Test bank intermediate accounting ch 17

Accounting and Financial Accountability (Universitas Gadjah Mada)



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CHAPTER 17

INVESTMENTS

TRUE-FALSE—Conceptual

Answer	No.	Description
F	1.	IASB requirements for held-for-collection investments.
T	2.	Classification categories for financial assets.
F	3.	Definition of amortized cost.
F	4.	Reporting debt investments at fair value.
F	5.	Calculation of gain on sale of debt investments.
T	6.	Reporting unrealized holding gain/loss account.
F	7.	Accounting for debt investments using fair value.
T	8.	Using amortized cost or fair value method for debt investment.
T	9.	Using fair value option.
F	10.	Definition of significant influence.
T	11.	Reporting Unrealized Holding Gain/Loss—Equity account.
T	12.	Examples of significant influence.
T	13.	Definition of controlling interest.
T	14.	Effect of dividends on investment under equity.
F	15.	Reporting revenue under fair value method.
T	16.	Definition of controlling interest.
F	17.	Calculation of impairment loss.
T	18.	Accounting for an impaired investment.
F	19.	Transfer between investment classifications.
T	20.	Transfers between categories.

MULTIPLE CHOICE—Conceptual

Answer	No.	Description
c	21.	Identification of financial assets.
b	22.	Valuation of debt investments.
c	23.	Reporting held-to-collection investments.
c	24.	Reporting investments at fair value.
c	25.	Financial assets measurement categories.
b	26.	IFRS measurement requirements for financial assets.
c	27.	Investment accounting approach for held-for-collection investments.
c	S28.	Identifying investments accounted for at amortized cost.
c	29.	Definition of amortized cost.
d	30.	Calculating gain on sale of debt investment.
b	31.	Reporting held for collection investments.
a	32.	Recording amortization of bond premium.
d	33.	Effective-interest rate method.
c	34.	Sale of debt investment prior to maturity.
c	35.	Calculating unrealized holding gain or loss.
c	36.	Accounting for trading investments.
c	37.	Accounting for trading debt investments.
c	38.	Reporting trading debt investments.
c	39.	Valuation of investments in trading debt investments.
c	40.	Differences between amortized cost and fair value methods.

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MULTIPLE CHOICE—Conceptual (cont.)

Answer	No.	Description
c	41.	Fair value option.
d	42.	Reporting changes in fair value.
a	43.	Fair value option.
a	[P]44.	Identifying non-trading investments.
b	[S]45.	Passive interest investment.
b	46.	Reporting unrealized holding gains or losses.
b	47.	Conditions for using the equity method.
d	48.	Ownership interest required for using the consolidation method.
d	49.	Reason equity investments are held.
a	50.	Non-trading equity investments.
a	[S]51.	Fair value vs. equity method.
c	[P]52.	Fair value vs. equity method.
a	53.	Recording of dividends received under the equity method.
d	54.	Recognition of earnings of investee using the equity method.
d	55.	Effect of using the fair value method in error.
d	56.	Accounting for debt investment impairments.
b	57.	Calculation of impairment loss.
c	58.	Calculation of impairment loss on debt investments.
b	59.	Accounting for transfers of debt investments.
b	60.	Transfer of investments between categories.
c	61.	Definition of “gains trading” or “cherry picking”.
b	62.	Accounting for transfers between categories.
c	63.	Transfers of investments between classifications.
a	*64.	Accounting for derivatives.
c	*65.	Characteristics of a derivative instrument.
b	*66.	Identifying companies that are arbitrageurs.
c	*67.	Accounting for fair value hedges.
b	*68.	Gains/losses on cash flow hedges.
a	*69.	Identifying an embedded derivative.

[P] These questions also appear in the Problem-Solving Survival Guide.
[S] These questions also appear in the Study Guide.
*This topic is dealt with in an Appendix to the chapter.

MULTIPLE CHOICE—Computational

Answer	No.	Description
b	70.	Computing cost of bond investment.
d	71.	Calculation of discount amortization.
b	72.	Calculation of revenue from held-for-collection investments.
b	73.	Carrying value of held-to-maturity investments.
c	74.	Carrying value of non-trading debt investments.
a	75.	Calculation of income from non-trading debt investments.
b	76.	Calculation of income from held-for-collection investments.
b	77.	Determine gain on sale of debt investments.
c	78.	Computation of revenue from held-for-collection investment.
a	79.	Calculation of discount amortization.
c	80.	Calculation of revenue from held-for-collection investments.

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MULTIPLE CHOICE—Computational (cont.)

Answer	No.	Description
b	81.	Calculation of interest revenue from held-for-collection investment.
c	82.	Calculation of unrealized gain/loss.
c	83.	Calculation of total income/loss from trading investment.
a	84.	Computation of other comprehensive income.
c	85.	Computation of gain/loss on sale of bonds.
d	86.	Calculation of other comprehensive income.
b	87.	Calculation of loss on sale of bonds.
c	88.	Fair value for debt investment.
d	89.	Calculation of income from trading investment.
a	90.	Calculation of income from trading investment.
b	91.	Calculation of income from non-trading investment.
d	92.	Calculation of loss on sale of trading investment.
b	93.	Determination of unrealized loss on trading investment.
c	94.	Determination of accumulated other comprehensive income.
b	95.	Entry to record unrealized gain on non-trading investments.
c	96.	Fair value for trading investments.
a	97.	Unrealized gain on non-trading investments.
a	98.	Calculation of gain on sale of equity investment.
b	99.	Determination of unrealized loss on non-trading investments.
a	100.	Calculation of unrealized loss included in comprehensive income.
b	101.	Computation of purchase price of equity method investment.
c	102.	Computation of revenue from investment.
c	103.	Computation of investment account balance.
a	104.	Calculation of investment revenue.
c	105.	Accounting for equity investments/fair value method.
b	106.	Accounting for equity investments/equity method.
b	107.	Accounting for equity investments/fair value method.
b	108.	Equity method of accounting.
c	109.	Fair value method of accounting for equity investment.
c	110.	Equity method of accounting for equity investment.
c	111.	Balance of investment account using the equity method.
b	112.	Investment income recognized under the equity method.
c	113.	Balance of investment account using the equity method.
b	114.	Balance of investment account using the equity method.
d	115.	Investment revenue recognized under the equity method.
c	116.	Balance of investment account using the equity method.
a	117.	Calculation of purchase price of equity investment.
b	118.	Recovery of impairment loss.
b	119.	Calculation of impairment loss.
b	120.	Recovery of impairment loss.

MULTIPLE CHOICE—CPA Adapted

Answer	No.	Description
d	121.	Carrying value of non-trading debt investments.
d	122.	Unrealized loss on trading and non-trading investments.
c	123.	Unrealized loss on trading and non-trading investments.
d	124.	Classification of an equity investment.
c	125.	Investment income recognized under the equity method.

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MULTIPLE CHOICE—CPA Adapted (cont.)

Answer	No.	Description
b	126.	Balance of investment account using the equity method.
c	127.	Sale of equity investment.
a	128.	Calculate the acquisition price of an equity investment.

EXERCISES

Item	Description
E17-129	Debt investments.
E17-130	Debt investment purchased at a premium.
E17-131	Debt investment purchased at a discount.
E17-132	Investment in equity securities.
E17-133	Fair value and equity methods (essay).
E17-134	Fair value and equity methods.
E17-135	Impairment.
E17-136	Comprehensive income calculation.
*E17-137	Fair value hedge.
*E17-138	Cash flow hedge.

PROBLEMS

Item	Description
P17-139	Trading equity investments.
P17-140	Trading investments.
P17-141	Non-trading equity investments.
*P17-142	Derivative financial instrument.
*P17-143	Free-standing derivative.

CHAPTER LEARNING OBJECTIVES

1. Describe the accounting framework for financial assets.
2. Understand the accounting for debt investments at amortized cost.
3. Understand the accounting for debt investments at fair value.
4. Describe the accounting for the fair value option.
5. Understand the accounting for equity investments at fair value.
6. Explain the equity method of accounting and compare it to the fair value method for equity investments.
7. Discuss the accounting for impairments of debt investments.
8. Describe the accounting for transfer of investments between categories.
9. Explain who uses derivatives and why.

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*10. Understand the basic guidelines for accounting for derivatives.

*11. Describe the accounting for derivative financial instruments.

*12. Explain how to account for a fair value hedge.

*13. Explain how to account for a cash flow hedge.

*14. Identify special reporting issues related to derivative financial instruments that cause unique accounting problems.

*15. Describe required fair value disclosures.

