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Students' Department

H. P. Baumann

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Students' Department

H. P. BAUMANN, *Editor*

AMERICAN INSTITUTE EXAMINATIONS

[NOTE.—The fact that these solutions appear in THE JOURNAL OF ACCOUNTANCY should not cause the reader to assume that they are the official solutions of the board of examiners. They represent merely the opinions of the editor of the *Students' Department*.]

EXAMINATION IN ACCOUNTING THEORY AND PRACTICE—PART II

May 15, 1931, 1:30 P. M. to 6:30 P. M.

The candidate must answer all the following questions.

No. 2 (30 points):

From the data following, prepare the journal entries necessary properly to adjust the accounts for the purpose of consolidation and submit a consolidated balance-sheet, together with working papers.

The results of examinations of the books of the Kerry Dairy Company and its subsidiaries, as of June 30, 1929, were shown as follows:

	Kerry Dairy Co.	City Creamery	Watson & Roan, Inc.	Newport Dairy Co.
<i>Assets</i>				
Cash	\$ 7,500	\$ 4,500	\$ 8,000	\$ 1,500
Notes receivable	10,000		5,000	2,000
Accounts receivable	24,000	10,000	17,500	6,800
Merchandise inventories	15,000	8,000	13,000	4,000
Investments:				
City Creamery	28,000			
Watson & Roan, Inc.	52,000			
Newport Dairy Co.	30,000			
Land	11,500		7,000	
Buildings	26,000		28,000	
Plant equipment	34,000	25,000	35,000	42,000
Delivery equipment	8,000	3,000	9,000	7,000
Deficit				2,400
	\$246,000	\$50,500	\$122,500	\$65,700
<i>Liabilities</i>				
Notes payable	\$ 15,000	\$ 7,500	\$ 10,000	\$12,000
Accounts payable	20,000	6,200	2,700	4,200
Bonds payable	40,000		20,000	
Reserves for depreciation	35,000	6,000	18,600	9,500
Capital stock	125,000	25,000	65,000	40,000
Surplus	11,000	5,800	6,200	
	\$246,000	\$50,500	\$122,500	\$65,700

During the course of the audit, the following facts were discovered:

The holding company purchased 90 per cent. of the capital stock of the City Creamery, July 1, 1926; 80 per cent. of that of Watson & Roan, Inc., July 1, 1925, and 75 per cent. of that of the Newport Dairy Co., July 1, 1927, when this company was organized.

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The investment in the City Creamery was arbitrarily increased on the books of the holding company in 1929 by a charge thereto and a credit to surplus of \$2,000. Except for this entry, the book value of the investment represented cost. The investment in the Newport Dairy Co. was also carried at cost. The holding company had, however, taken up its share of the profits and losses of Watson & Roan, Inc., through the investment account.

An analysis of the surplus accounts of the subsidiary companies was as follows:

	City Creamery	Watson & Newport Roan, Inc. Dairy Co.	
Balance—June 30, 1925		\$15,200	
Profit—1925-1926		2,500	
Balance—June 30, 1926	\$3,500	17,700	
Profit—1926-1927	2,400*	8,000*	
Balance—June 30, 1927	1,100	9,700	
Profit—1927-1928	1,500	2,700	\$1,500*
Balance—June 30, 1928	2,600	7,000	1,500*
Profit—1928-1929	3,200	800*	900*
Balance—June 30, 1929	\$5,800	\$ 6,200	\$2,400*

The inter-company accounts were as follows:

	Kerry Dairy Co.	City Creamery	Watson & Newport Roan, Inc. Dairy Co.	
On the books of				
Notes receivable—				
Kerry Dairy Co.		\$2,000	\$3,000	\$5,000
Watson & Roan, Inc.				3,000
Notes payable—				
City Creamery	\$2,000			
Watson & Roan, Inc.	3,000			
Newport Dairy Co.	5,000		3,000	
Accounts receivable—				
Kerry Dairy Co.		2,400	1,700	1,800
City Creamery				600
Accounts payable—				
City Creamery	2,200			
Watson & Roan, Inc.	1,600			
Newport Dairy Co.	1,500	600		

The inventories of the subsidiary companies contain goods purchased from the holding company on which the latter made a profit of 10 per cent., viz, City Creamery \$3,000, and Watson & Roan, Inc. \$1,200.

In June, 1929, the Newport Dairy Co. purchased plant equipment from Watson & Roan, Inc., and paid \$12,000 therefor. The cost to Watson & Roan, Inc. (less depreciation) was \$10,000.

The differences in inter-company accounts represent remittances in transit at the date of closing.

Solution:

ADJUSTMENTS AND ELIMINATIONS

(A)

Surplus—Kerry Dairy Company	\$ 2,000	
Investment—City Creamery		\$ 2,000
To reverse arbitrary write-up of investment in City Creamery.		

