchase is subject to 6% PST and 5% GST. What amount will be debited to the Supplies account as a result of this transaction?
a) $6,200
b) $6,510
c) $6,572
d) $6,882

Answer: c

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Difficulty: Medium
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Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $6,200 x 1.06 = $6,572

23. At December 31, 2023, Nixel Corp.'s records show the following balances, all of which are normal: PST Payable, $800; GST Payable, $500; GST Receivable, $345. In January 2024, Nixel pays the Federal Government the net amount owing for GST owing from December. The journal entry to record this payment will include a
a) debit to GST Payable of $155.
b) credit to Cash of $500.
c) credit to GST Payable of $500.
d) credit to GST Receivable of $345.

Answer: d

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: to clear GST Receivable account

24. Baxter Ltd. has made a total of $46,500 in instalments for corporate income tax for calendar 2023, all of which have been debited to Current Tax Expense. At year end, Dec. 31, 2023, the accountant has calculated that the corporation's actual tax liability is only $43,000. What is the correct adjusting entry to reflect this fact?
a) Dr. Current Tax Expense $3,500, Cr. Income Taxes Payable $3,500
b) Dr. Income Taxes Payable, $3,500, Cr. Current Tax Expense $3,500
c) Dr. Income Taxes Receivable $3,500, Cr. Current Tax Expense $3,500
d) Dr. Current Tax Expense $43,000, Cr. Income Taxes Payable $43,000

Answer: c

Difficulty: Medium
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Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic
Feedback: $46,500 – $43,000 = $3,500 overpaid = Income Taxes Receivable

25. Included in Harrison Inc.'s account balances at December 31, 2023, were the following:

4% note payable issued October 1, 2023, maturing September 30, 2024	$250,000
6% note payable issued April 1, 2023, payable in six equal annual instalments of $100,000 beginning April 1, 2024	600,000

Harrison's December 31, 2023 financial statements were to be issued on March 31, 2024. On January 15, 2024, the entire $600,000 balance of the 6% note was refinanced by issuance of a long-term note to be repaid in 2027. In addition, on March 10, 2024, Harrison made arrangements to refinance the 4% note on a long-term basis. Under IFRS, on the December 31, 2023 statement of financial position, the amount of the notes payable that Harrison should classify as current liabilities is
a) $0.
b) $100,000.
c) $250,000.
d) $350,000.

Answer: d

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic
Feedback: $250,000 + $100,000 = $350,000

26. On September 1, 2023, Coffee Ltd. issued a $1,800,000, 12% note to Humungous Bank, payable in three equal annual principal payments of $600,000. On this date, the bank's prime rate was 11%. The first payment for interest and principal was made on September 1, 2024. At December 31, 2024, Coffee should record accrued interest payable of
a) $72,000.
b) $66,000.
c) $48,000.
d) $44,000.

Answer: c

Difficulty: Medium

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Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($1,800,000 – $600,000) ×.12 × 4 ÷ 12 = $48,000

27. Jordan Corp. operates in Ontario, selling a variety of goods. For most of these goods, Jordan must charge 13% HST, for some they only have to charge 5% HST; while a very few are tax exempt. During June of this year, the company reported sales of $200,000, on which 70% were charged 13% HST, 25% were charged only 5% HST, and the rest were tax exempt sales. The total amount of HST collected in June was
a) $10,000.
b) $18,200.
c) $20,700.
d) $26,000.

Answer: c

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($200,000 x 13% x 70%) + ($200,000 x 5% x 25%) = $20,700

28. On February 1, Triple H Enterprises issues a $50,000 six-month note payable to MBO bank. It is a zero-interest-bearing note and the bank's discount rate is 4%. Which one of the following entries is required on February 1 by Triple H Enterprises? (Round to the nearest dollar.)
a) Cr. Notes Payable $50,000
b) Dr. Notes Payable $50,000
c) Cr. Notes Payable $48,077
d) Cr. Notes Payable $49,020

Answer: d

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting

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Bloomcode: Application
AACSB: Analytic
Feedback: $50,000 ÷ (1 + (4% x 6/12)) = $49,020

29. On February 1, Triple H Enterprises issues a $50,000 six-month note payable to MBO bank. It is a zero-interest-bearing note and the bank's discount rate is 4%. How much interest expense is recognized upon maturity? (Round to the nearest dollar.)
a) $980
b) $1,000
c) $2,000
d) None, this is a zero-interest bearing note.

Answer: a

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $50,000 ÷ (1 + (4% x 6/12)) = $49,020; $50,000 – $49,020 = $980

30. Which of the following statements is FALSE?
a) Under IFRS, a company may exclude a short-term obligation from current liabilities if, at statement of financial position date, the entity expects to refinance under an existing agreement for at least a year, and the decision is solely at its discretion.
b) Cash dividends should be recorded as a liability when they are declared by the board of directors.
c) Under the cash basis method, warranty costs are charged to expense as they are paid.
d) Federal income taxes withheld from employees' payroll cheques should be recorded as a long-term liability.

Answer: d

Difficulty: Easy
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

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31. Which of the following are included in the employer's Salaries and Wages Expense?
a) employee income tax deducted, employer portion of CPP/QPP and EI
b) employer portion of CPP/QPP and EI, union dues
c) employer portion of CPP/QPP and EI only
d) employer portion of EI, union dues, and employee income tax deducted

Answer: c

Difficulty: Easy
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

32. Under ASPE, payroll taxes such as the employer portion of EI should be recognized as an expense
a) when the amount is remitted to the government.
b) when the related payroll is recorded.
c) when the employee amount is remitted.
d) using whatever policy the company chooses.

Answer: b

Difficulty: Easy
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

33. Accumulating rights to benefits (for employees)
a) are rarely mandated by provincial labour law.
b) include vested rights that do not depend on the employee’s continued service.
c) are rights that do not accrue with employee service.
d) are not accrued as an expense in the period earned.

Answer: b

Difficulty: Easy
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge

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AACSB: Analytic

34. A liability for compensated absences such as vacations, for which it is expected that employees will be paid, should
a) be accrued during the period when the compensated time is expected to be used by employees.
b) be accrued during the period following vesting.
c) be accrued during the period when earned.
d) not be accrued unless a written contractual obligation exists.

Answer: c

Difficulty: Easy
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

35. Non-accumulating rights to benefits, such as parental leave, are generally accounted for by
a) the full accrual method.
b) the event accrual method.
c) the cash method.
d) financial statement note disclosure only.

Answer: b

Difficulty: Easy
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

36. Which of the following is generally NOT used as a basis for calculating bonuses or profit-sharing amounts?
a) a percentage of the employees' regular pay rates
b) the company's pre-tax income
c) productivity increases
d) gross sales

Answer: d

Difficulty: Easy

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Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

37. The total payroll of Carbon Company for the month of October was $240,000, all subject to CPP deductions of 5.45% and EI deductions of 1.58%. As well, $60,000 in federal income taxes and $6,000 of union dues were withheld. The employer matches the CPP employee deductions and contributes 1.4 times the employee EI deductions. What amount should Carbon record as employer payroll tax expense for October?
a) $16,872.00
b) $18,388.80
c) $24,388.80
d) $78,388.80

Answer: b

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($240,000 × 5.45%) + ($240,000 × 1.58% × 1.4) = $18,388.80

Use the following information for questions 38–39.

Silver Ltd. has 35 employees who work 8-hour days and are paid hourly. On January 1, 2023, the company began a program of granting its employees 10 days paid vacation each year. Vacation days earned in 2023 may be taken starting on January 1, 2024. Information relative to these employees is as follows:

Year	Hourly Wages	Vacation Days Earned by Each Employee	Vacation Days Used by Each Employee
2023	$12.90	10	0
2024	13.50	10	8
2025	14.25	10	10

Silver has chosen to accrue the liability for compensated absences (vacation pay) at the current rates of pay in effect when the vacation pay is earned.

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38. What is the amount of vacation pay expense that should be reported on Silver's income statement for 2023?
a) $37,800
b) $36,120
c) $34,440
d) $0

Answer: b

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $12.90 × 8 × 10 × 35 = $36,120

39. What is the amount of the Vacation Wages Payable that should be reported at December 31, 2025?
a) $39,900
b) $45,360
c) $47,460
d) $47,880

Answer: c

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($14.25 × 8 × 10 × 35) + ($13.50 × 8 × 2 × 35) = $47,460

40. Information regarding Oxygen Inc.'s payroll for the period ended March 22 follows:

Gross salaries and wages	$100,000
CPP rate	5.45%
EI rate	1.58%
Employee income tax	deducted $20,000
Company pension deducted	5% of gross salaries and wages
Union dues deducted	$800

Assume 100% of the gross salaries and wages are subject to CPP and EI. Therefore, the NET pay for this period is
a) $73,340.
b) $67,170.

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c) $68,390.
d) $72,220.