SUMMARY OF LEARNING OBJECTIVES BY QUESTIONS

Item	Type	Item	Type	Item	Type	Item	Type	Item	Type	Item	Type	Item	Type
Learning Objective 1													
1.	TF	21.	MC	23.	MC	25.	MC	27.	MC				
2.	TF	22.	MC	24.	MC	26.	MC	70.	MC				
Learning Objective 2													
3.	TF	29.	MC	33.	MC	73.	MC	77.	MC	81.	MC	130.	E
4.	TF	30.	MC	34.	MC	74.	MC	78.	MC	82.	MC	131.	E
5.	TF	31.	MC	71.	MC	75.	MC	79.	MC	121.	MC		
S28.	MC	32.	MC	72.	MC	76.	MC	80.	MC	129.	E		
Learning Objective 3													
6.	TF	8.	TF	36.	MC	38.	MC	40.	MC	84.	MC	86.	MC
7.	TF	35.	MC	37.	MC	39.	MC	83.	MC	85.	MC	87.	MC
Learning Objective 4													
9.	TF	41.	MC	42.	MC	43.	MC	P44.	MC	88.	MC		
Learning Objective 5													
10.	TF	S45.	MC	49.	MC	91.	MC	95.	MC	99.	MC	124.	MC
11.	TF	46.	MC	50.	MC	92.	MC	96.	MC	100.	MC	139.	P
12.	TF	47.	MC	89.	MC	93.	MC	97.	MC	122.	MC	140.	P
13.	TF	48.	MC	90.	MC	94.	MC	98.	MC	123.	MC	141.	P
Learning Objective 6													
14.	TF	53.	MC	103.	MC	108.	MC	113.	MC	125.	MC	133.	E
15.	TF	54.	MC	104.	MC	109.	MC	114.	MC	126.	MC	134.	E
16.	TF	55.	MC	105.	MC	110.	MC	115.	MC	127.	MC	136.	E
S51.	MC	101.	MC	106.	MC	111.	MC	116.	MC	128.	MC		
P52.	MC	102.	MC	107.	MC	112.	MC	117.	MC	132.	E		
Learning Objective 7													
17.	TF	56.	MC	58.	MC	119.	MC	135.	E				
18.	TF	57.	MC	118.	MC	120.	MC	140.	P				

Note: TF = True-False
MC = Multiple Choice
E = Exercise
P = Problem

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SUMMARY OF LEARNING OBJECTIVES BY QUESTIONS (cont.)

Learning Objective 8						
19. TF	20. TF	59. MC	60. MC	P61. MC	62. MC	
Learning Objective 9*						
64. MC						
Learning Objective 10*						
65. MC						
Learning Objective 11*						
66. MC	142. P	143. P				
Learning Objective 12*						
67. MC	137. E					
Learning Objective 13*						
68. MC	138. E					
Learning Objective 14*						
69. MC						

Note: TF = True-False
MC = Multiple Choice
E = Exercise
P = Problem

TRUE-FALSE—Conceptual

1. The IASB requires that investments meeting the business model (held-for-collection) and contractual cash flow tests be valued at fair value.

2. The IASB requires that companies classify financial assets into two measurement categories – amortized cost and fair value.

3. Amortized cost is the initial recognition amount of the investment minus cumulative amortization.

4. Companies measure debt investments at fair value if the objective of the company's business model is to hold the financial asset to collect the contractual cash flows.

5. The gain on sale of debt investments is the excess of the selling price over the fair value of the bonds.

6. The Unrealized Holding Gain or Loss–Income account is reported in the other income and expense section of the income statement.

7. At each reporting date, companies adjust debt investments' amortized cost to fair value, with any unrealized holding gain or loss reported as part of their comprehensive income.

8. Over the life of a debt investment, interest revenue and the gain on sale are the same using either amortized cost or fair value measurement.

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9. The fair value option is generally available only at the time a company first purchases the financial asset or incurs a financial liability.

10. Equity security holdings between 20 and 50 percent indicates that the investor has a controlling interest over the investee.

11. The Unrealized Holding Gain/Loss—Equity account is reported as a part of other comprehensive income.

12. Non-trading equity investments are recorded at fair value, with unrealized gains and losses reported in other comprehensive income.

13. An investment of more than 50 percent of the voting stock of an investee should lead to a presumption of significant influence over an investee.

14. All dividends received by an investor from the investee decrease the investment's carrying value under the equity method.

15. Under the fair value method, the investor reports as revenue its share of the net income reported by the investee.

16. A controlling interest occurs when one corporation acquires a voting interest of more than 50 percent in another corporation.

17. An impairment loss is the difference between an investment's cost and the expected future cash flows.

18. If a company determines that an investment is impaired, it writes down the amortized cost basis of the individual security to reflect this loss in value.

19. Companies account for transfers between investment classifications retroactively, at the end of the accounting period after the change in the business model.

20. Transferring an investment from one classification to another should occur only when the business model for managing the investment changes.

True-False Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
1.	F	6.	T	11.	T	16.	T
2.	T	7.	F	12.	T	17.	F
3.	F	8.	T	13.	F	18.	T
4.	F	9.	T	14.	T	19.	F
5.	F	10.	F	15.	F	20.	T

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MULTIPLE CHOICE—Conceptual

21. Which of the following is **not** a financial asset?
    a. Cash
    b. Equity investment
    c. Inventory
    d. Receivables

22. Debt investments not held for collection are reported at
    a. amortized cost.
    b. fair value.
    c. the lower of amortized cost or fair value.
    d. net realizable value.

23. Debt investments that meet the business model and contractual cash flow tests are reported at
    a. net realizable value.
    b. fair value.
    c. amortized cost.
    d. the lower of amortized cost or fair value.

24. Which of the following are reported at fair value?
    a. Debt investments.
    b. Equity investments.
    c. Both debt and equity investments.
    d. None of these answers choices are correct.

25. The IASB permits which of the following measurement categories for financial assets?

	Fair value	Amortized cost
a.	No	No
b.	Yes	No
c.	Yes	Yes
d.	No	Yes

26. IFRS requires companies to measure their financial assets based on all of the following **except**
    a. The company's business model for managing its financial assets.
    b. Whether the financial asset is a debt or equity investment.
    c. The contractual cash flow characteristics of the financial asset.
    d. All of these answer choices are IFRS requirements.

27. Match the investment accounting approach with the correct valuation approach:

	Not held-for-collection	Held-for-collection
a.	Amortized cost	Amortized cost
b.	Fair value	Fair value
c.	Fair value	Amortized cost
d.	Amortized cost	Fair value

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[S]28. Debt investments that are accounted for and reported at amortized cost, are
a. debt investments which are managed and evaluated based on a documented risk-management strategy.
b. trading debt investments.
c. held-for-collection debt investments.
d. All of these answer choices are correct.

29. Amortized cost is the initial recognition amount of the investment minus
a. repayments and net of any reduction for uncollectibility.
b. cumulative amortization and net of any reduction for uncollectibility.
c. repayments plus or minus cumulative amortization and net of any reduction for uncollectibility.
d. repayments plus or minus cumulative amortization.

30. A gain on sale of a debt investment is the excess of the selling price over the bonds
a. market price.
b. fair value.
c. face value.
d. book value.

31. Held-for-collection investments are reported at
a. acquisition cost.
b. amortized cost.
c. maturity value.
d. fair value.

32. A held-for-collection debt investment is purchased at a premium. The entry to record the amortization of the premium includes a
a. Credit to Debt Investments.
b. Credit to Interest Receivable.
c. Credit to Interest Revenue.
d. None of these answers are correct.

33. Which of the following is correct about the effective-interest method of amortization?
a. The effective-interest method applied to debt investments is different from that applied to bonds payable.
b. Amortization of a discount decreases from period to period.
c. Amortization of a premium decreases from period to period.
d. The effective-interest method applies the effective-interest rate to the beginning carrying amount for each interest period.

34. Which of the following is **not** generally correct about recording a sale of a debt investment before maturity date?
a. Accrued interest will be received by the seller even though it is not an interest payment date.
b. An entry must be made to amortize a discount to the date of sale.
c. The entry to amortize a premium to the date of sale includes a debit to Debt investments.
d. A gain on the sale is the excess of the selling price over the book value of the bonds.

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35. An unrealized holding gain or loss on a trading debt investment is the difference between the investment's
    a. fair value and original cost.
    b. face value and amortized cost.
    c. fair value and amortized cost.
    d. face value and original cost.

