**Chapter 13**

**Segment and Interim Reporting**

**Multiple Choice Questions**

 Wakefield Company uses a perpetual inventory system. In August, it sold 2,000 units from its LIFO-base inventory, which had originally cost $35 per unit. The replacement cost is expected to be $45 per unit. The company is planning to reduce its inventory and expects to replace only 1,500 of these units by December 31, the end of its fiscal year. The company replaced 1,500 units in November at an actual cost of $50 per unit.

1. Based on the preceding information, in the entry in August to record the sale of the 2,000 units:
A. Cost of Goods Sold will be debited for $70,000.
B. Inventory will be credited for $85,000.
**C.** Excess of Replacement Cost over LIFO Cost of Inventory Liquidation will be credited for $15,000.
D. Excess of Replacement Cost over LIFO Cost of Inventory Liquidation will be credited for $67,000.

2. Based on the preceding information, in the entry to record the replacement of the 1,500 units in November, Cost of Goods Sold will be debited for:
A. $52,500.
B. $22,500.
C. $15,000.
**D.** $7,500.

3. Based on the preceding information, in the entry to record the replacement of the 1,500 units in November, Inventory will be debited for:
**A.** $52,500.
B. $75,000.
C. $67,500.
D. $60,000.

4. Based on the preceding information, in the entry to record the replacement of the 1,500 units in November, Accounts Payable will be credited for:
A. $67,500.
**B.** $75,000.
C. $62,500.
D. $60,000.

5. Assume that the replacement did not happen in November. In December, the company decided not to replace any of the 1,500 units. The entry required on December 31 to eliminate valuation accounts related to the inventory that will not be replaced will include:
A. a debit to Excess of Replacement Cost over LIFO Cost of Inventory Liquidation for $22,500.
**B.** a credit to Cost of Goods Sold for $15,000.
C. a debit to Inventory for $70,000.
D. a debit to Inventory for $15,000.

6. William Corporation, which has a fiscal year ending January 31, had the following pretax accounting income and estimated effective annual income tax rates for the first three quarters of the year ended January 31, 2008:
 
William's income tax expenses in its interim income statement for the third quarter are:
A. $36,000.
B. $73,500.
**C.** $46,500.
D. $120,000.

7. On June 30, 2008, String Corporation incurred a $220,000 net loss from disposal of a business component. Also, on June 30, 2008, String paid $60,000 for property taxes assessed for the calendar year 2008. What amount of the preceding items should be included in the determination of String's net income or loss for the six-month interim period ended June 30, 2008?
**A.** $250,000
B. $220,000
C. $140,000
D. $280,000

8. Trevor Company discloses supplementary operating segment information for its three reportable segments. Data for 2008 are available as follows:
 
Additional 2008 expenses include indirect operating expenses of $200,000. Appropriately selected common indirect operating expenses are allocated to segments based on the ratio of each segment's sales to total sales. The 2008 operating profit for Segment B was:
A. $180,000
**B.** $120,000
C. $150,000
D. $250,000

9. Trevor Company discloses supplementary operating segment information for its three reportable segments. Data for 2008 are available as follows:
 
Allocable costs for the year was $180,000. Allocable costs are assigned based on the ratio of a segment's income before allocable costs to total income before allocable costs. The 2008 operating profit for Segment B was:
A. $110,000
B. $180,000
C. $126,000
**D.** $120,000

10. Trimester Corporation's revenue for the year ended December 31, 2008, was as follows:
 
Trimester has a reportable operating segment if that segment's revenue exceeds:
**A.** $65,500
B. $60,000
C. $64,500
D. $61,000

11. During the third quarter of 2008, Pride Company sold a piece of equipment at an $8,000
gain. What portion of the gain should Pride report in its income statement for the third
quarter of 2008?
A. $0
B. $2,000
C. $4,000
**D.** $8,000

12. On March 15, 2009, Clarion Company paid property taxes of $60,000 on its factory building for calendar year 2009. On July 1, 2009, Clarion made $40,000 in unanticipated repairs to its machinery. The repairs will benefit operations for the remainder of the calendar year. What total amount of these expenses should be included in Clarion's quarterly income statement for the three months ended September 30, 2009?
A. $55,000
B. $15,000
**C.** $35,000
D. $40,000

 Forge Company, a calendar-year entity, had 6,000 units in its beginning inventory for 2008. On December 31, 2007, the units had been adjusted down to $470 per unit from an actual cost of $510 per unit. It was the lower of cost or market. No additional units were purchased during 2008. The following additional information is provided for 2008:
 
Forge does not have sufficient experience with the seasonal market for its inventory units and assumes that any reductions in market value during the year will be permanent.