Answer: b

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $100,000 – ($100,000 x (.0545 +.0158 +.05)) – $20,000 – $800 = $67,170

41. Dixon Company's salaried employees are paid biweekly. Information relating to salaries for the calendar year 2023 is as follows:

Accrued salaries payable Jan. 1, 2023	$182,000
Salaries expense for 2023.....	1,820,000
Salaries paid during 2023 (gross).....	1,750,000

At December 31, 2023, what amount should Dixon report for accrued salaries payable?
a) $252,000
b) $240,000
c) $182,000
d) $70,000

Answer: a

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $1,820,000 + $182,000 – $1,750,000 = $252,000

42. Willow Corp.'s payroll for the period ended October 31, 2023 is summarized as follows:

Department Payroll	Total Wages	Income Tax Withheld	Amount of Wages Subject to Payroll Taxes	
			CPP/QPP	EI
Factory	$ 75,000	$10,000	$66,000	$22,000
Sales	22,000	3,000	16,000	2,000
Office	18,000	2,000	8,000	—
	$115,000	$15,000	$90,000	$24,000

Assume the following payroll tax rates:

CPP/QPP for employer and employee	5.45% each

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Employment Insurance	1.58% for employee 1.4 times employee premium for employer

What amount should Willow accrue as its share of payroll taxes in its October 31, 2023 statement of financial position? (Round to 2 decimal places.)
a) $4,853.40
b) $5,435.88
c) $5,284.20
d) $20,435.88

Answer: b

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($90,000 ×.0545) + ($24,000 ×.0158 × 1.4) = $5,435.88

43. Elm Corp.'s payroll for the period ended July 31, 2023 is summarized as follows:

Department Payroll	Total Wages	Income Tax Withheld	Amount of Wages Subject to Payroll Taxes	
			CPP/QPP	EI
Factory	$ 75,000	$10,000	$66,000	$22,000
Sales	22,000	3,000	16,000	2,000
Office	18,000	2,000	8,000	—
	$115,000	$15,000	$90,000	$24,000

Assume the following payroll tax rates:

CPP/QPP for employer and employee	5.45% each
Employment Insurance	1.58% for employee 1.4 times employee premium for employer

What is the total amount Elm must remit to the government for payroll? (Round to 2 decimal places.)
a) $15,000.00
b) $5,435.88
c) $10,720.08
d) $25,720.08

Answer: d

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

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Feedback: ($90,000 ×.0545) + ($24,000 ×.0158 × 1.4) +($90,000 ×.0545) + ($24,000 ×.0158) + $15,000 = $25,720.08

44. Under IFRS, a provision is
a) a special fund set aside to pay long-term debt.
b) unearned revenue.
c) a liability of uncertain timing or amount.
d) an allowance for future dividends to be paid.

Answer: c

Difficulty: Easy
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

45. At the time of recognition of an asset retirement obligation, the present value should be
a) recorded as a separate long-term asset and as an asset retirement obligation.
b) expensed and recorded as an asset retirement obligation.
c) expensed to “Asset Retirement Expense” in the period actually paid.
d) added to the related asset cost and recorded as an asset retirement obligation.

Answer: d

Difficulty: Easy
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

46. Under ASPE, an asset retirement obligation should be recognized when
a) an asset is impaired and is available for sale.
b) operation of an asset has resulted in an additional obligation such as the cost of cleaning up an oil spill.
c) there is a legal obligation to restore the site of the asset at the end of its useful life.
d) the company has an obligation to purchase a long-lived asset.

Answer: c

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Difficulty: Easy
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

47. Which of the following statements is INCORRECT regarding the recording of the related increase or accretion in the carrying amount of an asset retirement obligation (ARO)?
a) Under ASPE, it is recognized as interest expense.
b) Under ASPE, it is recognized as an operating expense (but not as interest expense).
c) Under IFRS, it is recognized as a borrowing cost.
d) The amount should be calculated using the same discount (interest rate) as was used to calculate the initial present value of the ARO.

Answer: a

Difficulty: Easy
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

Use the following information for questions 48–49.

Antimony Inc., a private company following ASPE, developed a new gold mine during 2023, and is required by provincial law to restore the site to its previous condition once mining operations are completed. The company estimates that the mine will close in 20 years and that the land restoration will cost $5,000,000. Antimony uses a 6% discount rate.

48. To the nearest dollar, the entry to record the asset retirement obligation is

a) Restoration Expense	93,541	
Asset Retirement Obligation		93,541
b) Restoration Expense	250,000	
Asset Retirement Obligation		250,000
c) Gold Mine	5,000,000	
Asset Retirement Obligation		5,000,000
d) Gold Mine	1,559,024	
Asset Retirement Obligation		1,559,024

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Answer: d

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: 20 N 6 I 5000000 FV CPT PV => $1,559,024

49. To the nearest dollar, the adjusting entry to record accretion at the end of Year One is

a) Accretion Expense	250,000	
Asset Retirement Obligation		250,000
b) Accretion Expense	93,541	
Asset Retirement Obligation		93,541
c) Gold Mine	93,541	
Asset Retirement Obligation		93,541
d) Interest Expense	93,541	
Asset Retirement Obligation		93,541

Answer: b

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $1,559,024 x 6% = $93,541

50. On April 30, 2023, Canuck Oil Corp. purchased an oil tanker depot for $1,200,000 cash. The company expects to operate this depot for eight years, at which time they will be legally required to dismantle the structure and remove the underground storage tanks. Canuck Oil estimates this asset retirement obligation (ARO) will cost $200,000. Assuming a 5% discount rate, to the nearest dollar, the amount to be recorded as the ARO is
a) $25,000.
b) $135,368.
c) $150,000.
d) $295,491.

Answer: b

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Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: 8 N 5 I/Y 200000 FV CPT PV => $135,368

51. On January 1, Thermal Power Incorporated builds a nuclear plant 50 miles outside of Timmins, Ontario that it is legally required to dismantle and remove at the end of its 40-year useful life. The total cost of dismantling and removing the plant is estimated at $650,000,000. The discount rate is 12%. Which of the following entries would be used to record the interest liability relating to the asset retirement obligation at the end of year one using IFRS? (Round to the nearest whole number.)
a) Dr. Interest Expense $838,250
b) Dr. Accretion Expense $838,250
c) Dr. Asset Retirement Obligation $838,250
d) Dr. Interest Expense $1,950,000

Answer: a

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: 40 N 12 I/Y 650,000,000 FV CPT PV => $6,985,419; $6,985,419 x 12% = $838,250

52. On January 1, Thermal Power Incorporated builds a nuclear plant 50 miles outside of Timmins, Ontario that it is legally required to dismantle and remove at the end of its 40-year useful life. The total cost of dismantling and removing the plant is estimated at $650,000,000. The discount rate is 12%. Which of the following entries would be used to record the interest liability relating to the asset retirement obligation at the end of year one using ASPE? (Round to the nearest whole number.)
a) Dr. Interest expense $838,250
b) Dr. Accretion Expense $838,250
c) Dr. Asset Retirement Obligation $838,250
d) Dr. Interest Expense $1,950,000

Answer: b

Difficulty: Medium

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Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: 40 N 12 I/Y 650000000 FV CPT PV => $6,985,419; $6,985,419 x 12% = $838,250

53. Using the revenue approach of accounting for product guarantees and warranty obligations,
a) the liability is measured at the estimated cost of meeting the obligation.
b) there is no effect on future income.
c) the liability is measured at the value of the services to be provided.
d) the liability is measured at the value of the services to be provided, but there is no effect on future income.

Answer: c

Difficulty: Easy
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

54. Which of the following statements is INCORRECT concerning warranties?
a) Using the expense approach, the warranty is provided with the product or service with no additional fee.
b) Where warranty costs are immaterial or when the warranty period is quite short, the warranty costs may be accounted for using the cash basis.
c) Using the revenue approach, the warranty is a separate deliverable from the related product or service.
d) The revenue approach must be used for income tax purposes.

Answer: d

Difficulty: Easy
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

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55. The current (commonly used) accounting treatment for premiums and coupons requires that the costs should
a) be recorded at the maximum possible redemption cost in the year of the related sales.
b) be recorded at the total estimated redemption cost in the year of the related sales.
c) be recorded in the year(s) that the redemption is expected to occur.
d) not be recorded at all.

Answer: b

Difficulty: Easy
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

56. What are the current International Financial Reporting Standards regarding how customer loyalty programs (such as frequent flyer points) should be accounted for?
a) They are recognized only in the financial statement notes.
b) They are recognized only when customers redeem their points.
c) They are not explicitly addressed.
d) The current proceeds are to be split between the original transaction and the award credits (as unearned revenue).

Answer: d

Difficulty: Easy
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

57. On Dec. 12, 2023, Ivory Coast Accountants received $5,000 from a customer as an advance payment for accounting work to be done. The payment was credited to Service Revenue. Thirty percent of the work was performed in December 2023, with the rest to be done in January 2024, at which time the customer will be billed. The required adjusting entry at December 31, 2023 (year end) is
a) Dr. Unearned Revenue $1,500, Cr. Service Revenue $1,500.
b) Dr. Service Revenue $1,500, Cr. Unearned Revenue $1,500.
c) Dr. Service Revenue $3,500, Cr. Unearned Revenue $3,500.

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d) Dr. Unearned Revenue $3,500, Cr. Service Revenue $3,500.

Answer: c

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Analysis
Feedback: Remove 70% of revenue and transfer to liability.
AACSB: Analytic

58. On January 1, 2023, Wick Ltd., a private company following ASPE, leased a building to Candle Corp. for a ten-year term at an annual rental of $90,000. At the inception of the lease, Wick received $360,000 covering the first two years rent of $180,000 and a security deposit of $180,000. This deposit will NOT be returned to Candle upon expiration of the lease but will be applied to payment of rent for the last two years of the lease. What portion of the $360,000 should be shown as a current and long-term liability, respectively, in Wick's December 31, 2023 statement of financial position?