36. Which of the following is **not** correct in regard to trading investments?
    a. They are held with the intention of selling them in a short period of time.
    b. Unrealized holding gains and losses are reported as part of net income.
    c. Any discount or premium is not amortized.
    d. All of these answer choices are correct.

37. In accounting for debt investments that are classified as trading investments,
    a. any unrealized gain (loss) is reported as part of equity.
    b. a premium is reported separately.
    c. the fair value is compared to amortized cost to compute any unrealized gain (loss).
    d. no discount or premium amortization is required.

38. Investments in trading debt investments are generally reported at
    a. amortized cost.
    b. face value.
    c. fair value.
    d. maturity value.

39. Investments in trading debt investments should be recorded on the date of acquisition at
    a. face value.
    b. fair value.
    c. amortized cost.
    d. the lower of face value or amortized cost.

40. Which of the following statements is true regarding the differences between amortized cost and fair value for debt investments?
    a. When bonds sold at a discount and are accounted for using amortized cost, interest revenue will be greater than the interest revenue recorded under fair value.
    b. When bonds sold at a premium and are accounted for using amortized cost, interest revenue will be less than the interest revenue recorded under fair value.
    c. Under the fair value approach, an unrealized gain or loss is recorded in each year whereas no unrealized gains or losses are recorded under the amortized cost method.
    d. All of these answer choices are correct.

41. Under IFRS, the fair value option
    a. must be applied to all instruments the company holds.
    b. may be selected as a valuation method by the company at any time during the first 2 years of ownership.
    c. reports all gains and losses in income.
    d. All of these answer choices are correct.

42. Under the fair value option, companies report all gains and losses related to changes in fair value in
    a. comprehensive income.
    b. income.
    c. equity.
    d. other comprehensive income.

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43. The fair value option allows a company to
    a. record income when the fair value of its investment increases.
    b. value its debt investments at fair value in some years but not other years.
    c. report most financial instruments at fair value by recording gains and losses as a separate component of stockholders' equity.
    d. All of these answer choices are true of the fair value option.

P44. Equity investments acquired by a corporation which are accounted for by recognizing unrealized holding gains or losses as other comprehensive income and as a separate component of equity are
    a. non-trading where a company has holdings of less than 20%.
    b. trading investments where a company has holdings of less than 20%.
    c investments where a company has holdings of between 20% and 50%.
    d. investments where a company has holdings of more than 50%.

S45. When a company has acquired a "passive interest" in another corporation, the acquiring company should account for the investment
    a. by using the equity method.
    b. by using the fair value method.
    c. by using the effective interest method.
    d. by consolidation.

46. Unrealized holding gains or losses on trading investments are reported in
    a. equity.
    b. net income.
    c. other comprehensive income.
    d. accumulated other comprehensive income.

47. When a company holds between 20% and 50% of the outstanding ordinary shares of an investee, which of the following statements applies?
    a. The investor should always use the equity method to account for its investment.
    b. The investor should use the equity method to account for its investment unless circumstances indicate that it is unable to exercise "significant influence" over the investee.
    c. The investor must use the fair value method unless it can clearly demonstrate the ability to exercise "significant influence" over the investee.
    d. The investor should always use the fair value method to account for its investment.

48. If the investor owns 60% of the investee's outstanding ordinary shares, the investor should generally account for this investment under the
    a. cost method.
    b. fair value method.
    c. consolidation equity method.
    d. consolidation method.

49. Under IFRS, the presumption is that equity investments are

	Held-for-trading	Held to profit from price changes
a.	Yes	No
b.	No	No
c.	No	Yes
d.	Yes	Yes

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50. Under IFRS,
    a. The accounting for non-trading equity investments deviates from the general provisions for equity investments.
    b. Realized gains and losses related to changes in the fair value of non-trading equity investments are reported as a part of other comprehensive income and as a component of other accumulated comprehensive income.
    c. Dividends received in cash are always reported as income on the income statement.
    d. All of hese answer choices are correct.

[S]51. Santo Corporation declares and distributes a cash dividend that is a result of current earnings. How will the receipt of those dividends affect the investment account of the investor under each of the following accounting methods?

	Fair Value Method	Equity Method
a.	No Effect	Decrease
b.	Increase	Decrease
c.	No Effect	No Effect
d.	Decrease	No Effect

[P]52. An investor has a long-term investment in ordinary shares. Regular cash dividends received by the investor are recorded as

	Fair Value Method	Equity Method
a.	Income	Income
b.	A reduction of the investment	A reduction of the investment
c.	Income	A reduction of the investment
d.	A reduction of the investment	Income

53. Koehn Corporation accounts for its investment in the ordinary shares of Sells Company under the equity method. Koehn Corporation should ordinarily record a cash dividend received from Sells as
    a. a reduction of the carrying value of the investment.
    b. share premium.
    c. an addition to the carrying value of the investment.
    d. dividend income.

54. Under the equity method of accounting for investments, an investor recognizes its share of the earnings in the period in which the
    a. investor sells the investment.
    b. investee declares a dividend.
    c. investee pays a dividend.
    d. earnings are reported by the investee in its financial statements.

55. Judd, Inc., owns 35% of Cosby Corporation. During the calendar year 2015, Cosby had net earnings of $300,000 and paid dividends of $30,000. Judd mistakenly recorded these transactions using the fair value method rather than the equity method of accounting. What effect would this have on the investment account, net income, and retained earnings, respectively?
    a. Understate, overstate, overstate
    b. Overstate, understate, understate
    c. Overstate, overstate, overstate
    d. Understate, understate, understate

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56. Impairments of debt investments are
    a. based on discounted contractual cash flows.
    b. recognized as a realized loss if the impairment is judged to be temporary.
    c. based on fair value for non-trading investments and on negotiated values for held-for-collection investments.
    d. evaluated at each reporting date for every held-for-collection investment.

57. An impairment loss is the difference between the recorded investment and the
    a. expected cash flows .
    b. present value of the expected cash flows.
    c. contractual cash flows.
    d. present value of the contractual cash flows.

58. Under IFRS, a company
    a. Should evaluate every investment for impairment.
    b. Accounts for an impairment as an unrealized loss, and includes it as a part of other comprehensive income and as a component of other accumulated comprehensive income until realized.
    c. Calculates the impairment loss on debt investments as the difference between the carrying amount plus accrued interest and the expected future cash flows discounted at the investment's historical effective-interest rate.
    d. All of these answer choices are correct.

59. Royce Company holds a portfolio of debt investments. The debt investments are not held-for-collection but managed to profit from interest rate changes. As a result, it accounts for these investments at fair value. As part of its strategic planning process, completed in the fourth quarter of 2015, Royce management decides to move from its prior strategy—which requires active management—to a held-for-collection strategy for these debt investments. The company will account for this change

	Method	Implementation
a.	Retrospectively	2015
b.	Prospectively	2016
c.	Retrospectively	2016
d.	Prospectively	2015

60. Companies account for transfers of investments between categories
    a. prospectively, at the end of the period after the change in the business model.
    b. prospectively, at the beginning of the period after the change in the business model.
    c. retroactively, at the end of the period after the change in the business model.
    d. retroactively, at the beginning of the period after the change in the business model.

61. "Gains trading" or "cherry picking" involves
    a. moving investments whose value has decreased since acquisition from non-trading to held-for-collection in order to avoid reporting losses.
    b. reporting investments at fair value but liabilities at amortized cost.
    c. selling investments whose value has increased since acquisition while holding those whose value has decreased since acquisition.
    d. All of these answer choices are considered methods of "gains trading" or "cherry picking."

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62. Transfers between categories
    a. result in companies omitting recognition of fair value in the year of the transfer.
    b. are accounted for at fair value for all transfers.
    c. are considered unrealized and unrecognized if transferred out of held-to-maturity into trading.
    d. will always result in an impact on net income.

63. Transfers of investments between classifications are done
    a. at the end of the accounting period.
    b. retroactively.
    c. prospectively.
    d. None of these answer choices are correct.

*64. Companies that attempt to exploit inefficiencies in various derivative markets by attempting to lock in profits by simultaneously entering into transactions in two or more markets are called
    a. arbitrageurs.
    b. gamblers.
    c. hedgers.
    d. speculators.

*65. All of the following statements regarding accounting for derivatives are correct *except* that
    a. they should be recognized in the financial statements as assets and liabilities.
    b. they should be reported at fair value.
    c. gains and losses resulting from speculation should be deferred.
    d. gains and losses resulting from hedge transactions are reported in different ways, depending upon the type of hedge.

*66. All of the following are characteristics of a derivative financial instrument *except* the instrument
    a. has one or more underlyings and an identified payment provision.
    b. requires a large investment at the inception of the contract.
    c. requires or permits net settlement.
    d. All of these answer choices are characteristics.

