Advanced Accounting, 11e **(Beams/Anthony/Bettinghaus/Smith)**

Chapter 5 Intercompany Profit Transactions - Inventories

Multiple Choice Questions

1) The material sale of inventory items by a parent company to an affiliated company
A) enters the consolidated revenue computation only if the transfer was the result of arm's length bargaining.
B) affects consolidated net income under a periodic inventory system but not under a perpetual inventory system.
C) does not result in consolidated income until the merchandise is sold to outside parties.
D) does not require a working paper adjustment if the merchandise was transferred at cost.
Answer: C
Objective: LO1
Difficulty: Easy

2) Phast Corporation owns a 80% interest in Stechno Company, acquired several years ago at a cost equal to book value and fair value. Stechno sells merchandise to Phast for the first time in 2011, and some is unsold at December 31, 2011. In computing income from the investee for 2011 under the equity method, Phast uses which equation?
A) 80% of Stechno's income less 100% of the unrealized profit in Phast's ending inventory
B) 80% of Stechno's income plus 100% of the unrealized profit in Phast's ending inventory
C) 80% of Stechno's income less 80% of the unrealized profit in Phast's ending inventory
D) 80% of Stechno's income plus 80% of the unrealized profit in Phast's ending inventory
Answer: C
Objective: LO1
Difficulty: Moderate

3) Assume there are routine inventory sales between parent companies and subsidiaries. When preparing the consolidated financial statements, which of the following line items is indifferent to the sales being either upstream or downstream?
A) Consolidated retained earnings
B) Consolidated gross profit
C) Noncontrolling interest share
D) Controlling interest share of consolidated net income
Answer: B
Objective: LO1
Difficulty: Easy

4) A(n) ________ sale is a sale by a parent company to a subsidiary. A(n) ________ sale is a sale by a subsidiary to a parent company.
A) deferred; realized.
B) realized; deferred.
C) upstream; downstream
D) downstream; upstream
Answer: D
Objective: LO2
Difficulty: Easy

Use the following information to answer the question(s) below.

Paggle Corporation owns 80% of Spillway Inc.'s common stock that was purchased at its underlying book value. At the time of purchase, the book value and fair value of Spillway's net assets were equal. The two companies report the following information for 2011 and 2012.

During 2011, one company sold inventory to the other company for $50,000 which cost the transferor $40,000. As of the end of 2011, 30% of the inventory was unsold. In 2012, the remaining inventory was resold outside the consolidated entity.

2011 Selected Data:	Paggle	Spillway
Sales Revenue	$600,000	$320,000
Cost of Goods Sold	320,000	155,000
Other Expenses	100,000	89,000
Net Income	$180,000	$76,000
Dividends Paid	19,000	0

2012 Selected Data:	Paggle	Spillway
Sales Revenue	$580,000	$445,000
Cost of Goods Sold	300,000	180,000
Other Expenses	130,000	171,000
Net Income	$150,000	$94,000
Dividends Paid	16,000	5,000

5) If the sale referred to above was a downstream sale, the total sales revenue reported in the consolidated income statement for 2011 would be

A) $870,000.
B) $880,000.
C) $920,000.
D) $970,000.

Answer: A

Explanation: A)

2011 combined sales	$920,000
Less: 2011 intercompany sales	(50,000)
Consolidated sales	$870,000

Objective: LO2

6) If the sale referred to above was a downstream sale, by what amount must Inventory on the consolidated balance sheet be reduced to reflect the correct balance as of the end of 2011?

