

# [Course project, notes to consolidated financial statements](https://assignbuster.com/course-project-notes-to-consolidated-financial-statements/)

[Finance](https://assignbuster.com/essay-subjects/finance/)

Notes to Consolidated Financial Statements Note 1 Business and Summary of Significant Accounting Principles (10 items) Description of Business The Open-Road Motorcycle Company is the largest online retailer of salvage title motorcycles. We are focused on bringing the customer the best value on entry level motorcycles by providing lower prices than our competitors. Our motorcycles are sold all over the United States, and we currently have 30 stores all across the country. Property, Plant and Equipment All property, plant and equipment are stated at cost and depreciated over their useful lives.

All depreciation expense incurred is derived using the straight line method. We do not depreciate our land. We estimate our useful life for our assets accordingly; buildings have a 40 year life, computer equipment has a 5 year life and the repair equipment a 15 year life. The estimated lives of our assets are reviewed periodically to determine if any impairment is present so the useful lives and depreciation can be adjusted for accuracy. Short-term Investments All of our investments are comprised of trading securities comprised of debt instruments in different industries.

The securities are reported at fair value with any unrealized gains and losses stated on net income. Securities that are still held at the end of the fiscal year are evaluated and are adjusted if necessary. Inventory Valuation All of our merchandise on our website is recorded at cost or fair value, whichever is lower. The salvage motorcycle inventory is recorded at cost. We value our inventory using the average method. If the motorcycle is considered “ unsellable”, it becomes disassembled and sold for parts.

All parts received from motorcycles that have been disassembled are not recorded because the cost has already been recorded from the original purchase. The motorcycle would be written off as a loss on net income and all sales from the parts are considered gains and are stated on net income. Refer to Note 2. Costs of Goods Sold Our Costs of goods sold is the cost of the motorcycles purchased, direct labor and depreciation expense. It includes all shipping and handling costs, air freight, train, and truck costs in received the merchandise and or motorcycles. Revenue Recognition

All revenue generated from sales of inventory are realized when it has been earned. Generally when the item purchased arrives and the ownership transfers. All shipping and handling costs are included in the sales price. Revenues earned from sales are stated net of tax. Sales from disassembled motorcycles are listed as gains or losses on net income. Advertising Costs All costs associated with the marketing our website, which include television and internet ads, are expensed when incurred. Typically our advertising costs stay the same every year at $4 million, since our beginning in 2006. Accounts Receivables

We record accounts receivables at net realizable value. This value is the remainder of the amount due on sales on credit less estimated uncollectable amounts. We calculate our estimated amount based on past write-offs. Our company credit policy extends a 30 day period in which the full payment is due upon completion of sale. The item must have a prepayment of at-least 50% of the motorcycle sales price before it is shipped. We believe that because of this policy the amount of uncollectable revenue is reduces and sales have increased. Contingencies Our company is currently involved in a lawsuit pending a settlement agreement.

A former employee was injured in an accident involving improper handling of the shipment. The settlement is considered probable and the estimated cost is $2 million. This amount is stated in current liabilities. Refer to Note 4. Pension and Other Postretirement Benefit Plans Our company contributes to pension and other postretirementhealthcare plans for all of our employees. We contribute 3% of gross wages into a retirement fund specified by each employee. Refer to note 11. Note 2 Inventories Our inventory is comprised of salvaged motorcycles and fully repaired motorcycles.

Inventories are valued at the lower of cost or market. We base our cost on the average cost method. Repaired motorcycles have title and labor costs included in the basis of valuation. Inventories consisted of the following (in millions): December 31, 2011 2010 Salvage motorcycle inventory $ 300 $310 Repaired motorcycle inventory $250 $200

Total inventories $550 $510 Note 3 Property, Plant and Equipment The following table illustrates our property, plant and equipment (in millions): December 31, 2011 2010 Land $ 600 $ 550 Buildings and garages 900 700 Machinery, repair and computers 00 350 1, 900 1, 600 Less: accumulated depreciation 350 300 Property, plant and equipment – net $ 1, 550 $ 1, 300 Note 4 Contingencies and Liabilities

Our company is currently involved in a lawsuit that is pending a settlement. The approximate amount of the settlement is $2 million. We have determined that the contingency is probable and the amount of the settlement is accurate. This amount is stated on the consolidated balance sheet for the current period. Note 5 Changes in Accounting Principles or Estimates We are currently using the average cost method for inventory valuation in place of LIFO.

We have determined this method is more accurate for valuation because prices tend to fluctuate and may skew net income unfavorably. Note 6 Post Balance Sheet Events Our company continually evaluates its motorcycle inventory to determine cost and its ability to sell. If a significant amount of inventory is deemed obsolete or “ unsellable,” it is adjusted in the next period. The amount is deducted from inventory and written off as a loss.

The motorcycles then become disassembled and all revenue generate from the parts are considered a gain. Note 7 Mergers and Acquisitions We recently acquired Pristine Paint Jobs Company during the year for $50 million. We acquired all buildings, land, equipment and certain patents on paint jobs. We have decided to expand our operations by completely restoring salvage motorcycles for a lower price. The following table illustrates the assets and liabilities received from the purchase (in millions):

Cash $ 3 Inventory 10 Equipment 35 Property, plant and Equipment 45 Total assets acquired 93 Accounts payable 40 Long-term debt 40 Total liabilities acquired 80 Total net assets acquired $13 Note 8 Lease Obligations We currently lease a special modification machine that restores the engine and parts to 95%. The lease agreement is based on a 5 year term for $500, 000 a year. The following table illustrates our payments for the term of the lease.

Years ending December 31, Lease Payments 2011 $500, 000 2012 $500, 000 2013 $500, 000 2014 $500, 000 2015 $500, 000 Total cost of the lease $2, 500, 000 Note 9 EPS Our company has 200, 000 shares authorized with 100, 000 outstanding. We have no preferred stock or treasury stock. The following table will illustrate the current and previous earnings per share. 2011 2010

Net Income (in millions) $ 5 $ 4 Number of shares outstanding 100, 000 100, 000 EPS $50 $40 Note 10 Long-Term Debt With the acquisition of Pristine Paint Jobs, we acquired $40 million in long-term debt. Our long term debt prior to the acquisition was $25 million. Our long term debt consists of a $25 million note payable at a fixed interest rate of 1. 5 percent due December 31, 2040.

The following illustrates the long term debts acquired from the purchase of Pristine Paint Jobs. \* $20 million total principal amount of notes due November 20, 2035, at a fixed rate of 1 percent; and \* $20 million total principal amount of notes due November 20, 2035, at a fixed rate of 1. 5 percent. Note 11 Employee Pension Obligations We continue to contribute to employee retirement plans for all of our employees. These pension plans are funded and are based on salaries and years of service. The total contribution for the year is $10 million. In 2010 our total contribution was $9 million. We contribute 3% of employee wages into the plan. The increase in contribution is due to the increase of our workforce.