*67. The accounting for fair value hedges records the derivative at its
    a. amortized cost.
    b. carrying value.
    c. fair value.
    d. historical cost.

*68. Gains or losses on cash flow hedges are
    a. ignored completely.
    b. recorded in equity, as part of other comprehensive income.
    c. reported directly in net income.
    d. reported directly in retained earnings.

*69. An option to convert a convertible bond into ordinay shares is a(n)
    a. embedded derivative.
    b. host security.
    c. hybrid security.
    d. fair value hedge.

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Multiple Choice Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
21.	c	28.	c	35.	c	42.	d	49.	d	56.	d	63.	c
22.	b	29.	c	36.	c	43.	a	50.	a	57.	b	*64.	a
23.	c	30.	d	37.	c	44.	a	51.	a	58.	c	*65.	c
24.	c	31.	b	38.	c	45.	b	52.	c	59.	b	*66.	b
25.	c	32.	a	39.	c	46.	b	53.	a	60.	b	*67.	c
26.	b	33.	d	40.	c	47.	b	54.	d	61.	c	*68.	b
27.	c	34.	c	41.	c	48.	d	55.	d	62.	b	*69.	a

MULTIPLE CHOICE—Computational

70. Kern Company purchased bonds with a face amount of $400,000. Kern purchased the bonds at 102 and paid brokerage costs of $6,000. The amount to record as the cost of this debt investment is
    a. $406,000.
    b. $414,000.
    c. $408,000.
    d. $400,000.

Use the following information for questions 71 and 72.

Patton Company purchased $400,000 of 10% bonds of Scott Co. on January 1, 2016, paying $376,100. The bonds mature January 1, 2026; interest is payable each July 1 and January 1. The discount of $23,900 provides an effective yield of 11%. Patton Company uses the effective-interest method and holds these bonds for collection.

71. On July 1, 2016, Patton Company should increase its Debt Investments account for the Scott Co. bonds by
    a. $2,392.
    b. $1,371.
    c. $1,196.
    d. $686.

72. For the year ended December 31, 2016, Patton Company should report interest revenue from the Scott Co. bonds of:
    a. $42,392.
    b. $41,409.
    c. $41,368.
    d. $40,000.

73. On August 1, 2016, Renfro Co. purchased to hold for collection, 1,000, $1,000, 9% bonds for $940,000 (a 10% effective interest rate). The bonds, which mature on August 1, 2026, pay interest semiannually on February 1 and August 1. Renfro uses the effective interest method of amortization. The bonds should be reported in the December 31, 2016 statement of financial position at a carrying value of
    a. $943,333.
    b. $941,667.

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c. $940,000.
d. $942,000.

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74. On September 1, 2016, Howell Company purchased 600 of the $1,000 face value, 9% bonds of Ramsey, Incorporated, for $625,000 (an 8% effective interest rate). The bonds, which mature on September 1, 2021, pay interest semiannually on March 1 and September 1. Assuming that Howell uses the effective interest method of amortization and that the bonds are appropriately classified as non-trading, the net carrying value of the bonds should be shown on Howell's December 31, 2016, statement of financial position at
    a. $600,000.
    b. $625,000.
    c. $623,667.
    d. $622,333.

75. On July 1, 2016, Horton Co. purchased Lopez, Inc., 10-year, 9%, bonds with a face value of $500,000, for $470,000 (a 10% effective interest rate). Interest is payable semiannually on January 1 and July 1. The bonds mature on July 1, 2026. Horton uses the effective interest method of amortization. Ignoring income taxes, the amount reported in Horton's 2016 income statement as a result of Horton's non-trading investment in Lopez was
    a. $23,500.
    b. $21,150.
    c. $22,500.
    d. $20,000.

76. On October 1, 2016, Menke Co. purchased to hold for collection, 200, $1,000, 9% bonds for $210,000 (an 8% effective interest rate). Interest is paid semiannually on April 1 and October 1 and the bonds mature on October 1, 2017. Menke uses effective interest amortization. Ignoring income taxes, the amount reported in Menke's 2016 income statement from this investment should be
    a. $4,500.
    b. $4,200.
    c. $4,725.
    d. $4,000.

77. During 2014, Hauke Co. purchased 2,000, $1,000, 9% bonds. The carrying value of the bonds at December 31, 2015 was $1,950,000. The bonds mature on March 1, 2015, and pay interest on March 1 and September 1. Hauke sells 1,000 bonds on March 1, 2016, for $980,000, after the interest has been received. Hauke uses effective interest amortization (10% effective interest rate). The gain on the sale is
    a. $0.
    b. $3,750.
    c. $5,000.
    d. $6,250.

78. On January 3, 2016, Moss Co. acquires $100,000 of Adam Company's 10-year, 10% bonds at a price of $106,418 to yield 9%. Interest is payable each December 31. The bonds are classified as held-for-collection. Assuming that Moss Co. uses the effective-interest method, what is the amount of interest revenue that would be recognized in 2016 related to these bonds?
    a. $10,000
    b. $10,642
    c. $9,578
    d. $9,540

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Use the following information for questions 79 and 80.

Carsen Company purchased $200,000 of 10% bonds of Garrison Co. on January 1, 2016, paying $211,950. The bonds mature January 1, 2026; interest is payable each July 1 and January 1. The discount of $11,950 provides an effective yield of 9%. Carsen's objective is to hold the bonds to collect the contractual cash flows. Carsen Company uses the effective interest method.

79. On July 1, 2016, Carsen Company should decrease its Held-for-Collection Debt Investments account for the Garrison Co. bonds by:
    a. $462.
    b. $808.
    c. $924.
    d. $1,598.

80. For the year ended December 31, 2016, Carsen Company should report interest revenue from the Garrison Co. bonds at:
    a. $20,000.
    b. $19,037.
    c. $19,055.
    d. $19,076.

81. Sycamore, Inc. purchased €100,000 of 8 percent bonds of Alvarado Industries on January 1, 2015, at a discount, paying €92,278. The bonds mature January 1, 2020, and yield 10 percent; interest is payable each July 1 and January 1. Sycamore has a business model whose objective is to hold assets in order to collect contractual cash flows and the contractual terms of the financial asset provides specified dates with regard to cash flows that are solely payments of principal and interest. On December 31, 2015, when the market rate of interest is 12%, and the fair value of the bonds is €89,934, Sycamore will record interest revenue of
    a. €5,396
    b. €4,645
    c. €4,497
    d. €4,614

82. Sycamore, Inc. purchased €100,000 of 8 percent bonds of Alvarado Industries on January 1, 2015, at a discount, paying €92,278. The bonds mature January 1, 2020, and yield 10 percent; interest is payable each July 1 and January 1. Sycamore manages and evaluates investment performance on a documented risk-management or investment strategy based on fair value information. On December 31, 2015, when the market rate of interest is 12%, and the fair value of the bonds is €89,934, Sycamore will record an unrealized gain/loss of
    a. €2,344 loss
    b. €2,958 loss
    c. €3,603 loss
    d. €2,958 gain

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83. Bear Co. purchased $500,000 of bonds at par. Bear management has an active trading business model for this investment. At December 31, Bear received annual interest of $20,000, and the fair value of the bonds was $470,400. In Bear Co.'s year-end statement of financial position what amount will be reported for the bond investment and how much total income/loss will be reported on its income statement?

	Statement of financial position	Income statement
a.	$500,000	$20,000
b.	$470,400	$20,000
c.	$470,400	($9,600)
d.	$470,400	$49,600

Use the following information for questions 84 and 85.

Landis Co. purchased $500,000 of 8%, 5-year bonds from Ritter, Inc. on January 1, 2015, with interest payable on July 1 and January 1. The bonds sold for $520,790 at an effective interest rate of 7%. Using the effective-interest method, Landis Co. decreased the non-trading Debt Investments account for the Ritter, Inc. bonds on July 1, 2015 and December 31, 2015 by the amortized premiums of $1,770 and $1,830, respectively.

84. At December 31, 2015, the fair value of the Ritter, Inc. bonds was $530,000. What should Landis Co. report as other comprehensive income and as a separate component of equity?
    a. $12,810.
    b. $9,210.
    c. $3,600.
    d. No entry should be made.

85. At April 1, 2016, Landis Co. sold the Ritter bonds for $515,000. After accruing for interest, the carrying value of the Ritter bonds on April 1, 2016 was $516,875. Assuming Landis Co. has a portfolio of non-trading Debt Investments, what should Landis Co. report as a gain (or loss) on the bonds?
    a. ($14,685).
    b. ($10,935).
    c. ($1,875).
    d. $ 0.