	Current Liability	**Long-term Liability**
a)	$0	$360,000
b)	$90,000	$180,000
c)	$180,000	$180,000
d)	$180,000	$90,000

Answer: b

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $90,000 (50% to be earned in 2024) and $180,000 (security deposit)

59. Platinum Corp. uses the expense approach to account for warranties. They sell a used car for $30,000 on Oct. 25, 2023, with a one-year warranty covering parts and labour. Warranty expense is estimated at 2% of the selling price, and the appropriate adjusting entry is recorded at Dec. 31, 2023. On March 12, 2024, the car is returned for warranty repairs. This cost Platinum $200 in parts and $120 in labour. When recording the March 12, 2024 transaction, Platinum would debit Warranty Expense with
a) zero.
b) $120.

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c) $200.
d) $320.

Answer: a

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: Debit is to the liability account, not the expense account.

60. Robertson Corp. uses the revenue approach to account for warranties. During 2023, the company sold $750,000 worth of products, all of which carried a two-year warranty (included in the price). It was estimated that 2% of the selling price represented the warranty portion, and that 40% of this related to 2023, and 60% to 2024. Assuming that Robertson incurred costs of $5.500 to service the warranties in 2024, what is the net warranty revenue (revenue minus warranty costs) for 2024?
a) $3,500
b) $9,500
c) $5,500
d) $9,000

Answer: a

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $750,000 x 2% x 60% = $9,000; $9,000 – $5,500 costs = $3,500

61. In 2023, Hydrogen Corp. began selling a new line of products that carry a two-year warranty against defects. Based upon past experience with other products, the estimated warranty costs related to dollar sales are as follows:

First year of warranty	2%
Second year of warranty	5%

Sales and actual warranty expenditures for 2023 and 2024 are presented below:

	2023	**2024**
Sales	$450,000	$600,000
Actual warranty expenditures	15,000	30,000

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Hydrogen uses the expense approach to account for warranties. What is the estimated warranty liability at the end of 2024?
a) $73,500
b) $43,500
c) $28,500
d) $12,000

Answer: c

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: [($450,000 + $600,000) ×.07] – $15,000 – $30,000 = $28,500

62. Krypton Foods distributes coupons to consumers that may be presented, on or before a stated expiry date, to grocery stores for discounts on certain Krypton products. The stores are reimbursed when they send the coupons in to Krypton. In Krypton's experience, only about 50% of these coupons are redeemed. During 2023, Krypton issued two separate series of coupons as follows:

Issued On	Total Value	Coupon Expiry Date	Amounts Reimbursed as of Dec 31/23
Jan 1/23	$250,000	June 30/23	$118,000
Jul 1/23	360,000	Dec. 31/23	150,000

Krypton's only journal entries for 2023 recorded debits to Premium Expense, and credits to Cash of $268,000. Their December 31, 2023 statement of financial position should include an Estimated Liability for Premiums of
a) $0.
b) $30,000.
c) $62,000.
d)$180,000.

Answer: a

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: All coupons have expired by Dec 31/23.

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63. Woodwards Store sells major household appliance service contracts for cash. The service contracts are for a one-year, two-year, or three-year period. Cash receipts from contracts are credited to Unearned Revenue. This account had a balance of $600,000 at December 31, 2022 before year-end adjustment. Service contract costs are charged as incurred to the service contract expense account, which had a balance of $150,000 at December 31, 2022. Outstanding service contracts at December 31, 2022 expire as follows:

During 2023	During 2024	During 2025
$125,000	$200,000	$90,000

What amount should be reported as Unearned Revenue in Woodwards' December 31, 2022 statement of financial position?
a) $450,000
b) $415,000
c) $300,000
d) $275,000

Answer: b

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $125,000 + $200,000 + $90,000 = $415,000

64. Jackpine Trading Stamp Co. records trading stamp revenue and provides for the cost of redemptions in the year stamps are sold. Jackpine's past experience indicates that only 75% of the stamps sold will be redeemed. Jackpine's liability for stamp redemptions was $3,000,000 at December 31, 2022. Additional information for 2023 is as follows:

Stamp revenue from stamps sold to licensees	$2,000,000
Cost of redemptions for stamps sold prior to 2023.....	1,350,000

If all the stamps sold in 2023 were presented for redemption in 2023, the redemption cost would be $1,000,000. What amount should Jackpine report as a liability for stamp redemptions at December 31, 2023?
a) $3,750,000
b) $2,650,000
c) $2,400,000
d) $1,650,000

Answer: c

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program

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obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $3,000,000 + ($2,000,000 × 75%) – $1,350,000 – ($1,000,000 x 75%) = $2,400,000

65. Appliances R US sells high-end programmable convection ovens for $2,500. The selling price includes a $300 two-year warranty package that provides for repairs and maintenance. In 2023, Appliances R Us sold 100 ovens and incurred $11,250 in servicing costs. Which of the following entries is required, assuming the revenue is earned evenly over the two-year term, to account for the remeasurement of unearned revenues at the end of 2023?
a) Dr. Warranty Expense $15,000
b) Dr. Unearned Revenue $15,000
c) Dr. Materials, Cash, Payables $11,250
d) Dr. Warranty Revenue $11,250

Answer: b

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $300 x 100 x 1/2 = $15,000

66. Appliances R US sells high-end programmable convection ovens for $2,500. The selling price includes a $300 two-year warranty package that provides for repairs and maintenance. In 2023, Appliances R Us sold 100 ovens and incurred $11,250 in servicing costs. Which of the following entries is required to account for the servicing costs at the end of 2023?
a) Dr. Warranty Expense $11,250
b) Dr. Unearned Revenue $15,000
c) Dr. Materials, Cash, Payables $11,250
d) Dr. Warranty Revenue $11,250

Answer: a

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting

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Bloomcode: Application
AACSB: Analytic

67. Under ASPE, a contingent liability is recognized if
a) it is certain that funds are available to settle the contingency.
b) an asset may have been impaired.
c) the amount of the loss can be reasonably estimated and it is likely that an asset has been impaired or a liability incurred as of the financial statement date.
d) it is likely that an asset has been impaired or a liability incurred even though the amount of the loss cannot be reasonably estimated.

Answer: c

Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

68. Under current IFRS requirements, a provision is recognized if
a) the amount of the loss can be reliably measured, and it is probable that an asset has been impaired or a liability incurred as of the financial statement date.
b) the amount of the loss cannot be measured reliably but it is probable that an asset has been impaired, or a liability incurred as of the financial statement date.
c) it relates to a lawsuit commenced after the statement of financial position date, the outcome of which can be reliably measured.
d) it relates to an asset recognized as impaired after the statement of financial position date.

Answer: a

Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

69. Which of the following may NOT be accrued as a contingent liability?

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a) threat of expropriation of assets
b) pending or threatened litigation
c) guarantees of indebtedness of others
d) potential income tax refunds

Answer: d

Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

70. Which of the following commitments would NOT require disclosure in the financial statement notes?
a) major property, plant, and equipment expenditures
b) payments under non-cancellable operating leases
c) large purchases of materials in the normal course of business
d) commitments involving significant risk

Answer: c

Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

71. Harriet Ltd. has a likely loss that can only be reasonably estimated within a range of outcomes. No single amount within the range is a better estimate than any other amount. Under ASPE, the loss accrual should be
a) zero.
b) the maximum of the range.
c) the mean of the range.
d) the minimum of the range.

Answer: d

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Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

72. Asbestos Corp. is being sued for illness caused to local residents as a result of negligence on the company's part in permitting the local residents to be exposed to highly toxic chemicals. Asbestos's lawyer states that it is likely the corporation will lose the suit and be found liable for a judgement which may cost Asbestos anywhere from $300,000 to $1,500,000. However, the lawyer states that the most likely cost is $900,000. As a result of the above facts, using ASPE, Asbestos should accrue
a) a loss contingency of $300,000 and disclose an additional contingency of up to $1,200,000.
b) a loss contingency of $900,000 and disclose an additional contingency of up to $600,000.
c) a loss contingency of $900,000 but not disclose any additional contingency.
d) no loss contingency but disclose a contingency of $300,000 to $1,500,000.

Answer: b

Difficulty: Medium
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic
Feedback: $900,000 and $600,000

73. At January 1, 2023, Neon Corp. owned a machine that had cost $100,000. The accumulated depreciation to date was $60,000, estimated residual value was $6,000, and fair value was $160,000. On January 4, 2023, this machine suffered major damage due to Argon Corp.’s actions and was written off as worthless. In October 2023, a court awarded damages of $160,000 against Argon in favour of Neon. At December 31, 2023, the final outcome of this case was awaiting appeal and was, therefore, uncertain. However, in the opinion of Neon's attorney, Argon's appeal will be denied. At December 31, 2023, what amount should Neon accrue for this gain contingency?
a) $160,000
b) $130,000
c) $100,000
d) $0

Answer: d

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Difficulty: Medium
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $0; Gain contingencies are not accrued.

74. When a company is threatened with litigation, which of the following factors needs to be considered in determining whether a liability should be recorded under IFRS?
a) the time period in which the cause of action occurred
b) the likelihood of an unfavourable outcome
c) the ability to make a reasonable estimate of the loss
d) All these factors must be considered.

Answer: d

Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

75. Under IFRS, a contingent gain will be recorded in the financial statements when
a) it is deemed likely to occur and the amount can be reasonably estimated.
b) it is deemed likely to occur.
c) the amount can be reasonably estimated.
d) a recovery has been made.