A) $3,000
B) $10,000
C) $14,000
D) $20,000

Answer: A

Explanation: A)

Selling price	$50,000
Less: Cost of sales	40,000
Original unrealized profit	10,000
Unsold percentage	30%
Unrealized profit	$3,000

Objective: LO2

7) For 2011, consolidated net income will be what amount if the intercompany sale was downstream?
A) $180,000
B) $253,000
C) $256,000
D) $259,000
Answer: B
Explanation: B)

2011 Combined Net Income	$256,000
Less: Unrealized Profit (above)	(3,000)
2011 Consolidated Net Income	$253,000

Objective: LO2
Difficulty: Moderate

8) If the intercompany sale mentioned above was an upstream sale, what will be the reported amount of total consolidated sales revenue for 2012?
A) $1,025,000
B) $1,900,000
C) $1,950,000
D) $2,000,000
Answer: A
Explanation: A) There were no intercompany sales in 2012 to eliminate.
Objective: LO2
Difficulty: Moderate

9) If the intercompany sale was an upstream sale, the total amount of consolidated cost of goods sold for 2012 will be
A) $300,000.
B) $430,000.
C) $470,000.
D) $477,000.
Answer: D
Explanation: D)

Combined cost of goods sold	$480,000
Less: Unrealized profit in the 2012 beginning inventory	(3,000)
Consolidated cost of sales	$477,000

Objective: LO2
Difficulty: Moderate

Use the following information to answer the question(s) below.

Pouch Corporation acquired an 80% interest in Shenley Corporation on January 1, 2012, when the book values of Shenley's assets and liabilities were equal to their fair values. The cost of the 80% interest was equal to 80% of the book value of Shenley's net assets. During 2012, Pouch sold merchandise that cost $70,000 to Shenley for $86,000. On December 31, 2012, three -fourths of the merchandise acquired from Pouch remained in Shenley's inventory. Separate incomes (investment income not included) of the two companies are as follows:

	Pouch	Shenley
Sales Revenue	$180,000	$160,000
Cost of Goods Sold	120,000	90,000
Operating Expenses	17,000	21,000
Separate incomes	$ 43,000	$ 49,000

10) The consolidated income statement for Pouch Corporation and subsidiary for the year ended December 31, 2012 will show consolidated cost of sales of

A) $120,000.
B) $136,000.
C) $148,000.
D) $210,000.

Answer: B

Explanation: B)

Combined cost of sales	$210,000
Less: Intercompany cost of sales	(86,000)
Plus: Unrealized profit (16,000 × 75%)	12,000
Consolidated cost of sales	$136,000

Objective: LO3
Difficulty: Moderate

11) What is Pouch's income from Shenley for 2012?

A) $27,200
B) $29,600
C) $39,200
D) $49,000

Answer: A

Explanation: A) ($49,000 × 80%)- $12,000 = $27,200

Objective: LO3
Difficulty: Moderate

12) Swamp Co., a 55%-owned subsidiary of Pond Inc., made the following entry to record a sale of merchandise to Pond:

Accounts Receivable	40,000	
Sales Revenue		40,000

All Swamp sales are at 125% of cost. One-fourth of this merchandise remained in the Pond's inventory at year-end. A working paper entry to eliminate unrealized profits from consolidated inventory would include a credit to Inventory in the amount of

A) $2,000.
B) $2,500.
C) $8,000.
D) $10,000.

Answer: A

Explanation: A)

Selling price	$40,000
Less: Cost of sales ($40,000 / 125%)	32,000
Intercompany profit	8,000
× Unsold Portion (1/4) =	$2,000

Objective: LO3
Difficulty: Moderate

Use the following information to answer the question(s) below.

Pew Corporation acquired 80% ownership of Sordid Incorporated, at a time when Pew's investment cost was equal to 80% of Sordid's book value. At the time of acquisition, the book values and fair values of Sordid's assets and liabilities were equal. Pew uses the equity method. During 2011, Pew sold goods to Sordid for $160,000 making a gross profit percentage of 20%. Half of these goods remained unsold in Sordid's inventory at the end of the year. Income statement information for Pew and Sordid for 2011 were as follows:

	Pew	Sordid
Sales Revenue	$800,000	$300,000
Cost of Goods Sold	500,000	160,000
Operating Expenses	200,000	80,000
Separate incomes	$100,000	$60,000

13) The 2011 consolidated income statement showed cost of goods sold of
A) $500,000.
B) $516,000.
C) $532,000.
D) $660,000.
Answer: B
Explanation: B)

Combined Cost of Goods Sold	$660,000
Less: Intercompany Sales	(160,000)
Plus: Profit in ending inventory	16,000
Consolidated Cost of Goods Sold	$516,000