Questions 86 and 87 are based on the following information:

Richman Co. purchased $300,000 of 8%, 5-year bonds from Carlin, Inc. on January 1, 2015, with interest payable on July 1 and January 1. The bonds sold for $312,474 at an effective interest rate of 7%. Using the effective interest method, Richman Co. decreased the non-trading Debt Investments account for the Carlin, Inc. bonds on July 1, 2015 and December 31, 2015 by the amortized premiums of $1,062 and $1,098, respectively.

86. At December 31, 2015, the fair value of the Carlin, Inc. bonds was $318,000. What should Richman Co. report as other comprehensive income and as a separate component of equity?
    a. $0
    b. $2,160
    c. $5,526
    d. $7,686

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87. At February 1, 2016, Richman Co. sold the Carlin bonds for $309,000. After accruing for interest, the carrying value of the Carlin bonds on February 1, 2016 was $310,125. Assuming Richman Co. has a portfolio of non-trading debt securities, what should Richman Co. report as a gain (or loss) on the bonds?
    a. $0.
    b. ($1,125).
    c. ($6,561).
    d. ($8,811).

88. On January 1, 2016, Kam Co. purchases bonds issued by the Central Bank of Midland. Kam purchases debt investments that it plans to manage on a held-for-collection basis (and account for at amortized cost). Kam also manages and evaluates this investment in conjunction with a related liability that is measured at fair value. Kam plans to hold the debt investment until it matures in five years. At December 31, 2016, the amortized cost of this investment is $200,000; its fair value at December 31, 2016, is $226,000. If Kam chooses the fair value option to account for this investment, when must the election be made and at what value will the bond investment be reported on the December 31, 2016 statement of financial position?

	Date	Amount
a.	January 1, 2016	$200,000
b.	December 31, 2016	$200,000
c.	January 1, 2016	$226,000
d.	December 31, 2016	$226,000

89. Polska, Inc. purchased 400 ordinary shares of Millay Manufacturing as a trading investment for £26,400. During the year, Millay Manufacturing paid a cash dividend of £6.50 per share. At year-end, Milay Manufacturing shares were selling for £69 per share. On the income statement for the year ended December 31, what is the total amount of unrealized gain/loss and dividend revenue reported by Polska, Inc.?
    a. £2,600
    b. £1,200
    c. £1,400
    d. £3,800

90. Dumar Corporation purchased 800 ordinary shares of Viking Industries as a trading investment for $14,880. During the year, Viking Industries paid a cash dividend of $3.20 per share. At year-end, Viking's shares were selling for $17.40 per share. On the income statement for the year ended December 31, what is the total amount of unrealized gain/loss and dividend revenue reported by Dumar Corporation?
    a. $1,600
    b. $2,560
    c. $960
    d. $3,250

91. Loire Corporation purchased 1,600 ordinary shares of Comma Co. for $52,800. During the year, Comma paid a cash dividend of $13 per share. At year-end, Comma shares were selling for $38 per share. Loire Corporation purchased the shares to meet a non-trading regulatory requirement. What amount of total income will Loire Corporation report in its income statement for the year?
    a. $-0-
    b. $20,800
    c. $8,000

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d. $28,800

92. During 2016 Logic Company purchased 4,000 shares of Midi, Inc. for $30 per share. The investment was classified as a trading investment. During the year Logic Company sold 1,000 shares of Midi, Inc. for $35 per share. At December 31, 2016 the market price of Midi, Inc.'s shares was $28 per share. What is the total amount of gain/(loss) that Logic Company will report in its income statement for the year ended December 31, 2016 related to its investment in Midi, Inc. shares?
a. ($8,000)
b. $5,000
c. ($3,000)
d. ($1,000)

Use the following information for questions 93 and 94.

Instrument Corp. has the following investments which were held throughout 2015–2016:

		Fair Value	
	Cost	12/31/15	12/31/16
Trading	$300,000	$400,000	$380,000
Non-trading	300,000	320,000	360,000

93. What amount of gain or loss would Instrument Corp. report in its income statement for the year ended December 31, 2016 related to its investments?
a. $20,000 gain.
b. $20,000 loss.
c. $140,000 gain.
d. $80,000 gain.

94. What amount would be reported as accumulated other comprehensive income related to investments in Instrument Corp.'s statement of financial position at December 31, 2015?
a. $40,000 gain.
b. $60,000 gain.
c. $20,000 gain.
d. $120,000 gain.

95. At December 31, 2016, Atlanta Co. has a share portfolio valued at $40,000. Its cost was $33,000. If the Fair Value Adjustment account has a debit balance of $2,000, which of the following journal entries is required at December 31, 2016?

a.	Fair Value Adjustment	7,000	
	Unrealized Holding Gain or Loss–Equity		7,000
b.	Fair Value Adjustment	5,000	
	Unrealized Holding Gain or Loss–Equity		5,000
c.	Unrealized Holding Gain or Loss–Equity	7,000	
	Fair Value Adjustment		7,000
d.	Unrealized Holding Gain or Loss–Equity	5,000	
	Fair Value Adjustment		5,000

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96. Kramer Company's trading investments portfolio which is appropriately included in current assets is as follows:

	December 31, 2016		
	Cost	Fair Value	Unrealized Gain (Loss)
Catlett Corp.	$250,000	$200,000	$(50,000)
Lyman, Inc.	245,000	265,000	20,000
	$495,000	$465,000	$(30,000)

Ignoring income taxes, what amount should be reported as a charge against income in Kramer's 2016 income statement if 2016 is Kramer's first year of operation?
a. $0.
b. $20,000.
c. $30,000.
d. $50,000.

97. On its December 31, 2015, statement of financial position, Trump Co. reported its investment in non-trading securities, which had cost $600,000, at fair value of $550,000. At December 31, 2016, the fair value of the securities was $585,000. What should Trump report on its 2016 income statement as a result of the increase in fair value of the investments in 2016?
a. $0.
b. Unrealized loss of $15,000.
c. Realized gain of $35,000.
d. Unrealized gain of $35,000.

98. During 2015, Woods Company purchased 20,000 ordinary shares of Holmes Corp. common stock for $315,000 as a non-trading investment. The fair value of these shares was $300,000 at December 31, 2015. Woods sold all of the Holmes shares for $17 per share on December 3, 2016, incurring $14,000 in brokerage commissions. Woods Company should report a realized gain on the sale of stock in 2016 of
a. $11,000.
b. $25,000.
c. $26,000.
d. $40,000.

Use the following information for questions 99 and 100.

On its December 31, 2015 statement of financial position, Calhoun Company appropriately reported a $10,000 debit balance in its Fair Value Adjustment account. There was no change during 2016 in the composition of Calhoun's portfolio of equity securities held as non-trading securities. The following information pertains to that portfolio:

Security	Cost	Fair value at 12/31/16
X	$125,000	$160,000
Y	100,000	95,000
Z	175,000	125,000
	$400,000	$380,000

99. What amount of unrealized loss on these securities should be included in Calhoun's equity section of the statement of financial position at December 31, 2016?
a. $30,000.
b. $20,000.
c. $10,000.

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d. $0.

100. The amount of unrealized loss to appear as a component of comprehensive income for the year ending December 31, 2016 is
   a. $30,000.
   b. $20,000.
   c. $10,000.
   d. $0.

101. On January 2, 2016 Pod Company purchased 25% of the outstanding ordinary shares of Jobs, Inc. and subsequently used the equity method to account for the investment. During 2016 Jobs, Inc. reported net income of $420,000 and distributed dividends of $180,000. The ending balance in the Equity Investments account at December 31, 2016 was $320,000 after applying the equity method during 2016. What was the purchase price Pod Company paid for its investment in Jobs, Inc?
   a. $170,000
   b. $260,000
   c. $380,000
   d. $470,000

102. Ziegler Corporation purchased 25,000 ordinary shares of Sherman Corporation for $40 per share on January 2, 2015. Sherman Corporation had 100,000 ordinary shares outstanding during 2016, paid cash dividends of $60,000 during 2016, and reported net income of $200,000 for 2016. Ziegler Corporation should report revenue from investment for 2016 in the amount of
   a. $15,000.
   b. $35,000.
   c. $50,000.
   d. $55,000.

Use the following information for questions 103 and 104.

Harrison Co. owns 20,000 of the 50,000 outstanding ordinary shares of Taylor, Inc. During 2015, Taylor earns $800,000 and pays cash dividends of $640,000.

