

TERM TEST - OCTOBER 26, 1999
ANSWERS

PART A.

Form 00		Form 01	
1	C	1	D
2	B	2	D
3	D	3	C
4	D	4	A
5	C	5	B
6	A	6	C
7	B	7	A
8	C	8	D
9	A	9	D
10	D	10	D
11	D	11	E
12	D	12	A
13	E	13	C
14	A	14	C
15	C	15	E
16	C	16	B
17	E	17	C
18	B	18	A
19	C	19	C
20	A	20	B
21	C	21	B
22	B	22	A
23	B	23	B
24	A	24	A
25	B	25	D
26	A	26	C
27	D	27	D
28	C	28	B
29	D	29	C
30	B	30	B

PART B.

Bid A.

ITEM	CALCULATION	PV
BID A:		
Surface 1	12,000 sq. ft. x \$8.25	\$ 99,000.00
Surface 2	\$99,000 x .64993	64,343.07
Maintenance 1	12,000 x \$0.15 x 3.23972	5,831.50
Maintenance 2	12,000 x \$0.15 x (5.99525- 3.88965)	<u>3,890.08</u>
Total Bid A.		<u>\$172,964.65</u>
BID B:		
Surface 1	12,000 x \$12.50	\$150,000.00
Maintenance	12,000 x .05 x 5.99525	<u>3,597.15</u>
Total Bid B.		<u>\$153,597.15</u>

PART C.

Overview:

Company

- 1st year
- 6 month audit for bank due to loan application

Industry

- Cosmetics
- Currently labour disputes and strikes pending

Users

- bank – to approve loan application – conservative
- shareholders – conservative, long-term; aggressive, short-term
- union – aggressive – to get more pay/benefits for employees
- management – aggressive – to please bank; conservative – to create positive future trend and for negotiations with union leaders
- competitors
- RTC
- Suppliers – conservative

Role: Auditor – conservative

Constraints: GAAP – company being audited

FRO: Conservative

Issues:

1. Amortization of building
 - a) estimated life 20 years (realistic) vs. 35 years (biased)
GAAP requires information to be RELIABLE (free from bias)
 - b) Method SLN vs. DDB.
Choose either, but support – SLN most common for buildings
However, accelerated could be justified; e.g., cosmetics business – is technology an issue? Presentation, location important? Growth potential (1st year of operation).
2. Stock dividend – does not use cash; however dilutes EPS if earnings vs. earnings estimate is an issue. If the bank loan falls through the may have to issue more shares and will want stable or rising price. Until declared, not an accounting issue. When declared must be recorded.
3. Contingent liability
Discussion re treatment
 - Accrue if likely and amount is estimable
 - Disclose if not known (likelihood or amount)
 - Disclosure not required if not likely to happen
 - In this case MUST accrue
4. Strike
Not an accounting event; no disclosure in financial reports; will be reported in news media.

Recommendations must be in keeping with FRO and with GAAP. GAAP and accounting concepts should be discussed.