Objective: LO3
Difficulty: Moderate

14) What is Pew's income from Sordid for 2011?
A) $32,000
B) $48,000
C) $60,000
D) $75,000
Answer: A

15) The 2011 consolidated income statement showed noncontrolling interest share of
A) $3,200.
B) $6,400.
C) $8,800.
D) $12,000.
Answer: D
Explanation: D) Downstream sale has no effect on noncontrolling interest share; $60,000 × .2 = $12,000

16) On January 1, 2011, Plastam Industries acquired an 80% interest in Sparta Company to assure a steady supply of Sparta's inventory that Plastam uses in its own manufacturing businesses. Sparta sold 100% of its output to Plastam during 2011 and 2012 at a markup of 125% of Sparta's cost. Plastam had $12,000 of these items remaining in its inventory at December 31, 2012. If Plastam neglected to eliminate unrealized profits from all intercompany sales from Sparta, the inventory on the consolidated balance sheet at December 31, 2012 was

A) overstated by $1,920.
B) understated by $1,920.
C) overstated by $2,400.
D) understated by $2,400.

Answer: C

Explanation: C) $12,000 - ($12,000 / 1.250) = $2,400

Objective: LO4

Difficulty: Moderate

Use the following information to answer the question(s) below. .

Pelga Company routinely receives goods from its 80% -owned subsidiary, Swede Corporation. In 2011, Swede sold merchandise that cost $80,000 to Pelga for $100,000. Half of this merchandise remained in Pelga's December 31, 2011 inventory. This inventory was sold in 2012. During 2012, Swede sold merchandise that cost $160,000 to Pelga for $200,000. $62,500 of the 2012 merchandise inventory remained in Pelga's December 31, 2012 inventory. Selected income statement information for the two affiliates for the year 2012 was as follows:

	Pelga	Swede
Sales Revenue	$500,000	$400,000
Cost of Goods Sold	400,000	320,000
Gross profit	$100,000	$80,000

17) Consolidated cost of goods sold for Pelga and Subsidiary for 2012 were

A) $512,000.
B) $526,000.
C) $522,500.
D) $528,000.

Answer: C

Explanation: C)

Combined Cost of Goods Sold	$720,000
Less: Intercompany sales	(200,000)
Adjust: Profit -10,000+12,500	2,500
Consolidated Cost of Goods Sold	$522,500

Objective: LO4

Difficulty: Moderate

18) What amount of unrealized profit did Pelga Company have at the end of 2012?

A) $10,000
B) $12,500
C) $50,000
D) $62,500

Answer: B

Objective: LO4

Difficulty: Moderate

19) A parent company regularly sells merchandise to its 70% -owned subsidiary. Which of the following statements describes the computation of noncontrolling interest share?
A) The subsidiary's net income times 30%
B) (The subsidiary's net income × 30%) + unrealized profits in the beginning inventory - unrealized profits in the ending inventory
C) (The subsidiary's net income + unrealized profits in the beginning inventory - unrealized profits in the ending inventory) × 30%
D) (The subsidiary's net income + unrealized profits in the ending inventory - unrealized profits in the beginning inventory) × 30%
Answer: A
Objective: LO5
Difficulty: Moderate

20) Shalles Corporation, a 80%-owned subsidiary of Pani Corporation, sold inventory items to its parent at a $48,000 profit in 2012. Pani resold one -third of this inventory to outside entities. Shalles reported net income of $200,000 for 2012. Noncontrolling interest share of consolidated net income that will appear in the income statement for 2012 is
A) $30,400.
B) $32,000.
C) $33,600.
D) $40,000.
Answer: C
Explanation: C)

Shalles' reported income	$200,000
Less: Unrealized profits in ending inventory	(32,000)
Shalles' adjusted income	168,000
Noncontrolling interest percentage	20%
Noncontrolling interest share	$33,600