103. If the beginning balance in the investment account was $500,000, the balance at December 31, 2015 should be
   a. $820,000.
   b. $660,000.
   c. $564,000.
   d. $500,000.

104. Harrison should report investment revenue for 2015 of
   a. $320,000.
   b. $256,000.
   c. $64,000.
   d. $0.

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Use the following information for questions 105 through 108.

The summarized statements of financial position of Goebel Company and Dobbs Company as of December 31, 2015 are as follows:

Goebel Company
Statement of Financial Position
December 31, 2015

Assets	$1,200,000
Liabilities	$ 150,000
Share capital—ordinary	600,000
Retained earnings	450,000
Total equities	$1,200,000

Dobbs Company
Statement of Financial Position
December 31, 2015

Assets	$900,000
Liabilities	$225,000
Share capital—ordinary	555,000
Retained earnings	120,000
Total equities	$900,000

105. If Goebel Company acquired a 20% interest in Dobbs Company on December 31, 2015 for $195,000 and the fair value method of accounting for the investment were used, the amount of the debit to Equity Investments would have been
    a. $135,000.
    b. $111,000.
    c. $195,000.
    d. $180,000.

106. If Goebel Company acquired a 30% interest in Dobbs Company on December 31, 2015 for $225,000 and the equity method of accounting for the investment were used, the amount of the debit to Equity Investments would have been
    a. $285,000.
    b. $225,000.
    c. $180,000.
    d. $202,500.

107. If Goebel Company acquired a 20% interest in Dobbs Company on December 31, 2015 for $135,000 and during 2016 Dobbs Company had net income of $75,000 and paid a cash dividend of $30,000, applying the fair value method would give a debit balance in the Equity Investments account at the end of 2016 of
    a. $111,000.
    b. $135,000.
    c. $150,000.
    d. $144,000.

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108. If Goebel Company acquired a 30% interest in Dobbs Company on December 31, 2015 for $202,500 and during 2016 Dobbs Company had net income of $75,000 and paid a cash dividend of $30,000, applying the equity method would give a debit balance in the Equity Investments account at the end of 2016 of
    a. $202,500.
    b. $216,000.
    c. $225,000.
    d. $217,500.

Use the following information for questions 109 and 110.

Blanco Company purchased 200 of the 1,000 outstanding ordinary shares of Darby Company's for $300,000 on January 2, 2016. During 2016, Darby Company declared dividends of $50,000 and reported earnings for the year of $200,000.

109. If Blanco Company used the fair value method of accounting for its investment in Darby Company, its Equity Investments account on December 31, 2016 should be
    a. $290,000.
    b. $330,000.
    c. $300,000.
    d. $340,000.

110. If Blanco Company uses the equity method of accounting for its investment in Darby Company, its Equity Investments account at December 31, 2016 should be
    a. $290,000.
    b. $300,000.
    c. $330,000.
    d. $340,000.

Use the following information for questions 111 and 112.

Brown Corporation earns $240,000 and pays cash dividends of $80,000 during 2016. Dexter Corporation owns 3,000 of the 10,000 outstanding shares of Brown.

111. What amount should Dexter show in the investment account at December 31, 2016 if the beginning of the year balance in the account was $320,000?
    a. $392,000.
    b. $320,000.
    c. $368,000.
    d. $480,000.

112. How much investment revenue should Dexter report in 2016?
    a. $80,000.
    b. $72,000.
    c. $48,000.
    d. $240,000.

113. Myers Co. acquired a 60% interest in Gannon Corp. on December 31, 2015 for $945,000. During 2016, Gannon had net income of $600,000 and paid cash dividends of $150,000. At December 31, 2016, the balance in the investment account should be
    a. $945,000.
    b. $1,305,000.
    c. $1,215,000.

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d. $1,395,000.

Use the following information for questions 114 and 115.

Tracy Co. owns 4,000 of the 10,000 outstanding ordinary shares of Penn Corp. During 2016, Penn earns $120,000 and pays cash dividends of $40,000.

114. If the beginning balance in the investment account was $240,000, the balance at December 31, 2016 should be
a. $240,000.
b. $272,000.
c. $288,000.
d. $320,000.

115. Tracy should report investment revenue for 2016 of
a. $16,000.
b. $32,000.
c. $40,000.
d. $48,000.

116. Strickland Industries purchased a 30% interest in Spartan, Inc. for $600,000. Spartan, Inc. has 100,000 $10 par value ordinary shares outstanding. This investment enables Strickland to exert significant influence over Spartan. During the year, Spartan earned net income of $360,000 and paid dividends of $120,000; Strickland earned net income of $48,000 and paid dividends of $160,000. At the end of the year, the shares of Spartan were trading on an organized exchange for $22 per share. On Strickland's year-end statement of financial position, its investment in Spartan, Inc. will be valued at
a. $600,000
b. $660,000
c. $672,000
d. $696,000

117. On January 1 2016, Cypress Industries purchased 25% of the ordinary shares of Shane, Inc. The investment enables Cypress to exert significant influence over Shane, Inc. During the year, Shane earned net income of £160,000 and paid dividends of £40,000 and Cypress Industries earned net income of £280,000. At December 31, 2016, shares of Shane, Inc. were trading for £40 per share, and the value in the investment account on the books of Cypress was £395,000. What amount did Cypress Industries pay for its investment in Shane on January 1, 2016?
a. £365,000
b. £425,000
c. £325,000
d. £335,000

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118. At January 1, 2015, Redmond, Inc. has a held-for-collection investment in the bonds of Osborn Company with a carrying (and fair) value of $700,000. During the year, Redmond determined that due to poor economic prospects for Osborn, Redmond will not be able to collect all contractual cash flows and the bonds have decreased in value to $600,000. It is determined that this is a permanent loss in value. During 2016, events and economic conditions have changed such that the impairment loss has decreased (due to an improvement in the debtor's credit rating). The fair value of the bonds is now $708,000. How much, if any, recovery of impairment loss will Redmond, Inc. report on its income statement for the year ending December 31, 2016?
    a. $-0-
    b. $100,000
    c. $108,000
    d. $92,593

119. Quinn, Inc. has a debt investment in the bonds issued by Blake Company. The bonds were purchased at par for €800,000 and, at the end of 2015, have a remaining life of 3 years with annual interest payments at 10%, paid at the end of each year. This debt investment is classified as held-for-collection. Blake is facing a tough economic environment and informs all of its investors that it will be unable to make all payments according to the contractual terms. The controller of Quinn, Inc. has prepared the following revised expected cash flow forecast for this bond investment. All cash flows will take place on December 31. The market rate of interest at December 31, 2015 for investments of similar risk is 12%. What amount of loss, if any, will Quinn, Inc. record on its investment in Blake Company bonds at December 31, 2015?

Cash Flows	
2016	€ 70,000
2017	70,000
2018	770,000
Total cash flows	€ 910,000

Interest factors		
	10%	12%
1 period	.90909	.89286
2 periods	.82645	.79719
3 periods	.75132	.71178

    a. €133,626
    b. €99,996
    c. €90,000
    d. €-0-

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120. At January 2015, Manning, Inc. has a held-for-collection investment in the bonds of Edmond Company with a carrying (and fair) value of $900,000. During the year, Manning determined that due to poor economic prospects for Edmond, Manning will not be able to collect all contractual cash flows and the bonds have decreased in value to $775,000. It is determined that this is a permanent loss in value. During 2016, events and economic conditions have changed such that the impairment loss has decreased (due to an improvement in the debtor's credit rating). The fair value of the bonds is now $910,000. How much, if any, recovery of impairment loss will Manning, Inc. report on its income for the year ending December 31, 2016?
    a. $-0-
    b. $125,000
    c. $135,000
    d. $116,250

Multiple Choice Answers—Computational

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
70.	b	78.	c	86.	d	94.	c	102.	c	110.	c	118.	b
71.	d	79.	a	87.	b	95.	b	103.	c	111.	c	119.	b
72.	b	80.	c	88.	c	96.	c	104.	a	112.	b	*120.	b
73.	b	81.	b	89.	d	97.	a	105.	c	113.	c		
74.	c	82.	c	90.	a	98.	a	106.	b	114.	b		
75.	a	83.	c	91.	b	99.	b	107.	b	115.	d		
76.	b	84.	d	92.	d	100.	a	108.	b	116.	c		
77.	b	85.	c	93.	b	101.	b	109.	c	117.	a		

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MULTIPLE CHOICE—CPA Adapted

121. On July 1, 2016, Wenn Co. purchased 600 of the $1,000 face value, 8% bonds of Loy, Inc., for $630,000 (a 7% effective interest rate). The bonds, which mature on July 1, 2021, pay interest semiannually on January 1 and July 1. Wenn used the effective interest method of amortization and appropriately recorded the bonds as non-trading. On Wenn's December 31, 2016 statement of financial position, the carrying value of the bonds is
a. $630,000.
b. $625,800.
c. $626,100.
d. $628,050.