13. Based on the preceding information, the cost of goods sold for the first quarter is:
**A.** $636,000
B. $564,000
C. $546,000
D. $624,000

14. Based on the preceding information, the cost of goods sold for the second quarter is:
A. $416,000
B. $364,000
**C.** $304,000
D. $424,000

15. Based on the preceding information, the cost of goods sold for the year 2008, is:
A. $2,080,000
B. $1,880,000
C. $1,835,000
**D.** $1,910,000

16. Samuel Corporation foresees a downturn in its business in the medium term. It expects to sustain an operating loss of $160,000 for the full year ending December 31, 2008. Samuel's tax rate is 35 percent. Anticipated tax credits for 2008 total $8,000. No permanent differences are expected. Realization of the full tax benefit of the expected operating loss and realization of anticipated tax credits are assured beyond any reasonable doubt because they will be carried back. For the first quarter ended March 31, 2008, Samuel reported an operating loss of $30,000. How much of a tax benefit should Samuel report for the interim period ended March 31, 2008?
A. $8,000
**B.** $12,000
C. $13,500
D. $15,500

17. Five of eight internally reported operating segments of Rollins Company qualify under the standards set by FASB 131 for segment reporting. However, the five identified segments do not meet the 75 percent revenue test. FASB 131 prescribes that management:
A. subdivide segments until there are at least 10 reportable segments.
B. consolidate the remaining operating segments and include them under an "all other" category.
**C.** select additional operating segments until the 75% threshold is met.
D. include the heading "corporate headquarters" as an operating segment.

18. Derby Company pays its executives a bonus of 6 percent of income before deducting the bonus and income taxes. For the quarter ended March 31, 2008, Derby had income before the bonus and income tax of $12,000,000. For the year ended December 31, 2008, Derby estimates that its income before bonus and income taxes will be $70,000,000. For the quarter ended March 31, 2008, what is the amount of the bonus that Derby should deduct on its income statement?
A. $4,200,000
**B.** $720,000
C. $1,050,000
D. $180,000

19. In 2006 and 2007, each of Putney Company's four operating segments met one of the three quantitative tests for segment reporting. In 2008, Segment B failed to qualify under the prescribed tests because of abnormal financial conditions. The other three segments qualified for reporting. For 2008, Segment B:
A. should be excluded from segment disclosure but referred to in the management letter to shareholders.
B. should be distinctly separated from the other three segments and listed as a "nonqualifying" segment.
C. should be combined with one of the other three segments and reported.
**D.** should be included in the segment disclosures at the discretion of management.

20. Collins Company reported consolidated revenue of $120,000,000 in 2008. Collins operates in two geographic areas, domestic and Asia. The following information pertains to these two areas:
 
What calculation below is correct to determine if the revenue test is satisfied for the Asian operations?
A. $58,000,000/$140,000,000
**B.** $50,000,000/$120,000,000
C. $58,000,000/$120,000,000
D. $50,000,000/$140,000,000

 An analysis of Abbey Company's operating segments provides the following information:
 

21. Refer to the above information. Which of the operating segments above meet the revenue test?
A. B, D, and E
**B.** A and D
C. A, B, and D
D. B, C, D, and E

22. Refer to the above information. Which of the operating segments above meet the operating profit (loss) test?
**A.** B and E
B. A and B
C. A, B, and E
D. A, B, C, and E

23. Refer to the above information. Which of the operating segments above are reportable segments?
A. B, C, and D
B. A, B, D, and E
C. B, D, and E
**D.** A, B, C, D, and E

24. Crisfield Company has two reportable segments, C and D. Segment C made $4,000,000 of sales to external customers and $400,000 of sales to other operating segments. Segment D, on the other hand, made sales of $8,000,000 to external customers and $1,600,000 of sales to other operating segments. Crisfield Company reported $13,200,000 of revenues on its consolidated income statement. What calculation below correctly determines whether Crisfield Company's reportable segments satisfy the 75% revenue test?
A. $14,000,000/$15,200,000
B. $14,000,000/$13,200,000
**C.** $12,000,000/$13,200,000
D. $12,000,000/$15,200,000

25. Zeus Corporation has determined that it has 15 reportable operating segments. In order to comply with the standard for segment disclosures, Zeus Corporation should do which of the following?
A. Report 10 reportable segments and disclose the remaining 5 segments as other operating segments.
**B.** Report 10 reportable segments by combining the most closely related segments.
C. Report 15 reportable segments as long as the 75 percent revenue test has been satisfied.
D. Report 12 reportable segments and show all other operating segments in a column labeled "Other Operating Segments."