*Representing loss.

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(B)		
Notes payable.....	\$ 13,000	
Notes receivable.....		\$13,000
To eliminate inter-company notes payable and receivable.		

Company	Payable	Receivable
Kerry Dairy Co.....	\$	\$10,000
City Creamery.....	2,000	
Watson & Roan, Inc.....	3,000	3,000
Newport Dairy Co.....	8,000	
Total.....	<u>\$13,000</u>	<u>\$13,000</u>

(C)		
Cash.....		600
Accounts payable.....		5,900
Accounts receivable.....		6,500
To eliminate inter-company receivables and to record inter-company cash in transit.		

Company	Payables	Receivables	Cash
Kerry Dairy Co.....	\$	\$ 5,900	\$600
City Creamery.....	2,200	600	
Watson & Roan, Inc.....	1,600		
Newport Dairy Co.....	2,100		
Total.....	<u>\$5,900</u>	<u>\$6,500</u>	<u>\$600</u>

(D)		
Capital stock—City Creamery.....	22,500	
Investment in City Creamery.....		22,500
To eliminate the holding company's 90% interest in the capital stock (\$25,000) of City Creamery.		

(E)		
Capital stock—Watson & Roan, Inc.....	52,000	
Investment in Watson & Roan, Inc.....		52,000
To eliminate the holding company's 80% interest in the capital stock (\$65,000) of Watson & Roan, Inc.		

(F)		
Capital stock—Newport Dairy Co.....	30,000	
Investment in Newport Dairy Co.....		30,000
To eliminate the holding company's 75% interest in the capital stock (\$40,000) of Newport Dairy Co.		

(G)		
Surplus—City Creamery.....	3,150	
Investment in City Creamery.....		3,150
To eliminate the holding company's 90% interest in the surplus (\$3,500) of City Creamery at date of acquisition, July 1, 1926.		

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(H)

Surplus—Watson & Roan, Inc.	\$4,960	
Investment in Watson & Roan, Inc.		\$4,960
To eliminate the holding company's 80% interest in the surplus (\$6,200) of Watson & Roan, Inc., at June 30, 1929. The holding company has taken up its share of the profits and losses.		

In addition to the above adjustments and eliminations which are lettered for the purpose of identification in the working papers, the following adjustments should be taken up on the books of the Kerry Dairy Company:

Surplus	\$ 420	
Reserve for inter-company profit in inventories		\$ 420
To set aside the inter-company profit in inventories for goods sold to the following subsidiaries:		
City Creamery	\$3,000	
Watson & Roan, Inc.	1,200	
Total	<u>\$4,200</u>	
10% thereof		<u>\$ 420</u>

Surplus	2,000	
Reserve for inter-company profit in plant and equipment . .		2,000
To set aside the inter-company profit in plant and equipment sold in June, 1929, to Newport Dairy Co., by Watson & Roan, Inc.		
Selling price	\$12,000	
Cost to Watson & Roan, Inc. less depreciation	<u>10,000</u>	
Inter-company profit	<u>\$2,000</u>	

Cash (cash in transit)	600	
Accounts receivable		600
To record the cash in transit from the following:		
City Creamery	\$200	
Watson & Roan, Inc.	100	
Newport Dairy Co.	<u>300</u>	
Total	<u>\$600</u>	

KERRY DAIRY COMPANY AND ITS SUBSIDIARIES
Consolidated Balance-sheet, June 30, 1929

Assets

Current assets:

Cash:		
In banks	\$ 21,500	
In transit		600
	<u> </u>	<u>\$ 22,100</u>

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KERRY DAIRY COMPANY AND ITS SUBSIDIARIES
Consolidated Balance-sheet—Working papers, June 30, 1929

Assets	Kerry Dairy Company	City Creamery	Watson & Roan, Inc.	Newport Dairy Co.	Adjustments and eliminations	Consolidated balance-sheet
					Debit	
					Credit	
Cash.....	\$ 7,500	\$ 4,500	\$ 8,000	\$ 1,500		\$ 22,100
Notes receivable.....	10,000		5,000	2,000		4,000
Accounts receivable.....	24,000	10,000	17,500	6,800	\$ 13,000 (B)	51,800
Merchandise inventories.....	15,000	8,000	13,000	4,000	6,500 (C)	40,000
Land.....	11,500		7,000			18,500
Buildings.....	26,000		28,000			54,000
Plant equipment.....	34,000	25,000	35,000	42,000		136,000
Delivery equipment.....	8,000	3,000	9,000	7,000		27,000
Investment in City Creamery (90%).....	28,000				2,000 (A)	
Eliminate holding company's write-up (July 1, 1926).....					22,500 (D)	
Eliminate book value at acquisition:					3,150 (G)	350 (G)
Capital stock (90% of \$25,000).....						
Surplus (90% of \$3,500).....						
Good will.....						
Investment in Watson & Roan, Inc. (80%).....	52,000					
Eliminate present book value:						
Capital stock (80% of \$65,000).....					52,000 (E)	
Surplus (80% of \$6,200).....					4,960 (H)	4,960 (G)
Surplus arising through consolidation.....						
Investment in Newport Dairy Co. (75%).....	30,000					
Eliminate book value at acquisition:						
(July 1, 1927).....						
Capital stock (75% of \$40,000).....					30,000 (F)	
	<u>\$246,000</u>	<u>\$50,500</u>	<u>\$122,500</u>	<u>\$63,300</u>	<u>\$600</u>	<u>\$348,790</u>
					<u>\$134,110</u>	

