

Silic case



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Silic should record the one-off, fair-value revaluation as result of its adoption of SIIC tax regime. Because the building was appraised at €12, 500 and originally bought at €10, 000, the firm needs to make a journal entry to account for this increase in value 01/01/2003

- Buildings & Land €2, 500
- Revaluation Surplus €2, 500
- Land & Building = €12, 500 - €10, 000 = €2, 500

As we learned in class from reading Silic's financial statements, 82. % of the unrealized gains from revaluation will flow to the Revaluation Surplus account and 17. 1% will flow to the Other Creditors account.

- €2, 500
- 82. 9% = €2, 072
- €2, 500
- 17. 1% = €428

However, in this particular case, we combine the two accounts for simplicity purposes. On 12/31/2003, Silic need to record a depreciation expense on the building. 12/31/2003 Charge to Depreciation €500 Depreciation & Provisions €500 Revaluation Surplus €100 Consolidated Reserves €100

As given in the question, the depreciation expense is €500.

Silic depreciates its office and buildings on a straight-line basis. We can deduce the useful life of this particular building is 25 years ($€12, 500 / €500 = 25$ years).

The company also needs to amortize the revaluation surplus it originally recorded in response to the fair value revaluation based on the useful life of <https://assignbuster.com/silic-case/>

the building. $\text{€}2,500/25 \text{ years} = \text{€}100$. The amortized amount moved to consolidated reserves (retained earnings). On 01/01/2004, Silic sold the building at $\text{€}12,000$ in cash. 01/01/2004 Cash $\text{€}12,000$ Depreciation & Provisions $\text{€}2,900$ Building & Land $\text{€}12,500$

Gains on Disposal $\text{€}2,400$ Revaluation Surplus $\text{€}2,400$ Consolidated Reserves $\text{€}2,400$

The firm received $\text{€}12,000$ in cash by disposing the asset. The net value of the building was $\text{€}9,600$ ($\text{€}12,500 - \text{€}2,900 = \text{€}9,600$). Thus, the firm sold the building at a gain of $\text{€}2,400$.

In addition, the firm needs to clear the revaluation surplus of this building to zero, and move the amount to consolidated reserves. #2 a) On 12/31/2012, Silic demolishes a fully-depreciated building. It needs to make the journal entry: 12/31/2012

Charge to Depreciation Depreciation and Provision

Depreciation & Provision $\text{€}64,000$ Buildings & Land $\text{€}64,000$ * The firm needs to first record the depreciation expense for the last year of the asset's useful life. The amount cannot be determined by the given information provided in the question. * We also need to clear this particular building from the balance sheet by debiting Depreciation & Provision (contra-asset account) and crediting Building & Land. b) No, this would not produce a faithful representation of Silic's activities for the building. We still need to amortize the revaluation surplus for the last year.

It would not be representational faithful if the remaining value of fair-value mark-up still sits in the Revaluation Surplus account, because the gain is

already realized through the depreciation of the asset. We need to amortize the remaining surplus to consolidated reserves to show the event. Although this journal entry may not necessarily affect the value of total liabilities and equities, we still need to make sure to record this entry to provide investors with most representational faithful information. #3 01/01/2005 Buildings & Land€93, 863 Unrealized Gains on Land and Buildings€93, 863 The number is calculated by subtracting the historical cost of land and buildings on exhibit 4 from the fair value of these assets on exhibit 4b.

€1, 681, 493 - (€1, 139, 063 + €448, 567) = €93, 863 #4 (a) From my point of view, cost accounting method provides more relevant information to investors. According to FAC No. 8 Objectives of Financial Reporting, “relevant financial information is capable of making a difference in the decision made by users”. The two most important characteristics are the information’s predictive value and confirmatory value.

As indicated in the case, Silic primarily competes in the French commercial-property market, which 72% (2004 data) of its earnings was derived from rental properties. As a result, its ordinary course of business centers around its leasing activities, and the fair market value of the properties is not a significant indicator of the company’s performance. Thus, the fluctuation in the value of properties should not materially affect investors’ decision making. Since the 1980s, the commercial property market of Paris and its surrounding region had experienced substantial upward and downward movements in the values of properties.

If we incorporate the change in the fair market value into the computation of net income, Silic’s bottom line would fluctuate significantly each year.

However, the truth is “ the French real estate and property management industry had been growing steadily at an average rate of 2. 8% per year. ” The industry and the company have been on a steady growth trend. Investors would not be able capture the real picture of the operating performance of the company if it switched to fair market accounting of properties.

Therefore, I support the company’s decision of measuring investment property using the cost model. This election provides more relevant information to investors with regards to the company’s operating performance. I think historical cost accounting would present Silic in the most favorable light over time. As I discussed in part , the adoption of IAS no. 40 would require Silic to mark its investment properties to fair value during each reporting period, and report the gains and losses on its income statement.

As indicated in the case, French real estate market had experienced substantial upward and downward movements in the value of properties. Thus, a probable outcome of fair value accounting would be a significant fluctuation in the firm’s bottom line during each reporting period. Fluctuations in net income signals great risk of the financial performance of an entity. A normal risk averse investors would not invest in an company that poses significant risk. Therefore, I believe historical cost accounting would present Silic in the most favorable light over time.