**Problem 9-10 Contingent Liabilities**

Several items are listed for which the outcome of events is unknown at year-end.

1. A company offers a two-year warranty on sales of new computers. It believes that 4% of the computers will require repairs.
2. The company is involved in a trademark infringement suit. The company’s legal experts believe that an award of $500,000 in the company’s favor will be made.
3. A company is involved in an environmental cleanup lawsuit. The company’s legal counsel believes that the outcome may be unfavorable but has not been able to estimate the costs of the possible loss.
4. A soap manufacturer has included a coupon offer in the Sunday newspaper supplements. The manufacturer estimates that 25% of the 50-cent coupons will be redeemed.
5. A company has been sued by the federal government for price fixing. The company’s legal counsel believes that there will be an unfavorable verdict and has made an estimate of the probable loss.

**Required:**

1. Identify which of the items (a) through (e) should be recorded at year-end.
2. Identify which of the items (a) through (e) should not be recorded but should be disclosed in the year-end financial statements.

**Problem 10-5 Financial Statement Impact of a Lease**

On January 1, 2008, Muske Trucking Company leased a semitractor and trailer for five years. Annual payments of $28,300 are to be made every December 31 beginning December 3, 2008. Interest expense is based on a rate of 8%. The present value of the minimum lease payments is $113,000 and has been determined to be greater than 90% of the fair market value of the asset on January 1, 2008. Muske uses straight-line depreciation on all assets.

**Required:**

1. Prepare a table to show the five year amortization of the lease obligation.
2. Identify and analyze the effect of the lease signing on January 1, 2008.
3. Identify and analyze the effect of all transactions on December 31, 2009 (the second year of the lease).
4. Prepare the balance sheet presentation as of December 31, 2009, for the leased asset and the lease obligation.

**Problem 11-13 Effects of Stockholders’ Equity Transactions on Balance Sheet**

The following transactions occurred at Horton Inc. during its first year of operation.

1. Issued 100,000 shares of common stock at $5 each; 1,000,000 shares are authorized at $1 par value.
2. Issued 10,000 shares of common stock for a building and land. The building was appraised for $20,000, but the value of the land is undeterminable. The stock is selling for $10 on the open market.
3. Purchased 1,000 shares of its own common stock on the open market for $16 per share.
4. Declared a dividend of $0.10 per share on outstanding common stock. The dividend is to be paid after the end of the first year of operations. Market value of the stock is $26.
5. Declared a 2-for-1 stock split. The market value of the stock was $37 before the stock split.
6. Reported $180,000 of income for the year.

**Required:**

1. Identify and analyze the effect of each transaction.
2. Prepare the Stockholders’ Equity section of the balance sheet.
3. Explain the number of shares of stock issued and outstanding at the end of the year.

**Problem 8-8 Capital Expenditures, Depreciation, and Disposal**

Merton Company purchased a building on January 1, 2007, at a cost of $364,000. Morton estimated that the building’s life would be 25 years and the residual value at the end of 25 years would be $14,000.

On January 1, 2008, the company made several expenditures related to the building. The entire building was painted and floors were refinished at a cost of $21,000. A federal agency required Merton to install additional pollution control devices in the building at a cost of $42,000. With the new devices, Merton believed it was possible to extend the life of the building by an additional six years.

In 2007, Merton altered its corporate strategy dramatically. The company sold the building on April 1, 2009, for $392,000 in cash and relocated all operations to another state:

**Required:**

1. Determine the amount of depreciation that should be reflected on the income statement for 2007 and 2008.
2. Explain why the cost of the pollution control equipment was not expensed in 2008. What conditions would have allowed Merton to expense the equipment? If Merton has a choice, would it prefer to expense or capitalize the equipment?
3. What amount of gain or loss did Merton record when it sold the building? What amount of gain or loss would have been reported of the pollution control equipment had been expensed in 2008?

**Problem 9-11 Time Value of Money Concepts**

The following situations involve the application of the time value of money concept.

1. Janelle Carter deposited $9,750 in the bank on January 1, 1991, at an interest rate of 11% compounded annually. How much has accumulated in the account by January 1, 2008?
2. Mike Smith deposited $21,600 in the bank on January 1, 1998. On January 2, 2008, this deposit has accumulated to $42,487. Interest is compounded annually on the account. What rate of interest did Mike earn on the deposit?
3. Lee Spony made a deposit in the bank on January 1, 2001. The bank pays interest at the rate of 8% compounded annually. On January 1, 2008, the deposit has accumulated to $15,000. How much money did Lee originally deposit on January 1, 2001?
4. Nancy Holmes deposited $5,800 in the bank on January 1 a few years ago. The bank pays on interest rate of 10% compounded annually, and the deposit is now worth $15,026. How many years has the deposit been invested?