Answer: d

Difficulty: Easy
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Knowledge

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AACSB: Analytic

76. The numerator of the acid-test ratio consists of
a) total current assets.
b) cash and marketable securities.
c) cash and net receivables.
d) cash, marketable securities, and net receivables.

Answer: d

Difficulty: Easy
Learning Objective: Indicate how non-financial and current liabilities are presented and analyzed.
Section Reference: Presentation, Disclosure, and Analysis
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

77. The denominator of the days payable outstanding ratio can be
a) average daily sales.
b) average trade accounts payable.
c) average daily cost of goods sold.
d) average trade accounts receivable.

Answer: c

Difficulty: Easy
Learning Objective: Indicate how non-financial and current liabilities are presented and analyzed.
Section Reference: Presentation, Disclosure, and Analytics
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

78. Presented below is information available for Radon Corp.:

Current Assets	
Cash	$ 8,000
Marketable securities	150,000
Accounts receivable	122,000
Inventories	220,000
Prepaid expenses	60,000
Total current assets	$560,000

Total current liabilities are $100,000. Radon's acid-test ratio is
a) 5.60.
b) 5.30.

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c) 2.80.
d) .36.

Answer: c

Difficulty: Medium
Learning Objective: Indicate how non-financial and current liabilities are presented and analyzed.
Section Reference: Presentation, Disclosure, and Analytics
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($8,000 + $150,000 + $122,000) / $100,000 = 2.80

79. Lee Kim Inc.'s most recent statement of financial position includes

Cash	$7,500
Accounts receivable	10,000
Inventory	13,300
Plant and equipment (net)	73,700
Accounts payable	14,000
Long-term bonds payable	50,000
Common shares	20,000
Retained earnings	20,500

Lee Kim Inc. has a current ratio of
a) .27.
b) .48.
c) 1.63.
d) 2.20.

Answer: d

Difficulty: Medium
Learning Objective: Indicate how non-financial and current liabilities are presented and analyzed.
Section Reference: Presentation, Disclosure, and Analytics
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $\frac{\$7,500 + \$10,000 + \$13,300}{\$14,000} = 2.20$

80. Lee Kim Inc.'s most recent statement of financial position includes

Cash	$7,500
Accounts receivable	10,000
Inventory	13,300
Plant and equipment (net)	73,700

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Long-term bonds payable.....	50,000
Common shares.....	20,000
Retained earnings.....	20,500

Lee Kim Inc. has a quick ratio of 1.25. What is the value of the current liabilities?
a) $83,600
b) $24,640
c) $14,000
d) $8,000

Answer: c

Difficulty: Medium
Learning Objective: Indicate how non-financial and current liabilities are presented and analyzed.
Section Reference: Presentation, Disclosure, and Analytics
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: ($7,500 + $10,000) / x = 1.25; x = $17,500 / 1.25 = $14,000

81. Helium Corp. provides the following information for 2023 and 2024:

	2023	**2024**
Current assets.....	$23,000	$27,000
Accounts payable	9,000	10,000
Other current liabilities	5,000	4,000
Non-current liabilities	50,000	62,000
Sales revenue.....	125,000	135,000
Cost of goods sold	75,000	79,600

Helium's days payables outstanding for 2024 is
a) 43.6 days.
b) 46.2 days.
c) 47.2 days.
d) 48.7 days.

Answer: a

Difficulty: Medium
Learning Objective: Indicate how non-financial and current liabilities are presented and analyzed.
Section Reference: Presentation, Disclosure, and Analytics
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic
Feedback: $\frac{(\$10,000 + \$9,000) \div 2}{\$79,600 \div 365}$ = 43.6 days

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82. According to the Conceptual Framework, which of the following is NOT an essential characteristic of a liability?
a) It exists in the present time.
b) There is certainty about the amount of future outflows.
c) The obligation is enforceable on the obligor entity.
d) It represents an economic burden or obligation.

Answer: b

Difficulty: Easy
Learning Objective: Identify differences in accounting between IFRS and ASPE and what changes are expected in the near future.
Section Reference: IFRS/ASPE Comparison
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

83. Under ASPE, a contingent gain is recognized if
a) it is certain that funds will be received when the contingency is settled.
d) There are no circumstances where a contingency gain is recognized.
c) the amount of the gain can be reasonably estimated and it is likely that the gain will be realized.
b) it is likely that the gain has been realized even though the amount of the gain cannot be reasonably estimated.

Answer: d

Difficulty: Medium
Learning Objective: Identify differences in accounting between IFRS and ASPE, and what changes are expected in the near future.
Section Reference: IFRS/ASPE Comparison.
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Analytic

84. Under IFRS, the potential reimbursement from a contingent gain is recognized when
a) there is virtual certainly of recovery.
d) There are no circumstances where a contingency gain is recognized.
c) the amount of the gain can be reasonably estimated and it is likely that the gain will be realized.
b) it is likely that the gain has been realized even though the amount of the gain cannot be reasonably estimated.

Answer: a

Difficulty: Medium
Learning Objective: Identify differences in accounting between IFRS and ASPE, and what changes are expected in the near future.

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Section Reference: IFRS/ASPE Comparison.
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EXERCISES

Ex. 13-85 Non-financial versus financial liabilities
Why are non-financial liabilities more difficult to measure than financial liabilities?

Solution 13-85
Non-financial **liabilities** are more difficult to measure than financial liabilities because the obligations will be met with goods and services (that is, non-financial resources), and the timing of meeting the obligation and its amount are not fixed.

Difficulty: Easy
Learning Objective: Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.
Section Reference: Recognition and Measurement
CPA: Communication
CPA: Financial Reporting
Bloomcode: Comprehension
AACSB: Communication

Ex. 13-86 Interest-bearing note
Hanson Bank agrees to lend $250,000 to Mishin Corp. on May 1, 2023 and the company signs a $250,000, three-month, 6% note maturing on August 1, 2023.

Instructions
Prepare the journal entry to record the cash received by Mishin Corp. on May 1, the entry to record interest expense at Mishin's year-end of July 31 and the entry at maturity of the note.

Solution 13-86

May	1	Cash	250,000	
		Notes Payable		250,000
July	31	Interest Expense	3,750	
		Interest Payable		3,750
		($250,000 × 6% × 3/12 = $3,750)		
Aug	1	Notes Payable	250,000	
		Interest Payable	3,750	
		Cash		253,750

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting

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Bloomcode: Application
AACSB: Analytic

Ex. 13-87 Zero-interest-bearing note
Mishin Corp. issues a $250,000, three-month zero-interest-bearing note payable to Hanson Bank on May 1, 2023. The note has a present value of $246,305 based on the bank's discount rate of 6%.

Instructions
Prepare the journal entry to record the cash received by Mishin on May 1, the entry to record interest expense at the company's July 31 year-end and the entry at maturity of the note.

Solution 13-87

May	1	Cash	246,305	
		Notes Payable		246,305
July	31	Interest Expense	3,695	
		Notes Payable		3,695
		($246,305 × 6% × 3/12 = $3,695)		
Aug	1	Notes Payable	250,000	
		Cash		250,000

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex. 13-88 Notes payable
On August 31, 2023, Kamloops Corp. paid the Regal Bank part of an outstanding $300,000 long-term 10% note payable obtained one year earlier (August 31, 2022), by paying $180,000 plus $18,000 interest. In order to do this, Kamloops used $51,211 cash and signed a new one-year, zero-interest-bearing $160,000 note discounted at 9% by Regal (i.e. the bank issued a note at a discount designed to provide a 9% return over the one year period).

Instructions
a) Prepare the entry to record the refinancing.
b) Prepare the adjusting entry at December 31, 2023 in connection with the new zero-interest-bearing note.

Solution 13-88

a)		Notes Payable	180,000	

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	Interest Expense	18,000	
	Notes Payable ($160,000/1.09)		146,789
	Cash		51,211
b)	Interest Expense ($146,789 x 9% x 4 ÷ 12)	4,403.67	
	Notes Payable		4,403.67

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex.13-89 Sales taxes
For the month of November, Parry Sound Sales Ltd. recorded $280,000 in sales, 40% of which were on account (terms N30), and 60% of which were cash sales. The company is required to charge 6% PST and 5% GST on all sales.

Instructions
Prepare one journal entry to record the company's sales for November.

Solution 13-89

Accounts Receivable ($280,000 x 1.11 x 40%)	124,320	
Cash ($280,000 x 1.11 x 60%)	186,480	
Sales Revenue		280,000
GST Payable ($280,000 x 5%)		14,000
PST Payable ($280,000 x 6%)		16,800

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex. 13-90 Income taxes payable
Avalanche Ltd. operates a profitable business in a relatively stable market. Management estimates that monthly profit subject to taxes is $25,000. In order to ensure that the financial statements reflect all current obligations, management estimates the amount of taxes payable each month and makes the appropriate journal entries to the ledger. The company is subject to a 15% effective tax rate.

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Instructions

a) What is the monthly journal entry?

b) At the end of the 12 months, Avalanche completes its tax return and owes the tax authority $48,000 for the year. What is the adjusting journal entry?

Solution 13-90

a)	Income Tax Expense	3,750	
	Income Tax Payable		3,750
b)	Income Tax Expense ($48,000 – (12 x $3,750))	3,000	
	Income Tax Payable	45,000	
	Cash		48,000

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex. 13-91 Payroll entries

The total payroll of Lyndon Inc. was $230,000. Income taxes withheld were $55,000. The EI rate is 1.58% for the employee and 1.4 times the employee premium for the employer. The CPP contributions are 5.45% for both the employee and employer.

