COMM 217 – FINANCIAL ACCOUNTING
SOLUTIONS TO FINAL EXAM (REGULAR) – WINTER 2022

Question A (13 marks)

Req. 1 (5 marks)

<u>Factory building</u>:
Depreciation expense, 2021 = (Original cost – Estimated residual value) / Estimated useful life
= ($400,000 – $20,000) / 40 years = $9,500

<u>Cutting machine</u>:
Depreciation rate = (Original cost – Estimated residual value) / Estimated total machine hours
= ($125,000 – $25,000) / 80,000 hours = $1.25 per hour
Depreciation expense, 2021 = 15,000 x $1.25 = $18,750

<u>Delivery truck</u>:
Depreciation expense, 2020 = Carrying amount x (2/5) = $45,000 x 0.4 = $18,000
Depreciation expense, 2021 = ($45,000 – $18,000) x 0.4 = $10,800

Req. 2 (4 marks)

Accumulated depreciation, Dec. 31, 2021 = ($13,000 x $1.25) + $18,750 = $35,000

Gain (loss) = Cash – Carrying amount = $75,000 – ($125,000 – $35,000) = –$15,000 (loss)

Cash	75,000	
Accumulated depreciation	35,000	
Loss on sale of cutting machine	15,000	
Cutting machine		125,000

Req. 3 (4 marks)

Accumulated depreciation, April 1, 2022 = $9,500 x 2.5 years = $23,750
Carrying amount, April 1, 2022 = ($400,000 – $23,750) + $50,000 = $376,250 + $50,000
= $426,250

Revised annual depreciation = ($426,250 – $30,000) / (40 – 2.5) years = $10,567

Depreciation expense, 2022 = $9,500 x (3/12) + $10,567 x (9/12) = $2,375 + $7,925 = $10,300

Question B (16 marks)

Req. 1 (11.5 marks)

Jan. 3	Cash (5,000 shares x $70)	350,000	
	Land	240,000	
	Building (10,000 x $70 – $240,000)	460,000	
	Common shares		1,050,000
May 7	Common shares (1,000 shares x $45)	45,000	
	Contributed surplus on common shares	20,000	
	Cash (1,000 x $65)		65,000

Average price per share = ($750,000 + $1,050,000) / (25,000 + 15,000) = $45

Dec. 2	Dividends declared – Preferred (8,000 x $4 x 2 years)	64,000	
	Dividends payable – Preferred		64,000
	Dividends declared–Common	156,000	
	Stock dividend to be issued		156,000
	(40,000 – 1,000) x 5% x $80		
Dec. 20	Stock dividend to be issued	156,000	
	Common shares		156,000

Req. 2 (3 marks)

Brian Labelle received an additional 50 common shares as a result of the 5% stock dividend declared by PDP on May 7. The average cost per share is reduced to $70 ($73,500 / 1,050).

Dec. 30	Cash (500 shares x $75)	37,500	
	Investment in PDP shares (500 x $70)		35,000
	Gain on sale of shares		2,500

Req. 3 (1.5 marks)

The basic rights of common shareholders are:

1. To vote on significant corporate matters in person or by proxy (at the annual general meeting of shareholders).
2. To share in the distribution of earnings when dividends are declared.
3. To share in the distribution of assets upon liquidation of the corporation.

Question C

Req. 1 (7 marks)

FURNITURE R US
Statement of Cash Flows (partial)
For the Year Ended December 31, 2021

Operating activities	
Net earnings	$ 200
Add (deduct) items not affecting cash:	
Depreciation and amortization expense	65
Loss on sale of equipment	5
Changes in non-cash working capital items:	
Increase in accounts receivable, net	(30)
Increase in inventories	(55)
Decrease in accounts payable	(20)
Increase in accrued liabilities	70
Increase in income tax payable	15
Increase in customers' deposits	60
Increase in deferred warranty plan revenue	5
Net Cash flows from operating activities	$315

Note: Both the current and non-current portions of deferred warranty plan revenue relate to operating activities. But, most students may not include the change in the balance of the non-current portion. It is therefore excluded in this solution.

Req. 2 (2.5 marks)

Cash collections = Sales revenue – Increase in accounts receivable + Increase in customers' deposits
= $2,400 – ($160 – $130) + ($365 – $305) = $2,430

Req. 3 (2 marks)

Cash paid for SG&A expenses = SG&A expenses – Depreciation and amortization expense
– Increase in accrued liabilities
= $825 – $65 – ($200 – $130) = $690

Req. 4 (3 marks)

Dividends declared = Beginning retained earnings + Net earnings – Ending retained earnings
= $900 + $200 – $940 = $160

Dividends paid = Dividends declared + Decrease in dividends payable
= $160 + ($35 – $10) = $185

Dec. 30	Dividends payable	185	
	Cash		185

Req. 5 (3.5 marks)

Both the current and non-current portions of deferred warranty plan revenue should be considered.

Revenue from extended warranty plans = Beginning deferred warranty plan revenue
+ Additional extended warranty plan contracts in 2021
– Ending deferred warranty plan revenue

= ($55 + $95) + $80 – ($60 + $100) = $70

Dec. 30	Deferred warranty plan revenue	70	
	Warranty plan revenue		70

Req. 6 (9 marks)

a. **Quick ratio** = (Cash and cash equivalents + Accounts receivable, net) / Current liabilities
= ($480 + $160) / $815 = $640 / $815 = 0.79

This ratio is an indicator of the amount of quick assets available to satisfy current liabilities. The company has $0.79 in quick assets for every $1 of current liabilities.

a. **Receivables turnover ratio** = Net credit sales / Average net accounts receivable
= ($2,500 x 0.6) / [($130 + $160) / 2] = 10.34

This ratio indicates that the company collected its accounts receivable, on average, 10.34 times during 2021. It measures the effectiveness of the company's credit granting and collection activities.

b. **Debt-to-equity ratio** = Total liabilities / Shareholders' equity
= $1,405 / $1,090 = 1.29

The debt-to-equity ratio indicates how much debt has been used to finance the company's acquisition of assets relative to equity financing that is supplied by shareholders. The company has used $1.29 of debt for every $1 of equity to finance the acquisition of assets.

c. **Return on equity** = Net earnings / Average shareholders' equity
= $200 / [($1,115 + $1,090) / 2] = 0.18

ROE measures how much the firm earned as a percentage of shareholders' investment. It reflects how well has management used shareholders' investment to generate net earnings during the period.

d. **Gross profit percentage** = Gross profit / Net sales
= ($2,500 – $1,400) / $2,500 = 0.44 or 44%

This ratio measures how much gross profit is generated from every sales dollar. It reflects management's ability at selling goods and services for more than the costs to purchase or produce them.

e. **Fixed asset turnover ratio** = Sales revenue / Average net fixed assets
= $2,500 / ($700 + $660) / 2] = 3.68

This ratio measures the sales dollars generated by each dollar of fixed assets used. It reflects the company's effectiveness at generating sales from its fixed assets.

Question D

1. B [$6,000,000 x 0.747 + $330,000 x 4.212 = $5,871,960]	12. B
2. A	13. C
3. D [$5,871,960 x 0.06 x 9/12]	14. C
4. C	15. D
5. E	16. A
6. C [$6,000,000 x 101% - $5,943,000]	17. D
7. E	18. B [($770,000 – $750,000) x 45%]
8. C	19. A
9. B	20. C [$700,000 x 3% – $9,000]
10. B	21. B
11. D	22. A [($500,000 – $375,000) / 1,500,000