Question #1 (AICPA.083726FAR-SIM)

Immediately after a note payable was signed, its present value was $30,000. This note and $20,000 cash were used to acquire a used plant asset at the beginning of the current year. The interest rate implied in the note is 6%. Total interest payments due on the note over its term amount to $4,000. The term exceeds one year. No payments on the note are due during the current year. What amount of interest expense is recognized for the first year (current year) on this note, and what amount is capitalized to the plant asset account?

	Interest Expense	Capitalized Amount
☑	$1,800	$50,000

The interest expense recognized for the first year is .06($30,000) = $1,800. Although no interest is paid, interest is accrued, increasing the carrying value of the note. The asset is capitalized at $50,000, the sum of cash down payment and present value of the note. The interest over the note term is not capitalized because it does not assist in the process of placing the asset into its intended condition and location.

	Interest Expense	Capitalized Amount
☐	$3,000	$50,000
☐	$4,000	$30,000
☐	$0	$50,000

Question #2 (AICPA.083725FAR-SIM)

Plant assets are occasionally acquired by means other than by paying cash. Choose the correct statement about such acquisitions.

☐ A. If equipment is acquired with 100% debt financing, the equipment is capitalized at the sum of all interest and principal payments on the debt.

☑ B. If a building is acquired by issuing an amount of stock that is significant in relation to the amount of stock outstanding before the exchange, the fair value of the building should be used to initially debit the building account.

The more objective or readily determinable value is used for recording the building. If the number of shares is significant in relation to the total shares outstanding, the stock price will be affected by the increase in the shares outstanding resulting from the purchase. The more objective value is the appraised value of the building.

☐ C. If land is received by a firm as a donation, no amount should be recorded for the land because there is no cost to the firm.

☐ D. If land is acquired as one component of a group of plant assets for a discounted aggregate price, the amount capitalized for the land is its market value.

Question #3 (AICPA.090629FAR-II-D)

Young Corp. purchased equipment by making a down payment of $4,000 and issuing a note payable for $18,000. A payment of $6,000 is to be made at the end of each year for three years. The applicable rate of interest is 8%. The present value of an ordinary annuity factor for three years at 8% is 2.58, and the present value for the future amount of a single sum of one dollar for three years at 8% is .735. Shipping charges for the equipment were $2,000, and installation charges were $3,500. What is the capitalized cost of the equipment?

☐ A. $19,480

☐ B. $21,480

☑ C. $24,980

The capitalized cost is the sum of the down payment, present value of the note payments, and the shipping and installation charges. $4,000 + $6,000(2.58) $2,000 $3,500 = $24,980. The present value of the three payments required on the note is capitalized, which excludes the interest included in those payments. The two charges are capitalized because they were incurred to place the asset into its intended condition and location.

☐ D. $27,500

Question #4 (AICPA.083724FAR-SIM)

A plant asset under construction by a firm for its own use was completed at the end of the current year. The following costs were incurred:

Materials	$60,000
Labor	30,000
Incremental overhead	10,000
Capitalized interest	20,000

The asset has a service life of 10 years, estimated residual value of $10,000, and will be depreciated under the double declining balance method. At completion, the asset was worth $105,000 at fair value. What amount of depreciation will be recognized on the asset in total over its service life?

☐ A. $105,000

☐ B. $120,000

☑ C. $95,000

The sum of the four listed costs is $120,000, which exceeds fair value of $105,000. Therefore, the asset is capitalized at $105,000, the lesser of the two amounts. Subtracting the $10,000 residual value yields $95,000 depreciable cost-the total depreciation over the life of the asset.

☐ D. $90,000

Question #5 (AICPA.070770FAR)

Oak Co., a newly formed corporation, incurred the following expenditures related to land and building:

County assessment for sewer lines	$ 2,500
Title search fees	625
Cash paid for land with a building to be demolished	135,000
Excavation for construction of basement	21,000
Removal of old building $21,000 less salvage of $5,000	16,000

At what amount should Oak record the land?

☐ A. $138,125

☐ B. $153,500

☑ C. $154,125

The amounts necessary to get the land ready for its intended purpose attach themselves as a part of the total cost of the land. This would be the: $2,500+625+135,000+16,000=$154,125

☐ D. $175,625