Instructions (Round all values to the nearest dollar, if necessary.)

a) Prepare the journal entry for the salaries and wages paid.

b) Prepare the entry to record the employer payroll taxes.

Solution 13-91

a)	Salaries and Wages Expense	230,000	
	Employee Income Tax Deductions Payable		55,000
	EI Premiums Payable ($230,000 x 1.58%)		3,634
	CPP Contributions Payable ($230,000 x 5.45%)		12,535
	Cash		158,831
b)	Payroll Tax Expense	17,623	
	EI Premiums Payable ($3,634 × 1.4)		5,088
	CPP Contributions Payable		12,535

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting

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Bloomcode: Application
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Ex. 13-92 Compensated absences
Sycamore Ltd. began operations on January 2, 2023. The company employs 15 people who work 8-hour days. Each employee earns 10 paid vacation days annually. Vacation days may be taken after January 10 of the year following the year in which they are earned. The average hourly wage rate was $12.00 in 2023 and $12.75 in 2024. The average number of vacation days used by each employee in 2024 was 9. Sycamore accrues the cost of compensated absences at rates of pay in effect when earned.

Instructions
Prepare journal entries to record the transactions related to paid vacation days during 2023 and 2024.

Solution 13-92

2023		
Salaries and Wages Expense	14,400[1]	
Vacation Wages Payable		14,400

[1] 15 × 8 × $12.00 × 10 = $14,400

2024		
Salaries and Wages Expense	810	
Vacation Wages Payable	12,960[2]	
Cash		13,770[3]
Salaries and Wages Expense	15,300[4]	
Vacation Wages Payable		15,300

[2] $14,400 ÷ 10 × 9 = $12,960
[3] 15 × 8 × $12.75 × 9 = $13,770
[4] $15 × 8 x $12.75 x 10 = $15,300

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex.13-93 Compensated absences
HangTen Corp. prides itself on offering competitive compensation packages to its employees. Each employee is entitled to 40% of their wages for a period of 15 weeks upon being granted maternity / paternity leave. Ron Baker told his manager on May 1st that on Aug 1st he would like to take 15 weeks

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of paternity leave to be with his newborn child. Ron earns $65,000 a year in salary. Ron's manager has approved his request.

Instructions

a) What is the journal entry to record this compensated absence?

b) Are there any subsequent entries as a result of this transaction?

Solution 13-93

a)	Employee Benefit Expense	$7,500	
	Parental Leave Benefits Payable		$7,500

b) As Ron is paid by the company while he is away, the payable will be reduced by the cash paid to Ron according to his pay schedule.

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex.13-94 Asset retirement obligation – ASPE

Tin Mines International Ltd. discovered a new iron ore deposit, the Grouse Mine, and began production on January 1, 2023. The province requires mining companies to return the land to its natural state at the end of mining activity. Tin Mines International estimates that it will operate the mine for 25 years, at which time it will cost $25,000,000 for the land restoration project. Tin Mines International uses an 8% discount rate, and follows ASPE.

Instructions

a) Record any obligation for land restoration at January 1, 2023.

b) Record any entry required related to this obligation at December 31, 2023.

Solution 13-94

a)

<u>January 1, 2023</u>			
	Mineral Resources	3,650,448	
	Asset Retirement Obligation		3,650,448

25 N 8 I 25000000 FV CPT PV => $3,650,448

b)

<u>December 31, 2023</u>			
	Accretion Expense	292,036	
	Asset Retirement Obligation		292,036

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$3,650,448 x 8% = $292,036

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex.13-95 Asset retirement obligation – IFRS
Nickel Mines Global Inc. discovered a new nickel ore deposit, the Flush Mine, and began production on January 1, 2023. The province requires mining companies to return the land to its natural state at the end of mining activity. Nickel Mines Global estimates that it will operate the mine for 25 years, at which time it will cost $25,000,000 for the land restoration project. Nickel Mines Global uses an 8% discount rate and follows IFRS.

Instructions

a) Record any obligation for land restoration at January 1, 2023.
b) Record any entry required related to this obligation at December 31, 2023.

Solution 13-95

a)

January 1, 2023		
Mineral Resources	3,650,448	
Asset Retirement Obligation		3,650,448

25 N 8 I 25000000 FV CPT PV => $3,650,448

b)

December 31, 2023		
Interest Expense	292,036	
Asset Retirement Obligation		292,036

$3,650,448 x 8% = $292,036

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

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Ex.13-96 Product guarantee and expense approach
Chapelle Appliances sells dishwashers for $1,200 each, which includes a 2-year warranty that requires the company to perform periodic services and to replace defective parts. During 2023, Chapelle sold 600 dishwashers on account. Based on past experience, the company has estimated the total 2-year warranty costs at $40 for parts and $75 for labour. (Assume sales all occur at December 31, 2023.)
In 2024, Chapelle Company incurred actual warranty costs relative to 2023 dishwasher sales of $4,000 for parts and $7,500 for labour.

Instructions
Using the expense warranty approach, prepare the entries to reflect the above transactions (accrual method) for 2023 and 2024.

Solution 13-96

2023		
Accounts Receivable	720,000	
Sales Revenue (600 x $1,200)		720,000
Warranty Expense (600 x ($40 + $75))	69,000	
Warranty Liability		69,000
2024		
Warranty Liability	11,500	
Inventory		4,000
Salaries and Wages Payable		7,500

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex.13-97 Product guarantee and expense approach
Chapelle Appliances sells dishwashers for $1,200 each, which includes a 2-year warranty that requires the company to perform periodic services and to replace defective parts. During 2023, Chapelle sold 600 dishwashers on account. Based on past experience, the company has estimated the total 2-year warranty costs at $40 for parts and $75 for labour. (Assume sales all occur at December 31, 2023.)
In 2024, Chapelle Company incurred actual warranty costs relative to 2023 dishwasher sales of $4,000 for parts and $7,500 for labour.

Instructions
Using the cash basis method, what are the Warranty Expense balances for 2023 and 2024 and prepare the entries?

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Solution 13-97
Warranty expense balance:
2023 $0
Chapelle was not required to honour any warranty during 2023, so no entry is required.

2024 $11,500 ($4,000 + $7,500)

Warranty Expense	11,500	
Inventory		4,000
Salaries and Wages Payable		7,500

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex. 13-98 Premiums
Modern Music gives its customers coupons which are redeemable for a poster plus a Hens and Chicks DVD. One coupon is issued for each dollar of sales. On presentation of 100 coupons and $5.00 cash, the customer receives the poster and DVD. Modern estimates that 80% of the coupons will be presented for redemption. Sales for Year One were $1,050,000, and 510,000 coupons were redeemed. Sales for Year Two were $1,260,000, and 1,275,000 coupons were redeemed. Modern bought 30,000 posters at $2.00 each, and 30,000 DVDs at $5.50 each.

Instructions
Prepare the following entries for both years, assuming all the coupons expected to be redeemed from Year One were redeemed by the end of Year Two.

Entry	Year One	Year Two
a) To record coupons redeemed		
b) To record estimated liability		

Solution 13-98

	Entry	Year One		Year Two	
a)	Estimated Liability for Premiums			8,250	
	Premium Expense [($510,000 ÷ 100) x ($7.50 – $5)]	12,750		*23,625	
	Cash ($510,000 ÷ 100) × $5	25,500		**63,750	
	Inventory of Premiums		38,250		95,625

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*[($1,275,000 ÷ 100) x ($7.50 – $5)] – $8,250
**($1,275,000 ÷ 100) x $5

b)	Premium Expense	*8,250		1,575	
	Estimated Liability for Premiums		8,250		1,575

*[($1,050,000 x.80) – $510,000] ÷ 100 × $2.50

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Ex. 13-99 Premiums
Fido Corp. includes one coupon in each bag of dog food it sells. In return for three coupons, customers receive a dog toy that the company purchases for $1.20 each. Fido's experience indicates that 60% of the coupons will be redeemed. During 2023, 100,000 bags of dog food were sold, 12,000 toys were purchased, and 45,000 coupons were redeemed. During 2024, 120,000 bags of dog food were sold, 16,000 toys were purchased, and 60,000 coupons were redeemed.

Instructions
Determine the premium expense to be reported in the income statement and the estimated liability for premiums on the statement of financial position for 2023 and 2024.

Solution 13-99

	2023	**2024**
Premium expense	$24,000 (1)	$28,800 (3)
Estimated liability for premiums	6,000 (2)	10,800 (4)

(1) 100,000 ×.6 = 60,000; 60,000 ÷ 3 = 20,000; 20,000 × $1.20 = $24,000
(2) 45,000 ÷ 3 = 15,000; 20,000 –15,000 = 5,000; 5,000 × $1.20 = $6,000
(3) 120,000 ×.6 = 72,000; 72,000 ÷ 3 = 24,000; 24,000 × $1.20 = $28,800
(4) 60,000 ÷ 3 = 20,000; 5,000 + 24,000 – 20,000 = $9,000; 9,000 × $1.20 = $10,800

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs and Unearned Revenue
CPA: Financial Reporting
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Ex. 13-100 Contingent liabilities
Below are three independent situations:

1. In August, 2023, a worker was injured in the factory in an accident partially the result of his own negligence. The worker has sued his employer, Prince Corp., for $500,000. Prince's legal counsel believes it is possible that the outcome of the suit will be unfavourable and that the settlement would cost the company from $150,000 to $400,000.
2. On October 4, 2023, a lawsuit for breach of contract seeking damages of $2,400,000 was filed by an author against Queen Corp. Queen's legal counsel believes that an unfavourable outcome is more likely than not. A reliable measurement of the award to the plaintiff is between $600,000 and $1,800,000.
3. King Ltd. is involved in a pending court case. King's lawyers believe it is likely that King will be awarded damages of $700,000.