122. Valet Corp. began operations in 2016. An analysis of Valet's equity investments portfolio acquired in 2016 shows the following totals at December 31, 2016 for trading and non-trading investments:

	Trading Investments	Non-trading Investments
Aggregate cost	$90,000	$110,000
Aggregate fair value	65,000	95,000

What amount should Valet report in its 2016 income statement for unrealized holding loss?
a. $40,000.
b. $10,000.
c. $15,000.
d. $25,000.

123. At December 31, 2016, Jeter Corp. had the following equity investments that were purchased during 2016, its first year of operation:

	Cost	Fair Value	Unrealized Gain (Loss)
Trading Investments:			
Security A	$ 90,000	$ 60,000	$(30,000)
B	15,000	20,000	5,000
Totals	$105,000	$ 80,000	$(25,000)
Non-trading Investments:			
Security Y	$ 70,000	$ 80,000	$ 10,000
Z	85,000	55,000	(30,000)
Totals	$155,000	$135,000	$(20,000)

All market declines are considered temporary. Fair value adjustments at December 31, 2016 should be established with a corresponding charge against

	Income	Equity
a.	$45,000	$ 0
b.	$30,000	$30,000
c.	$25,000	$20,000
d.	$25,000	$ 0

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124. On December 29, 2016, James Co. sold an equity investment that had been purchased on January 4, 2015. James owned no other equity investments. An unrealized holding loss was reported in the 2015 income statement. A realized gain was reported in the 2016 income statement. Was the equity investment classified as non-trading and did its 2015 market price decline exceed its 2016 market price recovery?

	Non-trading	2015 Market Price Decline Exceeded 2016 Market Price Recovery
a.	Yes	Yes
b.	Yes	No
c.	No	Yes
d.	No	No

Use the following information for questions 125 through 127.

Rich, Inc. acquired 30% of Doane Corp.'s ordinary shares on January 1, 2015 for $400,000. During 2015, Doane earned $160,000 and paid dividends of $100,000. Rich's 30% interest in Doane gives Rich the ability to exercise significant influence over Doane's operating and financial policies. During 2016, Doane earned $200,000 and paid dividends of $60,000 on April 1 and $60,000 on October 1. On July 1, 2016, Rich sold half of its shares in Doane for $264,000 cash.

125. Before income taxes, what amount should Rich include in its 2015 income statement as a result of the investment?
   a. $160,000.
   b. $100,000.
   c. $48,000.
   d. $30,000.

126. The carrying amount of this investment in Rich's December 31, 2015 statement of financial position should be
   a. $400,000.
   b. $418,000.
   c. $448,000.
   d. $460,000.

127. What should be the gain on sale of this investment in Rich's 2016 income statement?
   a. $64,000.
   b. $55,000.
   c. $49,000.
   d. $40,000.

128. On January 1, 2016, Reston Co. purchased 25% of Ace Corp.'s ordinary shares; no goodwill resulted from the purchase. Reston appropriately carries this investment at equity and the balance in Reston's investment account was $720,000 at December 31, 2016. Ace reported net income of $450,000 for the year ended December 31, 2016, and paid ordinary share dividends totaling $180,000 during 2016. How much did Reston pay for its 25% interest in Ace?
   a. $652,500.
   b. $765,000.
   c. $787,500.
   d. $877,500.

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Multiple Choice Answers—CPA Adapted

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
121.	d	123.	c	125.	c	127.	c		
122.	d	124.	d	126.	b	128.	a		

DERIVATIONS — Computational

No.	Answer	Derivation
70.	b	($400,000 × 1.02) + $6,000 = $414,000.
71.	d	($376,100 × .055) – ($400,000 × .05) = $686.
72.	b	$376,100 × .055 = $20,686 ($376,100 + $686) × .055 = $20,723; $20,686 + $20,723 = $41,409.
73.	b	[($940,000 × .10 × 5/12) – ($1,000,000 × .09 × 5/12)] = $1,067. $940,000 + $1,067 = $941,667.
74.	c	($600,000 × .09 × 4/12) – ($625,000 × .08 × 4/12) = $1,333 $625,000 – $1,333 = $623,667.
75.	a	[($470,000 × .10 × 6/12) = $23,500.
76.	b	($210,000 × .08 = $4,200.
77.	b	($1,950,000 × .10 × 2/12) – ($2,000,000 × .09 × 2/12) = $2,500 ($1,950,000 + $2,500) ÷ 2 = $976,250; $980,000 – $976,250 = $3,750.
78.	c	($106,418 × .09) = $9,578.
79.	a	($200,000 × .05) – ($211,950 × .045) = $462.
80.	c	($200,000 × .05) + [($211,950 – $462) × .045] = $483. $20,000 – ($462 + $483) = $19,055.
81.	b	(€92,278 × .05) – (€100,000 × .04) = €614 (€92,278 + €614) × .05 = €4,645.
82.	c	(€92,278 × .05) – (€100,000 × .04) = €614 [(€92,278 + €614) × .05] – (€100,000 × .04) = €645 (€92,278 + €614 + €645) – €89,934 = €3,603 loss.
83.	c	($500,000 – $470,400) – $20,000 = ($9,600).
84.	d	
85.	c	$516,875 – $515,000 = $1,875.
86.	d	$318,000 – ($312,474 – $1,062 – $1,098) = $7,686.

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DERIVATIONS — Computational (cont.)

No.	Answer	Derivation
87.	b	$310,125 – $309,000 = $1,125.
88.	c	Fair value option elected at time of purchase; bond investment valued at its fair value.
89.	d	(400 × £6.50) + [(£69 × 400) – £26,400] = £3,800.
90.	a	(800 × $3.20) + [($17.40 × 800) – $14,880] = $1,600.
91.	b	1,600 × $13 = $20,800.
92.	d	[($35 – $30) × 1,000] – [($30 – $28) × 3,000] = ($1,000).
93.	b	$400,000 – $380,000 = $20,000 loss.
94.	c	$320,000 – $300,000 = $20,000 gain.
95.	b	($40,000 – $33,000) – $2,000 = $5,000 unrealized gain.
96.	c	$30,000 (unrealized loss).
97.	a	$0 (non-trading investment).
98.	a	[(20,000 × $17) – $14,000] – $315,000 = $11,000.
99.	b	($400,000 – $380,000) = $20,000.
100.	a	$10,000 + $20,000 = $30,000.
101.	b	X + [($420,000 – $180,000) × .25] = $320,000 X + $60,000 = $320,000 X = $260,000.
102.	c	$200,000 × (25,000 ÷ 100,000) = $50,000.
103.	c	$500,000 + [($800,000 – $640,000) × (20,000 ÷ 50,000)] = $564,000.
104.	a	$800,000 × (20,000 ÷ 50,000) = $320,000.
105.	c	$195,000, acquisition cost.
106.	b	$225,000, acquisition cost.
107.	b	$135,000, acquisition cost.
108.	b	$202,500 + ($75,000 × .3) – ($30,000 × .3) = $216,000.
109.	c	$300,000, acquisition cost.

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DERIVATIONS — Computational (cont.)

No.	Answer	Derivation
110.	c	$300,000 + ($200,000 × .2) – ($50,000 × .2) = $330,000.
111.	c	$320,000 + ($240,000 × .3) – ($80,000 × .3) = $368,000.
112.	b	$240,000 × .3 = $72,000.
113.	c	$945,000 + ($600,000 × .6) – ($150,000 × .6) = $1,215,000.
114.	b	$240,000 + ($120,000 × .4) – ($40,000 × .4) = $272,000.
115.	d	$120,000 × .4 = $48,000.
116.	c	$600,000 + [($360,000 – $120,000) × .30] = $672,000.
117.	a	£395,000 – [(£160,000 – £40,000) × .25] = £365,000.
118.	b	$700,000 – $600,000 = $100,000.
119.	b	(€70,000 × .90909) + (€70,000 × .82645) + (€770,000 × .75132) = €700,004 €800,000 – €700,004 = €99,996.
120.	b	$900,000 – $775,000 = $125,000.