26. FASB 131 requires certain disclosures about major customers. All of the following statements about those disclosures are true with the exception of which statement?
A. The identity of the segment reporting the revenue from a significant customer must be disclosed a footnote.
B. The amount of revenue from a significant customer must be disclosed in a footnote.
**C.** For applying the disclosure test a threshold of 10 percent of total revenues is mandated.
D. A local, state, or foreign government can be considered a major customer.

27. The management approach to the definition of segments for financial reporting expects a company to:
I. Report disaggregated information on the same organizational basis as used by the company's internal decision makers.
II. Report disaggregated information for at least ten segments.
**A.** I
B. II
C. Both I and II
D. Neither I nor II

28. Main Manufacturing Corporation reported consolidated revenues of $50,000,000 on its income statement for 2008. The management of the corporation identified 3 industry segments, M, N, and O. These segments had the following intersegment sales and transfers during 2008:
 
For Main Manufacturing Corporation, the revenue test would be satisfied if any of its industry segments had revenue equal to or greater than which of the following?
A. $7,400,000
**B.** $5,740,000
C. $5,000,000
D. $4,260,000

29. Stone Company reported $100,000,000 of revenues on its 2008 income statement. During the year ended December 31, 2008, Stone made sales of $8,000,000 to external customers in Western Europe. In addition, Stone made sales of $10,000,000 to the U.S. government and $4,000,000 of sales to various state governments. In the footnotes to its financial statements for 2008, in reporting enterprisewide disclosures, Stone is required to disclose:
 
**A.** Option A
B. Option B
C. Option C
D. Option D

30. Tyler Company incurred an inventory loss due to a decline in market prices during its first quarter of operations in 2008. At the end of the first quarter, management of the company believed the decline in market prices to be permanent. In the second quarter, the market prices of Tyler's inventories increased above their acquisition cost. Market prices remained higher than acquisition cost during the remainder of 2008. How should Tyler report the facts above on its first and second quarter income statements?
 
**A.** Option A
B. Option B
C. Option C
D. Option D

31. Denver Company, a calendar-year corporation, had the following actual income before income tax expense and estimated effective annual income tax rates for the first three quarters in 2008:
 
Denver's income tax expense in its interim income statement for the third quarter should be:
A. $126,000.
**B.** $68,400.
C. $62,400.
D. $54,000.

32. **APB Opinion 28** uses which view of interim reporting?
**A.** Integral
B. Discrete
C. Segmental
D. Comprehensive

33. Which of the following observations is true of the discrete view of interim reporting?
A. An interim period is viewed as an installment of an annual period.
B. Recognition and adjustment of certain income or expense items may be affected by judgments about the expected results of the entire year's operations.
**C.** Each interim period is considered as a basic accounting period to be evaluated as if it were an annual accounting period.
D. One interim period would not bear the entire expense that benefits more than one interim period.

34. Mason Company paid its annual property taxes of $240,000 on February 15, 2009. Mason also anticipates that its annual repairs expense for 2009 will be $1,200,000. This amount is usually incurred and paid in July and August when operations are shut down so that machinery and equipment can be repaired. What amount should Mason deduct for property taxes and repairs in each quarter for 2009?
 
A. Option A
**B.** Option B
C. Option C
D. Option D

35. Toledo Imports, a calendar-year corporation, had the following income before tax expense and estimated effective annual income tax rates for the first three quarters in 2008:
 
Toledo's income tax expense in its interim income statement for the nine months ended September 30 and for the third quarter, respectively, are:
A. $250,800 and $103,200.
B. $252,000 and $108,000.
**C.** $252,000 and $103,200.
D. $250,800 and $108,000.

36. Estimated gross profit rates may be used to estimate a company's cost of goods sold and its ending inventory for:
**A.** quarterly but not for annual financial statements.
B. both quarterly and annual financial statements.
C. neither quarterly nor annual financial statements.
D. annual but not for quarterly financial statements.

37. Davis Company uses LIFO for all of its inventories. During its second quarter of 2009, Davis experienced a LIFO liquidation. Davis fully expects to replace the liquidated inventory in the early part of the third quarter. How should Davis report the inventory temporarily liquidated on its income statement for the second quarter?
A. Cost of goods sold for the second quarter should include the acquisition cost of the goods temporarily liquidated.
**B.** Cost of goods sold for the second quarter should include the expected replacement cost of the goods temporarily liquidated.
C. Cost of goods sold for the second quarter should not include the expected replacement cost of the goods temporarily liquidated.
D. Cost of goods sold for the second quarter is not affected by the temporary liquidation of LIFO inventory.