Instructions
Discuss the proper accounting treatment, including any required disclosures, for each situation. Give the rationale for your answers. Assume all companies involved use IFRS.

Solution 13-100
1. Prince should disclose, in the notes to the financial statements, the existence of a possible contingent liability related to the law suit. The note should indicate the range of the possible loss. The contingent liability should not be accrued because the loss is only possible, not probable (as required by IFRS).

2. The likely award should be accrued by a debit to an estimated loss account and a credit to an estimated liability using the expected value method. Queen should disclose the following in the notes to the financial statements: the amount of the suit, the nature of the contingency, the reason for the accrual, and the range of the possible loss. The accrual is made because it is more likely than not (probable) that a liability has been incurred and the amount of the loss can be measured reliably.

3. King should not record the gain contingency until it is realized. Usually, gain contingencies are neither accrued nor disclosed. The $700,000 gain contingency should be disclosed only if the likelihood that it will be realized is very high.

Difficulty: Medium
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Analysis
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PROBLEMS

Pr. 13-101 Common types of current liabilities
Define and identify common types of current liabilities and how they are valued.

Solution 13-101
Current liabilities are obligations due within one year or the operating cycle where this is longer than one year from the statement of financial position date. The liquidation of a current liability is reasonably expected to require the use of current assets or the creation of other current liabilities. Theoretically, liabilities should be measured at the present value of the future outlay of cash required to liquidate them. In practice, current liabilities, other than borrowings, are usually recorded in accounting records and reported in financial statements at their full maturity value. There are several types of current liabilities, the most common being accounts and notes payable, sales taxes payable, and payroll-related obligations.

Difficulty: Easy
Learning Objective: Define liabilities, distinguish financial liabilities from other liabilities, and identify how they are measured.
Section Reference: Recognition and Measurement
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

Pr. 13-102 Accounts and notes payable
Below are selected transactions of Blackbird Ltd. for 2023, which uses a perpetual inventory system:

1. On May 10, the company purchased goods from Jay Corp. for $60,000, terms 2/10, n/30. The invoice was paid on May 18.
2. On June 1, the company purchased equipment for $180,000 from Seagull Ltd., paying $60,000 in cash and giving a one-year, 8% note for the balance.
3. On September 30, the company borrowed $162,000 from the Second National Bank by signing a one year, zero-interest-bearing note for $178,200. The discount rate was 10%.

Instructions

a) Prepare the journal entries necessary to record these transactions using appropriate dates.
b) Prepare the adjusting entries necessary at December 31, 2023 in order to properly record interest expense related to the above transactions.
c) Indicate the manner in which the above transactions should be reflected in the Current Liabilities section of Blackbird's December 31, 2023 statement of financial position.
d) **CRITICAL THINKING:** The purchase of equipment and inventory on credit are both examples of the company borrowing to purchase items needed to operate the business. Are the amounts owing categorized differently under liabilities and why?

Solution 13-102

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a)

May 10, 2023		
Inventory	60,000	
Accounts Payable		60,000
May 18, 2023		
Accounts Payable	60,000	
Inventory		1,200
Cash		58,800
June 1, 2023		
Equipment	180,000	
Cash		60,000
Notes Payable		120,000
September 30, 2023		
Cash	162,000	
Notes Payable		162,000

b)

Interest Expense	5,600	
Interest Payable ($120,000 × 8% × 7 ÷ 12)		5,600
Interest Expense	4,050	
Notes Payable ($16,200 x 3 ÷ 12)		4,050

c) Current Liabilities

Interest payable	$ 5,600
Note payable—Seagull Ltd.	120,000
Note payable—Second Provincial Bank ($162,000 + $4,050)	166,050
	$291,650

d) **CRITICAL THINKING**: Yes, they are categorized differently. The purchase of goods for resale such as inventory, and even supplies, are categorized as accounts payable if they are purchased on credit instead of with cash. The term accounts payable implies that the borrowing is short term (generally 30 to 90 days) and typically does not have an interest arrangement. The purchase of equipment (a long-term asset), if purchased on credit, would normally be for a longer term, but more importantly would also require an interest arrangement and stated due date. Once a payable has a due date and interest arrangement, it is classified as a note payable. Notes payable can be classified as either current (due within one year of the statement of financial position date), or long term. This distinction helps the user understand the difference in the nature of the liabilities.

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities

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Pr. 13-103 Presentation of short-term debt
At their last year end, December 31, 2023, the liabilities outstanding of Copper Corp. included the following:

1. Cash dividends on common shares, $100,000, payable on January 15, 2024
2. Note payable to Manitoba Bank, $850,000, due January 20, 2024
3. Serial bonds, $2,000,000, of which $500,000 matures during 2024
4. Note payable to Ontario Bank, $200,000, due January 27, 2024

The following transactions occurred early in 2024:

January 15: The cash dividends were paid.
January 20: The note payable to Manitoba Bank was paid.
January 25: Copper entered into a financing agreement with Saskatchewan Bank, enabling it to borrow up to $1,000,000 at any time through the end of 2024. Amounts borrowed under the agreement would bear interest at 1% above the bank's prime rate and would mature three years from the date of the loan. The corporation immediately borrowed $800,000 to replace the cash used in paying its January 20 note to Manitoba Bank.
January 26: 40,000 common shares were issued for $300,000. $200,000 of the proceeds was used to pay off the note payable to Ontario Bank.
February 1: The financial statements for 2023 were issued.

Instructions

a) Prepare a partial statement of financial position for Copper Corp., showing the manner in which the above liabilities should be presented at December 31, 2023 under IFRS. The liabilities should be properly classified between current and long-term, and any appropriate note disclosure should be included.

b) **CRITICAL THINKING:** Identify and describe some reasons why Copper Corp. would issue shares to pay off a note payable.

Solution 13-103

a)

Current liabilities:		
Dividends payable on common shares	$100,000	
Note payable—Manitoba Bank	850,000	
Note payable—Ontario Bank—Note 1	200,000	
Currently maturing portion of serial bonds	500,000	
Total current liabilities		$1,650,000
Long-term debt:		
Serial bonds not maturing currently	1,500,000	

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Total long-term debt	1,500,000
Total liabilities	$3,150,000

Note 1: On January 26, 2024, the corporation issued 40,000 common shares and received proceeds totalling $300,000, of which $200,000 was used to liquidate a note payable that matured on January 27, 2024.

b) **CRITICAL THINKING**: A company should always be reviewing its capital structure to ensure that it is efficient from both a cost and investor satisfaction perspective. In this particular case the cost of equity is less than the cost of this particular debt, Ontario bank issued a demand for payment, an existing investor wanted to increase its position in Copper Corp., and there was no other operational use for the cash. Copper Corp. was having difficulty making the interest/principal payments on the note and needed a cash injection.

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-104 Refinancing of short-term debt
HighTide Inc. is a new business that has been operating for just under two years with great success. Located on a beach, HighTide is in the business of everything to do with surfing. The owner Alex is an avid surfer. In addition to selling boards and accessories, Alex provides surfing lessons on a regular basis. Some of the lessons are located on other beaches in the area. As a result, Alex purchased a new van for the company using a line of credit that the bank extended after the first year of operating the business. The bank found out that Alex did this during the annual review and required Alex take out a term loan to pay off the line of credit. The amount still owing on the line of credit related to the van purchase is $35,000. The bank set up the term loan for 4 years, with a $800 monthly payment.

Instructions

a) Prepare the journal entry for this refinancing arrangement
b) How would the term loan be presented on the statement of financial position
c) **CRITICAL THINKING** Why did the bank make HighTide restructure the debt in this way?

Solution 13-104

a)	Line of Credit.....	35,000	
	Bank Loans.....		35,000
b)	Current Liabilities		
	Current Portion of Bank Loan	9,600	
	Non-Current Liabilities		

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Bank Loans		25,400

c) **CRITICAL THINKING**: Lines of credit are extended for companies to bridge working capital / cash shortfalls. HighTide should be using the line of credit to pay for timing differences related to inventory purchases and cash collections from sales to customers. A purchase of a van, which is a long-term asset, would not be an acceptable use of the line of credit because long-term assets should be paid for with long-term debt.

Difficulty: Medium
Learning Objective: Define current liabilities and identify and account for common types of current liabilities.
Section Reference: Common Current Liabilities
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-105 Payroll deduction entries
Boxcom Company had a total bi-weekly payroll of $90,000. The entire payroll was subject to CPP (5.45%), EI (1.58%), and income tax withholdings of $11,880. Union dues of $1,125 and health insurance premiums of $2,850 were also withheld.

Instructions

a) Prepare the journal entry to record the employee wages/salaries and payroll deductions.
b) Prepare the journal entry to record the employer payroll contributions.
c) Prepare the journal entry to record the remittance to the Receiver General.