Objective: LO5
Difficulty: Moderate

Exercises

1) Penguin Corporation acquired a 60% interest in Squid Corporation on January 1, 2012, at a cost equal to 60% of the book value of Squid's net assets. At the time of the acquisition, the book values of Squid's assets and liabilities were equal to the fair values. Squid reports net income of $880,000 for 2012. Penguin regularly sells merchandise to Squid at 120% of Penguin's cost. The intercompany sales information for 2012 is as follows:

Intercompany sales at selling price	$672,000
Sales value of merchandise unsold by Squid	$132,000

Required:

1. Determine the unrealized profit in Squid's inventory at December 31, 2012.

2. Compute Penquin's income from Squid for 2012.

Answer:

Requirement 1

$132,000 - ($132,000/1.2) =	$22,000

Requirement 2

Penquin's income from Squid:	
Penquin's share of Squid income ($880,000 × 60%)	$528,000
Less: Unrealized profit in ending inventory	(22,000)
Penquin's income from Squid	$506,000

Objective: LO3
Difficulty: Moderate

2) Salli Corporation regularly purchases merchandise from their 90% -owner, Playtime Corporation. Playtime purchased the 90% interest at a cost equal to 90% of the book value of Salli's net assets. At the time of acquisition, the book values and fair values of Salli's assets and liabilities were equal. Playtime makes their sales to Salli at 120% of cost. In 2012, Salli reported net income of $460,000, and made purchases totaling $172,000 from Playtime. Although Salli had no inventory on hand at the beginning of 2012 that they had purchased from Playtime, at year end, they had $51,600 of this merchandise in inventory.

Required:

1. Determine the unrealized profit in Salli's inventory at December 31, 2012.

2. Compute Playtime's income from Salli for 2012.

Answer:

Requirement 1

$51,600 - ($51,600 /1.2) =	$ 8,600

Requirement 2

Playtime's share of Salli's income ($460,000 × 90%)	$414,000
Less: Unrealized profit in ending inventory	$8,600
Income from Salli	$405,400

Objective: LO3
Difficulty: Moderate

3) Pirate Transport bought 80% of the outstanding voting stock of Seaways Shipping at book value several years ago. (At the time of purchase, the fair value and book value of Seaways' net assets were equal.) Pirate sells merchandise to Seaways at 120% above Pirate's cost. Intercompany sales from Pirate to Seaways for 2012 were $450,000. Unrealized profits in Seaways' December 31, 2011 inventory and December 31, 2012 inventory were $17,000 and $15,000, respectively. Seaways reported net income of $750,000 for 2012.

Required:

1. Determine Pirate's income from Seaways for 2012.

2. In General Journal format, prepare consolidation working paper entries at December 31, 2012 to eliminate the effects of the intercompany inventory sales assuming the perpetual inventory method is used.

Answer:

Requirement 1

Pirate's Share of Seaways Income ($750,000 × 80%)	$600,000
Less: Profit in Ending Inventory	(15,000)
Add: Profit in Beginning Inventory	17,000
Pirate's Income from Seaways	$602,000

Requirement 2

	Debit	Credit
Sales Revenue	450,000	
Cost of Goods Sold		450,000
To eliminate intercompany sales and cost of goods sold		
Investment in Seaway	17,000	
Cost of Goods Sold		17,000
To recognize previously deferred unrealized profits from the beginning inventory		
Cost of Goods Sold	15,000	
Inventory		15,000
To eliminate intercompany profit in the ending inventory from cost of goods sold and inventory		

Objective: LO3, 4

Difficulty: Moderate

4) Psalm Enterprises owns 90% of the outstanding voting stock of Solomon Siding, which was purchased at a cost equal to 90% of the book value of Solomon's net assets many years ago. (At the time of purchase, the fair value and book value of Solomon's net assets were equal.) Psalm purchases merchandise from Solomon at 110% above Solomon's cost. In 2012, intercompany sales from Solomon to Psalm amounted to $362,000. Unrealized profits in Psalm's December 31, 2011 inventory and December 31, 2012 inventory were $82,000 and $26,000, respectively. Solomon reported net income of $980,000 for 2012.