38. How would a company report a change in an accounting principle made on the last day of the third quarter?
**A.** Retrospective application to all pre-change interim periods reported.
B. No change is required.
C. Apply to current and prospective interim periods only.
D. Apply to prospective interim periods only.

39. Missoula Corporation disposed of one of its segments in the second quarter and incurred a gain from disposal of discontinued segment of $600,000, net of taxes. What is the effect of this gain from disposal of discontinued segment?
A. Increase net income from operations for the year by $600,000.
**B.** Increase second quarter net income by $600,000.
C. Increase each quarter's net income by $150,000.
D. Increase each of the last three quarters' net income by $200,000.

40. Frahm Company incurred a first quarter operating loss before income tax effect of $4,000,000. This is a normal occurrence for Frahm because of seasonal fluctuations. Experience has demonstrated the income earned during the remaining quarters far exceeds the first quarter losses each year. Frahm estimates its annual income tax rate will be 30 percent. What net loss should Frahm report for the first quarter?
A. $4,000,000
**B.** $2,800,000
C. $700,000
D. $0

41. The income tax expense applicable to the second quarter's income statement is determined by:
A. dividing the estimated annual income tax expense by four and allocating the amount to the second quarter.
B. multiplying the effective income tax rate times the income before tax for the second quarter.
**C.** subtracting the income tax expense applicable to the first quarter from the income tax expense applicable to the first two quarters.
D. subtracting the income tax liability applicable to the first quarter from the income tax liability applicable to the first two quarters.

42. Which of the following are established by FASB 131 as "enterprisewide disclosure" standards to provide more information about the risks to a company?
I. Information about dominant industry segments.
II. Information about major customers.
III. Information about geographic areas
**A.** Both II and III
B. Both I and III
C. Both I and II
D. I, II, and II

43. FASB 131 uses a(n) \_\_\_\_\_\_ approach to the definition of segments.
A. line of business
B. entity approach
C. portfolio
**D.** management

**Essay Questions**

44. Iona Corporation is in the process of preparing its financial statements for the first quarter of 2009 and has asked your advice as to how to report several items. These items include the following events which took place during the first quarter of 2009 (assume all amounts are material):

1) Iona redeemed bonds with a carrying value of $4,000,000 at a cost of $3,760,000. This early extinguishment occurred because Iona wants to issue new debt at lower interest rates.

2) Iona uses the LIFO method for its inventories. On January 1, 2009, inventories amounted to $10,000,000, while, on March 31, 2009, inventories totaled $9,200,000. Iona expects to replace the liquidated inventory at the beginning of the second quarter at a cost of $1,000,000.

3) Iona changed its depreciation method on $4,000,000 of its delivery trucks from the declining balance method to the straight-line method. On January 1, 2009, accumulated depreciation under the declining balance method was $2,800,000. Had the straight-line method been used, accumulated depreciation on January 1, 2009, would have been $2,300,000. The remaining life of the trucks is two years.

4) Iona pays its top executives a bonus at year-end of 6 percent of operating income before bonus and income taxes. Operating income before bonus and income taxes for the three months ended March 31, 2009, was $10,000,000. Iona estimates that its yearly operating income before bonus and income taxes will be $60,000,000.

5) Iona closes its manufacturing operations in July of each year in order to make its major annual repairs. Iona estimates that the cost of these repairs in 2009 will be $1,000,000.

Required:
For each of the events numbered 1 through 5, indicate how that event should be reported on Iona's income statement for the three months ended March 31, 2009, and the balance sheet accounts effects at March 31, 2009. Ignore income taxes.

1) Iona should report a gain (nonoperating i.e., not extraordinary) from early extinguishment of debt for $240,000 on the income statement. On the balance sheet, long-term debt will be reduced by $4,000,000, retained earnings will increase by $240,000, and cash will be reduced by $3,760,000.

2) Cost of goods sold should be increased by $1,000,000, the expected replacement cost of inventory. This assumes the cost of the liquidated inventory was not part of cost of goods sold. If the cost of the liquidated inventory has been charged to cost of goods sold, then only the difference between the expected replacement cost of $1,000,000 and the cost of the inventory liquidated of $800,000 should be the increase to cost of goods sold. On the balance sheet, inventory should be reported at $9,200,000, and a liability titled "Excess of Replacement Cost Over Lifo Cost of Inventory Liquidated" should be reported at $200,000.

3) The remaining book value of the trucks is $1,200,000 and will be depreciated over two years, accounted for currently and prospectively as a change in estimate. The current annual depreciation expense of $600,000 is allocated quarterly and therefore $150,000 is an operating expense in the first quarter. On the balance sheet, the accumulated depreciation is $2,800,000 (prior) and $150,000 (current) = $2,950,000.