Solution 13-105

a)

Salaries and Wages Expense	90,000	
Employee Income Tax Deductions Payable		11,880
CPP Contributions Payable (5.45% x $90,000)		4,905
EI Premiums Payable (1.58% x $90,000)		1,422
Union Dues Payable		1,125
Health Insurance Premium Payable		2,850
Cash		67,843

b)

Payroll Tax Expense	6,896	
CPP Contributions Payable		4,905
EI Premiums Payable (1.58% x $90,000 x 1.4)		1,991

c)

Employee Income Tax Deductions Payable	11,880	
CPP Contributions Payable ($4,905 + $4,905)	9,810	
EI Premiums Payable ($1,422 + $1,991)	3,413	

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Cash..... 25,103

Difficulty: Medium
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Pr. 13-106 Employee-related liabilities
Identify and account for the major types of employee-related liabilities

Solution 13-106
Employee-related liabilities include (1) payroll deductions, (2) compensated absences and (3) bonus agreements. Payroll deductions are amounts withheld from employees along with the employer's required contributions that have not yet been remitted to the government. Compensated absences earned by employees are company obligations that should be recognized as the employees earn the entitlement to them, provided they can be reasonably measured. Bonuses based on income should be accrued as an expense and liability as the income is earned.

Difficulty: Easy
Learning Objective: Identify and account for the major types of employee-related liabilities.
Section Reference: Employee-Related Liabilities
CPA: Financial Reporting
Bloomcode: Knowledge
AACSB: Analytic

Pr. 13-107 Asset retirement obligation – IFRS
Extraction Friendly Ltd. (EFL) specializes in extracting ore. It prides itself for following high environmental standards in the extraction process. On January 1, 2019, EFL purchased the extraction rights to use a parcel of land from the province of New Brunswick. The rights cost $15,000,000 and allowed the company to extract ore for five years, i.e., until Dec 31, 2023. EFL expects to extract the ore evenly over the contract period. At the end of the contract, EFL has one year to clean up and restore the land. EFL estimates this will cost $2,000,000.

EFL uses a discounted cash flow method to calculate the fair value of this obligation and believes that 8% is the appropriate discount rate. EFL uses the straight-line depreciation method. EFL uses the calendar year as its fiscal year and follows IFRS.

As a helpful suggestion, students may want to draw a timeline of events before solving the questions given below.

Instructions (Round all values to the nearest dollar.)
a) Prepare the journal entries to be recorded on January 1, 2019.

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b) Prepare the journal entries to be recorded on December 31, 2019. Show the amounts and accounts to be reported on the classified statement of financial position at December 31, 2019.

c) Prepare the journal entries to be recorded on December 31, 2023. Show the amounts and accounts reported on the classified statement of financial position at December 31, 2023.

d) After 2023, EFL was supposed to clean up and restore the land. Even though the company spent a considerable amount of money on restoration, it was sued by the province of New Brunswick for not following the contract's requirements. On February 3, 2025, judgement was rendered against EFL for $3,000,000. The company claims that because the language in the contract was misleading regarding the restoration costs, it plans to appeal the judgement and expects the ruling to be reduced to anywhere between $1,000,000 and $2,000,000, with $1,500,000 being the probable amount. EFL has not yet released its 2024 financial statements. Discuss how EFL should report this matter on its financial statements for the year ended December 31, 2024.

Solution 13-107

a) To record the purchase of the rights and the ARO:

January 1, 2019

Extraction Rights	15,000,000	
Cash		15,000,000
Extraction Rights	1,361,166	
Asset Retirement Obligation		1,361,166

5 N 8 I 2000000 FV CPT PV => 1,361,166

b) To depreciate the extraction rights over five years and also record accretion (interest) expense on the obligation.

December 31, 2019

Depreciation Expense	3,272,233	
(($15,000,000 + $1,361,166) ÷ 5)		
Accumulated Depreciation—Extraction Rights		3,272,233
Interest Expense**	108,893	
($1,361,166 x 8%)		
Asset Retirement Obligation		108,893

**If the company were using ASPE, the debit is to Accretion Expense

Statement of financial position amounts:

Account	Amount	Classification
Extraction rights net of accumulated depreciation	$13,088,928*	Long-term assets
Asset retirement obligation	$1,470,059**	Long-term liabilities

*$15,000,000 + $1,361,166 – $3,272,231 = $13,088,935
**$1,361,166 + $108,893 = $1,470,059

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c) For the depreciation of the extraction rights, the journal entry is the same every year.

December 31, 2023

Depreciation Expense	3,272,233	
Accumulated Depreciation—Extraction Rights		3,272,233

For the accretion (interest) costs, first you need to find the carrying value of the ARO at January 1, 2023 and then to calculate the expense. Since the carrying value at January 1, 2023 is $1,851,852, the interest expense is 1,851,852 x 8% = 148,149.

Interest Expense	148,148	
Asset Retirement Obligation		148,148

Statement of financial position amounts:

Account	**Amount**	**Classification**
Extraction rights net of accumulated depreciation	0	
Asset retirement obligation	$2,000,000	Current liabilities

Since by the end of 2023 the liability is due to be discharged within a year, it should be classified as a current liability.

d) This is a somewhat complicated situation. Clearly EFL is expecting a contingent loss of anywhere between $1,500,000 and $3,000,000. However, a $3,000,000 judgement has already been rendered against them, while the reduction in the loss is uncertain.
There are two legitimate approaches to this issue. The first approach is to record a loss of $1,500,000 for 2024 (since this amount is deemed probable) and to provide full disclosure in the notes about the ruling and the expected appeal.
The second approach is that the firm has incurred a contingent loss of $3,000,000 and expects a contingent gain of $1,500,000. Because losses are recorded immediately and contingent gains are not, then EFL should record a loss of $3,000,000 for 2024and provide full disclosure on the possible contingent gain.

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-108 Asset retirement obligation – ASPE
Grow It All Farms Ltd. is an agri-business that grows a variety of different grains on the land that it owns. Operations have been steadily expanding over the last few years. The company has now reached a point where it needs to create a reservoir for irrigation purposes. Management has applied to the municipality for permission to create the reservoir by creating a diversion from a creek that

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flows through land that the company owns. The permit has been approved on the condition that Grow It All Farms restore the land and creek to its natural state when operations cease. The company is required to provide the municipality with financial statements on an annual basis.
Management agreed to the condition and has engaged an engineering firm to scope and price out the work. The cost to create the reservoir and divert the creek is $4,000,000. The cost of the restoration is estimated to be $6,000,000 in 20 years. Grow It All Farms borrows at an average rate of 6% from its lenders.

Instructions

a) Prepare the journal entries to set up the asset and the obligation imposed by the municipality.
b) Assume that the fiscal year end is a full 12 months from the date of setting up the asset. Prepare any year-end journal entries.
c) After five years, the municipality has discovered that due to the creek diversion, the fish population has dramatically been depleted, which has affected local communities. To keep the permit in place, the municipality has demanded that Grow It All Farms pay to repopulate the creek immediately, and again when the restoration work is done in the future. Management has agreed. Prepare the journal entries to reflect these requirements assuming that the cost today is $250,000 and $500,000 in the future.
d) **CRITICAL THINKING:** Why is the municipality requiring Grow It All Farms to provide annual financial statements?

Solution 13-108

a)	Land Improvements	4,000,000	
	Cash		4,000,000
	To record the creation of the reservoir		
	Land Improvements	1,870,828	
	Asset Retirement Obligation		1,870,828
	To record the restoration obligation		

PV calculation, FV $6,000,000 N 20 I/Y 6%

b)	Depreciation Expense	293,541	
	Accumulated Depreciation—Land Improvements		293,541

($4,000000 + $1,870,828) / 20 = $293,541

	Accretion Expense	$112,250	
	Asset Retirement Obligation		$112,250

$1,870,828 x 6% = $112,250

c)	Land Improvements	$250,000	
	Cash		$250,000
	To record the immediate cost of repopulating the creek		

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Land Improvements	$208,633	
Asset Retirement Obligation		$208,633
To record the additional restoration obligation		

PV Calculation, FV $500,000, N 15, I/Y 6%

d) **CRITICAL THINKING:** The municipality is now a user of Grow It All Farms financial statements. The requirement to restore the land and creek to its natural state is a significant and expensive obligation. The municipality will want to review the financial statements of Grow It All Farms regularly to ensure that enough of a provision has been made to guarantee that the restoration will happen. A company can promise to clean up a site but making sure that there is enough resources to do so requires planning.

Difficulty: Medium
Learning Objective: Explain the recognition, measurement, and disclosure requirements for decommissioning and restoration obligations.
Section Reference: Decommissioning and Restoration Obligations
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-109 Premiums: expense versus revenue approach
Fancie Cosmetics offers its customers a traveller's gift set as a premium in exchange for $20 if the customer purchases one of the top brand cosmetic makeup kits. The company purchased for cash 2,000 gift sets at $25 each. It estimates that 60% of customers will participate in the promotion and that 10% of the amount received from customers relates to the awarded premiums. In 2023, the company sold 3,000 makeup kits at a sales price of $80 resulting in sales revenue of $240,000. By the end of the year, 1,500 customers took advantage of the promotion.

Instructions
a) Prepare the appropriate journal entries assuming that Fancie follows ASPE and uses the expense approach.
b) Prepare the appropriate journal entries assuming that Fancie follows IFRS and uses the revenue approach. For this part of the question, assume the selling price includes the offer for the premium.