Required:

1. Determine Psalm's income from Solomon for 2012.

2. In General Journal format, prepare consolidation working paper entries at December 31, 2012 to eliminate the effects of the intercompany inventory sales assuming the perpetual inventory method is used.

Answer:

Requirement 1

Psalm's income from Solomon:

Solomon's separate net income	$ 980,000
Add: Unrealized profit in beginning inventory	82,000
Less: Unrealized profit in ending inventory	(26,000)
Solomon adjusted income	1,036,000
Percentage	90%
Income from Solomon	$ 932,400

Requirement 2

	Debit	Credit
Sales Revenue	362,000	
Cost of Goods Sold		362,000
To eliminate intercompany sales and cost of goods sold		
Investment in Solomon	73,800	
Noncontrolling interest	8,200	
Cost of Goods Sold		82,000
To recognize previously deferred unrealized profits from the beginning inventory		
Cost of Goods Sold	26,000	
Inventory		26,000
To eliminate intercompany profit in the ending inventory from cost of goods sold and inventory		

Objective: LO3, 4

Difficulty: Moderate

5) Pfeifer Corporation acquired an 80% interest in Stern Corporation several years ago when the book values and fair values of Stern's assets and liabilities were equal. At the time of acquisition, the cost of the 80% interest was equal to 80% of the book value of Stern's net assets. Separate company income statements for Pfeifer and Stern for the year ended December 31, 2011 are summarized as follows:

	Pfeifer	Stern
Sales Revenue	$1,000,000	$600,000
Investment income from Stern	85,000	
Cost of Goods Sold	(600,000)	(300,000)
Expenses	(200,000)	(200,000)
Net Income	$285,000	$100,000

During 2010, Pfeifer sold merchandise that cost $120,000 to Stern for $180,000. Half of this merchandise remained in Stern's inventory at December 31, 2010. During 2011, Pfeifer sold merchandise that cost $150,000 to Stern for $225,000. One-third of this merchandise remained in Stern's December 31, 2011 inventory.

Required:
Prepare a consolidated income statement for Pfeifer Corporation and Subsidiary for 2011.
Answer:

Pfeifer Corporation and Subsidiary
Consolidated Income Statement
For the year ended December 31, 2011

Sales (combined $1,600,000 - $225,000 intercompany)	$1,375,000
Cost of Goods Sold (see below)	(670,000)
Expenses	(400,000)
Consolidated net income	305,000
Noncontrolling interest share	(20,000)
Controlling interest share	$ 285,000

Consolidated cost of goods sold computation:	
Combined cost of sales ($600,000 + $300,000)	$900,000
Less: Intercompany sales	(225,000)
Less: Unrealized profit in beginning inventory ($180,000 - $120,000) × 1/2	(30,000)
Add: Unrealized profit in ending inventory ($225,000 - $150,000) × 1/3	25,000
Consolidated Cost of Goods Sold	$ 670,000

Objective: LO3, 4
Difficulty: Moderate

6) Perry Instruments International purchased 75% of the outstanding common stock of Standard Systems in 1997 when the book values and fair values of Standard's assets and liabilities were equal. The cost of Perry's investment was equal to 75% of the book value of Standard's net assets. Separate company income statements for Perry and Standard for the year ended December 31, 2011 are summarized as follows:

	Perry	Standard
Sales Revenue	$2,400,000	$800,000
Investment income from Standard	142,000	
Cost of Goods Sold	(1,600,000)	(400,000)
Expenses	(450,000)	(200,000)
Net Income	$492,000	$200,000

During 2011, the companies began to manage their inventory differently, and worked together to keep their inventories low at each location. In doing so, they agreed to sell inventory to each other as needed at a markup of 10% of cost. Perry sold merchandise that cost $100,000 to Standard for $110,000, and Standard sold inventory that cost $80,000 to Perry for $88,000. Half of this merchandise remained in each company's inventory at December 31, 2011.