4) The bonus is accrued for the first quarter based upon the income of the quarter, not the estimate of income for the year. Bonus expense is 6% X $10,000,000, or $600,000, for the 1st quarter. On the March 31, 2009, balance sheet, the liability for the accrued bonus would be reported as a current liability of $600,000.

5) Since the repairs benefit the entire year, each quarter is benefited by the repairs made in July. It is correct to use the straight-line method to allocate the repairs in the absence of any other approach. Therefore, 1/4 ($1,000,000), or $250,000, should be charged to repairs expense in the first quarter. On the March 31, 2009, balance sheet, the $250,000 should be disclosed as a current liability and titled "Accrued Repairs Payable."

45. Ridge Company is in the process of determining its reportable segments for the year ended December 31, 2008. As the person responsible for determining this information, you gather the following information:

 

Required:
a) Using the appropriate tests, determine which of the industry segments listed above are reportable for 2008. Show your supporting computations in good form.
b) Indicate whether or not Ridge's reportable segments satisfy the 75 percent test. Show your supporting computations in good form.

 

Conclusions from the tests:

1. Operating segments A, L, and R satisfy the revenue test.
2. Operating segments A, L, R, and Z satisfy the segment profit (loss) test.
3. Operating segments A, R, and Z satisfy the identifiable assets test.

Conclusion:
Segments A, L, R, and Z are reportable segments while segments M and S are not.

b) The 75 percent test is calculated as follows:

 

Conclusion: The 75 percent revenue test is satisfied.

46. Lloyd Corporation reports the following information for 2008 for its three operating segments:
 

 

Indirect operating expenses are allocated to segments based upon the ratio of each segment's traceable operating expenses to total traceable operating expenses. Interest expense is allocated to segments based upon the ratio of each segment's sales to total sales.

Required:
a) Calculate the operating profit or loss for each of the segments for 2008.
b) Determine which segments are reportable, applying the operating profit or loss test.

a) Operating profit or loss for each segment.

 
Note: General corporate expenses are not allocated for the purpose of identifying reportable segments.

b) Reportable segments.

Segments B and C both meet the operating profit or loss test. The absolute dollar amount of their respective operating profit and loss amounts are 10% or more of the absolute dollar amount of the combined segment operating losses of $157,000 ($10,000 loss + $147,000 loss).

47. The information below is for the second quarter of Tampa Company for 2008:

 

Required:
Prepare an interim income statement for the second quarter for Tampa Company. Assume the LIFO liquidation is expected to be restored by the end of 2008.

Income statement for the second quarter for Tampa Company:

 

Note: Cost of sales was $12,400,000 because the LIFO liquidation was expected to be restored by the end of 2008. Gains from early extinguishment of debt are no longer reported as extraordinary items unless material and specifically deemed as such. Income tax expense for the second quarter is calculated on cumulative income before tax for the first two quarters and then net of income tax expense from the first quarter.

48. FASB 131, Disclosure about Segments of an Enterprise and Related Information, has taken what has been referred to as a "management approach" to the definition of a segment and the allocation of costs to a segment.

Required:
a) What is meant by a management approach? How does this concept of a management approach impact the decision to disclose information?
b) How are decisions about cost allocation handled in segment disclosures?

a) FASB 131 focuses on financial information that an enterprise's financial decision makers use to evaluate the entity's operating segments. The information provided about segments should correspond to the internal organization structure used by the chief operating decision maker in deciding how to allocate resources and in assessing performance.
b) FASB 131 stated that the allocations of revenues and costs should be included for a reported segment only if they are included in the segment's profit or loss that the chief operating decision maker uses.

49. FASB has specified a "75% percent consolidated revenue test".

Required:
a) What is the 75% test?
b) How is the 75% test impacted by the "10% Significance Rule"?

a) The total revenue from external sources by all separately reportable operating segments must equal at least 75% of the total consolidated revenue.

b) The reporting entity must identify additional operating segments as reportable until this 75% test is met. The 10% Significance Rule includes segments that have significant intersegment sales. If there are more then ten reportable segments then the segments should be aggregated until 75% of the external revenue is disclosed. An entity does not have to have ten reportable segments.

50. Interim income statements are required for Smith Orchards. Smith does most of its sales in the fall quarter of the year. These sales are both to individual and commercial customers. How do you recommend Smith report sales during the spring quarter of the year?

Smith Orchards should be encouraged to supplement their interim reports with information for the 12-month periods ending at the interim date for both the current and preceding years. This form of disclosure reduces the possibility that users of the reports might make unwarranted inferences about the annual results from an interim report with material seasonal variations.