Solution 13-109
a)

Inventory of Premiums	50,000	
Cash ($25 x 2,000 = $50,000)		50,000
Cash	240,000	
Sales Revenue		240,000
Cash (1,500 x $20)	30,000	

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Premium Expense	7,500	
Inventory of Premiums (1,500 x $25)		37,500
Premium Expense	1,500	
Estimated Liability for Premiums		1,500

*Total kits sold	3,000
Total estimated redemptions (60%)	1,800
Customer redemption in 2023	1,500
Estimated future redemptions	300
Cost per premium: ($25 – $20)	$5.00
Cost of estimated claims outstanding (300 x $5)	$1,500

b)

Inventory of Premiums	50,000	
Cash ($25 x 2,000 = $50,000)		50,000
Cash	240,000	
Sales Revenue		216,000
Unearned Revenue (10% x $240,000)		24,000
Cash (1,500 x $20)	30,000	
Premium Expense	7,500	
Inventory of Premiums (1,500 x $25)		37,500
Unearned Revenue	20,000	
Sales Revenue ($24,000 x 1,500 / 1,800)		20,000

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Application
AACSB: Analytic

Pr. 13-110 Premiums: multi-years
Creamy Candy Company offers a coffee mug as a premium for every ten 50-cent candy bar wrappers presented by customers together with $1.00. The purchase price of each mug to the company is 90 cents; in addition it costs 60 cents to mail each mug. The results of the premium plan for the years 2023 and 2024 are as follows (assume all purchases and sales are for cash):

	2023	**2024**
Coffee mugs purchased	480,000	400,000
Candy bars sold	3,750,000	4,500,000
Wrappers redeemed	1,900,000	2,800,000
2023 wrappers expected to be redeemed in 2024	1,300,000	

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2024 wrappers expected to be redeemed in 2025 1,800,000

Instructions

a) Prepare the general journal entries that should be made in 2023 and 2024 related to the above plan by assuming Creamy Candy uses the expense approach.

b) Indicate the account names, amounts, and classifications of the items related to the premium plan that would appear on the statement of financial position and income statement at the end of 2023 and 2024.

Solution 13-110

a)

2023

Inventory of Premiums (480,000 × $.90 = $432,000)	432,000	
Cash		432,000
Cash	1,875,000	
Sales Revenue (3,750,000 × $.50 = $1,875,000)		1,875,000
Cash [1,900,000 ÷ 10 × ($1.00 – $.60) = $76,000]	76,000	
Premium Expense	95,000	
Inventory of Premiums (190,000 × $.90 = $171,000)		171,000
Premium Expense (1,300,000 ÷ 10 × $.50 = $65,000)	65,000	
Estimated Liability for Premiums		65,000

2024

Inventory of Premiums (400,000 × $.90 = $360,000)	360,000	
Cash		360,000
Cash	2,250,000	
Sales Revenue (4,500,000 × $.50 = $2,250,000)		2,250,000
Cash [2,800,000 ÷ 10 × ($1.00 – $.60) = $112,000]	112,000	
Estimated Liability for Premiums	65,000	
Premium Expense	75,000	
Inventory of Premiums (280,000 × $.90 = $252,000)		252,000
Premium Expense	90,000	
Estimated Liability for Premiums		90,000
(1,800,000 ÷ 10 × $.50 = $90,000)		

b) Statement of financial position

Name	Classification	2023	2024
Inventory of Premium Mugs	Current Assets	$261,000	$369,000
Estimated Liability for Premiums	Current Liabilities	65,000	90,000

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Income Statement

Name	Classification	2023	2024
Premium Expense	Operating Expenses	160,000	165,000

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-111 Warranties

Alaska Computer Company sells computers for $2,000 each, which includes a three-year warranty that requires the company to perform periodic services and to replace defective parts. During 2023, Alaska sold 500 computers on account. Based on past experience, the company has estimated the total three-year warranty costs at $80 for parts and $100 for labour. (Assume sales all occur at December 31, 2023.)

In 2024, Alaska Computer Company incurred actual warranty costs relative to 2023 computer sales of $10,000 for parts and $12,000 for labour.

Instructions

a) Using the expense warranty approach, prepare the entries to reflect the above transactions (accrual method) for 2023 and 2024. Use Salaries and Wages Payable.

b) Using the cash basis method, what are the Warranty Expense balances for 2023 and 2024?

c) The transactions of part a) create what balance under current liabilities in the 2023 statement of financial position?

Solution 13-111

a)

2023

Accounts Receivable	1,000,000	
Sales Revenue		1,000,000
Warranty Expense (500 x ($80 + $100))	90,000	
Warranty Liability		90,000

2024

Warranty Liability	22,000	
Inventory		10,000
Salaries and Wages Payable		12,000

b) 2023 $0
2024 $22,000

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c) 2023 Current Liabilities—Warranty Liability $30,000
(The remainder of the $90,000 liability is a long-term liability.)

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-112 Unredeemed coupons
During 2023, Red Deer Corp. sold 200,000 tickets for hockey games for $60 each under a new sales promotion program. Each ticket contains one coupon. Any person who presents 2 coupons can receive a ticket to an Edmonton Flames football game for only $2. Red Deer pays $8.00 per football ticket and at the beginning of 2023 had purchased 80,000 tickets (any tickets not used in 2023 can be used in 2024). The company estimates that 60% of the coupons will be redeemed even though only 50,000 coupons had been processed during 2023.

Instructions

a) What amount should Red Deer report as a liability for unredeemed coupons on December 31, 2023?
b) What amount of expense will Red Deer report on its 2023 income statement as a result of the promotional program?
c) Prepare any necessary 2023 journal entries related to the promotion program.
d) Explain how the accounting treatment for this promotion is treated under IFRS.

Solution 13-112

a) The number of coupons expected to be processed is 200,000 x 60% = 120,000. In 2023, 50,000 coupons were processed, so 70,000 more are expected to be processed and accordingly 35,000 tickets to be purchased. The additional net cost per ticket is $6 and therefore the liability for unredeemed coupons at December 31, 2023 should be 35,000 x $6 = $210,000.

b) Promotion expense = (120,000 ÷ 2) x $6 = $360,000.

c)

Inventory of Premiums (80,000 x $8)	640,000	
Cash		640,000
Cash (200,000 x $60)	12,000,000	
Sales Revenue		12,000,000
Estimated Liability for Premiums	150,000	
Cash (50,000 ÷ 2 x $2)	50,000	
Inventory of Premium (50,000 ÷ 2 x $8)		200,000

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Premium Expense	360,000	
Estimated Liability for Premiums		360,000

d) Under IFRS, this promotion would be considered a multiple deliverables arrangement. Red Deer is selling two separate products (the hockey tickets and the football tickets), with the selling price of the hockey tickets inflated to encourage the ticket purchasers to also purchase football tickets. Therefore some of the revenue from the sale of each hockey ticket should be deferred and allocated to the delivery of the football tickets. An estimated amount should be deferred to 2024 when the remaining coupons will be redeemed.

Difficulty: Medium
Learning Objective: Explain the issues and account for product guarantees, other customer program obligations, and unearned revenue.
Section Reference: Product Guarantees, Customer Programs, and Unearned Revenue
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

Pr. 13-113 Contingencies
You have been hired by Yew Corp. to advise them on how to reflect the events below in their financial statements for the year ended December 31, 2023 under ASPE.

Event 1: The Division A employees union has been negotiating a new contract with Yew Corp. The union is requesting a 5% wage increase retroactive for two years. Yew's management has offered the union a 2% wage increase retroactive for one year. While the negotiations are still ongoing, the company believes that an agreement will soon be reached for a 4% wage increase retroactive for one year, but there is no guarantee that this will be the outcome of the negotiations.

Event 2: The Division B employees union is also negotiating a new contract with Yew Corp. However, these negotiations are proving to be very tough. So far there has not been much progress and management is pessimistic about a quick resolution. The company is concerned that during 2024 the Division B employees will decide to go on strike; in fact, Yew considers it very likely. At this point it is difficult to assess the economic consequences of the potential strike.

Event 3: Toward the end of 2023, a fire destroyed one of Yew's plants. The damage is estimated to be $8,000,000 and the company's insurance policy has maximum coverage of $15,000,000 for this. The deductible on the policy is $300,000. The company is concerned that the insurance premium ($200,000 in 2023) will double in 2024.

Instructions
For each of the above events, state the accounting treatment you believe is most appropriate. Be specific and give your rationale.

Solution 13-113
Event 1: The event is more likely than not to happen and the cost can be reasonably estimated. Yew Corp. should accrue an additional expense for 2023 based on the most likely outcome of a 4% wage increase retroactive for one year. In the notes to the financial statements, they should provide the

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range for the potential expense (2-5%, 1-2 years).

Event 2: If Yew Corp. considers this to be a contingent liability, note disclosure only would be appropriate, since the event is likely to happen but cannot be reasonably estimated. If they do not, then no disclosure is required.

Event 3: The $300,000 deductible payment should be accrued in 2023 as a loss from fire. While the premium is likely to increase and can be reasonably measured, the cost relates to future periods and therefore no expense should be accrued for 2023. Full disclosure of the event and of the expected cost increase for next year is appropriate, unless the amount is immaterial.

Alternatives the company could consider:
1. Shop around for a better deal on insurance.
2. Avoid the potential premium increase by choosing to self-insure.

Difficulty: Medium
Learning Objective: Explain and account for contingencies and uncertain commitments, and identify the accounting and reporting requirements for guarantees and commitments.
Section Reference: Contingencies, Uncertain Commitments, and Requirements for Guarantees and Other Commitments
CPA: Financial Reporting
Bloomcode: Analysis
AACSB: Analytic

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