Required:
Prepare a consolidated income statement for Perry Corporation and Subsidiary for 2011.
Answer:

Perry Corporation and Subsidiary
Consolidated Income Statement
For the year ended December 31, 2011

Sales (combined $3,200,000 - $198,000 intercompany)	$3,002,000
Cost of Goods Sold (see below)	(1,811,000)
Expenses	(650,000)
Consolidated net income	541,000
Noncontrolling interest share (see below)	(49,000)
Controlling interest share	$492,000

Consolidated cost of goods sold computation:	
Combined cost of sales ($1,600,000 + $400,000)	$2,000,000
Less: Intercompany sales ($110,000 + $88,000)	(198,000)
Add: Unrealized profit in ending inventory ($110,000 - $100,000) × 1/2	5,000
Add: Unrealized profit in ending inventory ($88,000 - $80,000) × 1/2	4,000
Consolidated Cost of Goods Sold	$1,811,000

Noncontrolling interest share calculation:	
Standard separate net income	$200,000
Less: Unrealized profit in ending inventory from upstream sale ($88,000 - $80,000) × 1/2	(4,000)
Standard's adjusted net income	$196,000
Noncontrolling interest share (25%)	$49,000

Objective: LO3, 4

7) Preen Corporation acquired a 60% interest in Shino Corporation at a cost equal to 60% of the book value of Shino's net assets in 2010. At the time of acquisition, the book value and fair value of Shino's assets and liabilities were equal. During 2011, Preen sold $120,000 of merchandise to Shino. All intercompany sales are made at 150% of Preen's cost. Shino's beginning and ending inventories resulting from intercompany sales for 2011 were $60,000 and $36,000, respectively. Income statement information for both companies for 2011 is as follows:

	Preen	Shino
Sales Revenue	$730,000	$262,000
Investment income from Shino	38,000	
Cost of Goods Sold	(319,000)	(172,000)
Expenses	(165,000)	(40,000)
Net Income	$284,000	$50,000

Required:
Prepare a consolidated income statement for Preen Corporation and Subsidiary for 2011.
Answer:

Preen Corporation and Subsidiary
Consolidated Income Statement
For the year ended December 31, 2011

Sales (combined $730,000 + $262,000 - $120,000)	$872,000
Cost of Goods Sold (see below)	(363,000)
Expenses	(205,000)
Consolidated net income	304,000
Noncontrolling interest share ($50,000 × 40%)	(20,000)
Controlling interest share	$284,000

Consolidated cost of goods sold computation:	
Combined cost of sales ($319,000 + $172,000)	$491,000
Less: Intercompany sales	(120,000)
Less: Unrealized profit in beginning inventory ($60,000 — ($60,000/1.5))	(20,000)
Add: Unrealized profit in ending inventory ($36,000 — ($36,000/1.5))	12,000
Consolidated Cost of Goods Sold	$363,000

Objective: LO3, 4
Difficulty: Moderate

8) Pexo Industries purchases the majority of their raw materials from a wholly -owned subsidiary, Springmade Chemicals. Pexo purchased Springmade to assure supply availability at a time when the materials were being rationed in the industry due to supply issues overseas. Pexo was able to purchase Springmade at the book value of Springmade's net assets. At the time of purchase, the book value and fair value of Springmade's net assets were equal. Pexo purchased $2,890,000 of materials from Springmade in 2011 alone. All intercompany sales are made at 120% of cost, although Springmade is able to mark up their products 80% to other outside buyers. Pexo carried inventory on their books at the beginning and end of the year in the amount of $450,000 and $480,000, respectively, all of which had been purchased from Springmade. Income statement information for both companies for 2011 is as follows:

	Pexo	Springmade
Sales Revenue	$3,793,000	$4,441,000
Investment income from Springmade	245,000	
Cost of Goods Sold	(3,139,000)	(3,270,000)
Expenses	(257,000)	(921,000)
Net Income	$642,000	$250,000

Required:
Prepare a consolidated income statement for Pexo Corporation and Subsidiary for 2011.