KERRY DAIRY COMPANY AND ITS SUBSIDIARIES
 Consolidated Balance-sheet—Working papers, June 30, 1929—(Continued)

	Kerry Dairy Company and Newports			Adjustments and eliminations		Consolidated balance-sheet
	Kerry Dairy Company	City Creamery Roan, Inc.	Watson & Roan, Inc.	Debit	Credit	
<i>Liabilities and net worth</i>						
Forwarded.....				\$ 600	\$134,110	
Notes payable.....	\$ 15,000	\$ 7,500	\$ 10,000	13,000 (B)		\$ 31,500
Accounts payable.....	20,000	6,200	2,700	4,200		27,200
Bonds payable.....	40,000		20,000	5,900 (C)		60,000
Reserves for depreciation.....	35,000	6,000	18,600			69,100
Capital stock:						
Kerry Dairy Company.....	125,000					125,000
City Creamery.....		25,000				
Eliminate holding company's 90%.....				22,500 (D)		
Minority interest 10%.....						2,500 (M)
Watson & Roan, Inc.....			65,000			
Eliminate holding company's 80%.....				52,000 (E)		
Minority interest 20%.....						13,000 (M)
Newport Dairy Co.....			40,000			
Eliminate holding company's 75%.....				30,000 (F)		
Minority interest 25%.....						10,000 (M)
Surplus:						
Kerry Dairy Company.....	11,000					
Less write-up of City Creamery's investment.....				2,000 (A)		
Reserve for inter-company profit:						
In inventories; 10% of \$4,200.....						420 (R)
On plant equipment.....						2,000 (R)
Balance—surplus.....		5,800				6,580 (S)
City Creamery.....						580 (M)
Minority; 10% of present surplus.....						
Eliminate holding company's 90% of \$3,500 surplus at acquisition.....				3,150 (G)		
Surplus; 90% of \$2,300 increase.....						2,070 (S)
Watson & Roan, Inc.....			6,200			
Minority; 20% of present surplus.....						1,240 (M)
Eliminate holding company's 80% of present surplus.....				4,960 (H)		
Newport Dairy Co.....			2,400			
Minority; 25% of present deficit.....						600 (M)
Surplus; 75% of \$2,400 decrease.....						1,800 (S)
	<u>\$246,000</u>	<u>\$50,500</u>	<u>\$122,500</u>	<u>\$63,300</u>	<u>\$134,110</u>	<u>\$348,790</u>

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Notes receivable.....	\$ 4,000	
Accounts receivable.....	51,800	
Inventories.....	\$40,000	
<i>Less</i> —reserve for inter-company profits...	420	39,580
		\$117,480
Fixed assets:		
Plant equipment.....	\$136,000	
<i>Less</i> —reserve for inter-company profit.....	2,000	
	\$134,000	
Delivery equipment.....	27,000	
Buildings.....	54,000	
Total.....	\$215,000	
<i>Less</i> —reserve for depreciation.....	69,100	
	\$145,900	
Land.....	18,500	
		164,400
		\$281,880
<i>Liabilities and net worth</i>		
Current liabilities:		
Notes payable.....	\$ 31,500	
Accounts payable.....	27,200	
		\$ 58,700
Bonds payable.....		60,000
Minority interest:		
Capital stock.....	\$ 25,500	
Surplus.....	1,220	
		26,720
Net worth:		
Capital stock.....	\$125,000	
Surplus.....	6,850	
Surplus arising through consolidation.....	4,610	
		136,460
		\$281,880

The surplus arising through the consolidation of the accounts of Watson & Roan, Inc., of \$4,960 is reduced, in the above balance-sheet by the amount of the "positive" good will arising through the consolidation of the accounts of City Creamery in the amount of \$350. Authoritative opinion can be mustered, also, to support the showing of the good will of \$350 in the balance-sheet, with the surplus arising through consolidation at \$4,960.