Answer:

Pexo Corporation and Subsidiary
Consolidated Income Statement
for the year ended December 31, 2011

Sales (combined $3,793,000 + $4,441,000 - $2,890,000)	$ 5,344,000
Cost of Goods Sold (see below)	(3,524,000)
Expenses	(1,178,000)
Consolidated net income	$ 642,000

Consolidated Cost of Goods Sold Computation:	
Combined cost of sales ($3,139,000 + $3,270,000)	$ 6,409,000
Less: Intercompany sales	(2,890,000)
Less: Unrealized profit in beginning inventory ($450,000 - ($450,000/1.2))	(75,000)
Add: Unrealized profit in ending inventory ($480,000 - ($480,000/1.2))	80,000
Consolidated Cost of Goods Sold	$3,524,000

Objective: LO3, 4
Difficulty: Moderate

9) PreBuild Manufacturing acquired 100% of Shoding Industries common stock on January 1, 2010, for $670,000 when the book values of Shoding's assets and liabilities were equal to their fair values and Shoding's stockholders' equity consisted of $380,000 of Capital Stock and $290,000 of Retained Earnings.

PreBuild's separate income (excluding investment income from Shoding) was $870,000, $830,000 and $960,000 in 2010, 2011 and 2012, respectively. PreBuild sold inventory to Shoding during 2010 at a gross profit of $50,000 and 50% remained at Shoding at the end of the year. The remaining 50% was sold in 2011. At the end of 2011, PreBuild has $54,000 of inventory received from Shoding from a sale of $180,000 which cost Shoding $150,000. There are no unrealized profits in the inventory of PreBuild or Shoding at the end of 2012. PreBuild uses the equity method in its separate books. Select financial information for Shoding follows:

	2010	2011	2012
Sales	$890,000	$995,000	$1,020,000
Cost of Sales	(420,000)	(475,000)	(505,000)
Gross Profit	470,000	520,000	515,000
Operating Expenses	(350,000)	(380,000)	(390,000)
Net Income	$120,000	$140,000	$125,000

Required:
Prepare a schedule to determine PreBuild Manufacturing's Consolidated net income for 2010, 2011, and 2012.
Answer:

	2010	2011	2012	
PreBuild's separate income	$870,000	$830,000	$960,000	
Add: Shoding's reported net income	120,000	140,000	125,000	
Unrealized profit in 2010 income	(25,000)	25,000		
Unrealized profit in 2011 income			(9,000)	9,000
Consolidated net income	$965,000	$986,000	$1,094,000	

Objective: LO4
Difficulty: Moderate

10) Peel Corporation acquired a 80% interest in Sitt Corporation at a cost equal to 80% of the book value of Sitt several years ago. At the time of purchase, the fair value and book value of Sitt's assets and liabilities were equal. Sitt purchases its entire inventory from Peel at 150% of Peel's cost. During 2011, Peel sold $190,000 of merchandise to Sitt. Sitt's beginning and ending inventories for 2011 were $72,000 and $66,000, respectively. Income statement information for both companies for 2011 is as follows:

	Peel	Sitt
Sales Revenue	$820,000	$440,000
Investment income from Sitt	146,000	
Cost of Goods Sold	(460,000)	(165,000)
Expenses	(120,000)	(95,000)
Net Income	$386,000	$180,000

Required:
Prepare a consolidated income statement for Peel Corporation and Subsidiary for 2011.

Answer:
Preliminary computations:

Unrealized profit in beginning inventory equals:	
$72,000 - ($72,000/1.5) =	$24,000
Unrealized profit in ending inventory:	
$66,000 - ($66,000/1.5) =	$22,000

Consolidated Net Income Statement:	
Sales (combined $1,260,000 - $190,000 intercompany	$1,070,000
Cost of Goods Sold (see below)	(433,000)
Expenses	(215,000)
Consolidated net income	422,000
Noncontrolling interest share	(36,000)
Controlling interest share	$ 386,000

Consolidated cost of goods sold computation:	
Combined cost of sales ($460,000 + $165,000)	$625,000
Less: Intercompany sales	(190,000)
Less: Unrealized profit in beginning inventory	(24,000)
Add: Unrealized profit in ending inventory	22,000
Consolidated Cost of Goods Sold	$433,000

Objective: LO3, 4
Difficulty: Moderate