DERIVATIONS — CPA Adapted

No.	Answer	Derivation
121.	d	($600,000 × .04) – ($630,000 × .035) = $1,950. $630,000 – $1,950 = $628,050.
122.	d	$90,000 – $65,000 = $25,000.
123.	c	
124.	d	Conceptual.
125.	c	$160,000 × 30% = $48,000.
126.	b	$400,000 + $48,000 – ($100,000 × 30%) = $418,000.
127.	c	$418,000 – ($60,000 × 30%) + ($200,000 × 50% × 30%) = $430,000. $264,000 – ($430,000 ÷ 2) = $49,000.
128.	a	$720,000 – ($450,000 × 25%) + ($180,000 × 25%) = $652,500.

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EXERCISES

Ex. 17-129—Debt Investments.

On January 1, 2015, Ellison Company purchased 12% bonds, having a maturity value of $800,000, for $860,652. The bonds provide the bondholders with a 10% yield. They are dated January 1, 2015, and mature January 1, 2020, with interest receivable December 31 of each year. Ellison's business model is to hold these bonds to collect contractual cash flows.

Instructions

(a) Prepare the journal entry at the date of the bond purchase.

(b) Prepare a bond amortization schedule through 2016.

(c) Prepare the journal entry to record the interest received and the amortization for 2015.

(d) Prepare any entries necessary at December 31, 2015, using the fair value option, assuming the fair value of the bonds is $860,000.

(e) Prepare any entries necessary at December 31, 2016, using the fair value option, assuming the fair value of the bonds is $840,000.

Solution 17-129

(a)

	January 1, 2015		
Debt Investments		860,652	
Cash			860,652

(b) Schedule of Interest Revenue and Bond Premium Amortization
12% Bonds Sold to Yield 10%

Date	Cash Received	Interest Revenue	Premium Amortized	Carrying Amount of Bonds
1/1/15	—	—	—	$860,652
12/31/15	$96,000	$86,065	$ 9,935	850,717
12/31/16	96,000	85,072	10,928	839,789

(c)

Cash	96,000	
Debt Investments		9,935
Interest Revenue		86,065

(d)

December 31, 2015		
Debt Investments	9,283	
Unrealized Holding Gain or Loss—Income ($860,000 – $850,717)		9,283

(e)

December 31, 2015		
Unrealized Holding Gain or Loss-Income	9,072	
Debt Investments ($849,072 – $840,000)		9,072
Carrying Value at 12/31/15	$860,000	
Amortization	(10,928)	
Carrying Value at 12/31/16	$849,072	

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Ex. 17-130—Debt Investment purchased at a premium.

On January 1, 2015, West Co. purchased $160,000 of 6% bonds for $168,300 (a 5% effective interest rate) as a non-trading investment. Interest is paid on July 1 and January 1 and the bonds mature on January 1, 2020.

Instructions

(a) Prepare the journal entry on January 1, 2015.

(b) The bonds are sold on November 1, 2015 at 105 plus accrued interest. Record amortization and interest revenue on the appropriate dates by the effective-interest method (round to the nearest dollar). Prepare all entries required to properly record the sale.

Solution 17-130

(a)	Debt Investments	168,300	
	Cash		168,300
(b)	Cash ($160,000 × .06 × 1/2)	4,800	
	Interest Revenue ($168,300 × .05 × 1/2)		4,208
	Debt Investments		592
	Interest Receivable ($160,000 x .06 x 1/3)	3,200	
	Interest Revenue (($168,300 - $592) x .05 x 1/3)		2,795
	Debt Investments		405
	Cash (($160,000 × 1.05) + $3,200)	171,200	
	Gain on Sale of Investments		697
	Debt Investments ($168,300 - $592 - $405)		167,303
	Interest Receivable		3,200

Ex. 17-131—Investment purchased at a discount.

On January 1, 2015, Kirmer Corp. purchased $450,000 of 6% bonds, interest payable on January 1 and July 1, for $428,800 (a 7% effective interest rate). The bonds mature on January 1, 2021. Record amortization and interest revenue on the appropriate dates by the effective-interest method (round to the nearest dollar). (Assume bonds are non-trading.)

Instructions

(a) Prepare the entry for January 1, 2015.

(b) The bonds are sold on October 1, 2015 for $427,000 plus accrued interest. Prepare all entries required to properly record the sale.

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Solution 17-131

(a)	Debt Investments	428,800	
	Cash		428,800
(b)	Cash ($450,000 × .6 × 1/2)	13,500	
	Debt Investments	1,480	
	Interest Revenue ($428,800 × .07 × 1/2)		14,980
	Interest Receivable ($450,000 x .06 x ¼)	6,750	
	Debt Investments	780	
	Interest Revenue (($428,800 + $1,480) x .07 x ¼)		7,530
	Cash ($427,000 + 6,750)	433,750	
	Loss on Sale of Investments	4,060	
	Debt Investments ($428,800 + $1,480 + $780)		431,060
	Interest Receivable		6,750

Ex. 17-132—Investment in equity securities.

Agee Corp. acquired a 25% interest in Trent Co. on January 1, 2016, for $500,000. At that time, Trent had 1,000,000 shares of its $1 par common stock issued and outstanding. During 2016, Trent paid cash dividends of $160,000 and thereafter declared and issued a 5% ordinary share dividend when the fair value was $2 per share. Trent's net income for 2016 was $360,000. What is the balance in Agee's investment account at the end of 2016?

Solution 17-132

Cost	$500,000
Share of net income (.25 × $360,000)	90,000
Share of dividends (.25 × $160,000)	(40,000)
Balance in investment account	$550,000

Ex. 17-133—Fair value and equity methods. (Essay)

Compare the fair value and equity methods of accounting for investments in shares subsequent to acquisition.

Solution 17-133

Under the fair value method, investments are originally recorded at cost and are reported at fair value. Dividends are reported as other income and expense. Under the equity method, investments are originally recorded at cost. Subsequently, the investment account is adjusted for the investor's share of the investee's net income or loss and this amount is recognized in the income of the investor. Dividends received from the investee are reductions in the investment account.

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Ex. 17-134—Fair value and equity methods.

Fill in the dollar changes caused in the Investment account and Dividend Revenue or Investment Revenue account by each of the following transactions, assuming Crane Company uses (a) the fair value method and (b) the equity method for accounting for its investments in Hudson Company.

	(a) Fair Value Method		(b) Equity Method	
Transaction	Investment Account	Dividend Revenue	Investment Account	Investment Revenue
1. At the beginning of Year 1, Crane bought 30% of Hudson's ordinary shares at their book value. Total book value of all Hudson's ordinary shares was $800,000 on this date.				
2. During Year 1, Hudson reported $60,000 of net income and paid $30,000 of dividends.				
3. During Year 2, Hudson reported $30,000 of net income and paid $40,000 of dividends.				
4. During Year 3, Hudson reported a net loss of $10,000 and paid $5,000 of dividends.				
5. Indicate the Year 3 ending balance in the Investment account, and cumulative totals for Years 1, 2, and 3 for dividend revenue and investment revenue.				

Solution 17-134

	(a) Fair Value Method		(b) Equity Method	
Transaction	Investment Account	Dividend Revenue	Investment Account	Investment Revenue
1.	240,000		240,000	
2.		9,000	18,000 (9,000)	18,000
3.		12,000	9,000 (12,000)	9,000
4.		1,500	(3,000) (1,500)	(3,000)
5.	240,000	22,500	241,500	24,000

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Ex. 17-135—Impairment.

Bosch Corporation has government bonds classified as held-for-collection at December 31, 2015. These bonds have a par value of $600,000, an amortized cost of $600,000, and a fair value of $555,000. In evaluating the bonds, Bosch determines the bonds have a $45,000 permanent decline in value. That is, the company believes that impairment accounting is now appropriate for these bonds.

Instructions

(a) Prepare the journal entry to recognize the impairment.

(b) What is the new cost basis of the bonds? Given that the maturity value of the bonds is $600,000, should Bosch Corporation amortize the difference between the carrying amount and the maturity value over the life of the bonds?

(c) At December 31, 2016, the fair value of the municipal bonds is $570,000. Prepare the entry (if any) to record this information.

Solution 17-135

(a) The entry to record the impairment is as follows:

Loss on Impairment ($600,000 – $555,000)	45,000	
Debt Investments		45,000

(b) The new cost basis is $555,000. If the bonds are impaired, it is inappropriate to increase (amortize) the asset back up to its original maturity value.

(c)

Debt Investments	15,000	
Recovery of Impairment Loss ($570,000 – $555,000)		15,000

Ex. 17-136—Comprehensive income calculation.

The following information is available for Irwin Company for 2016:

Net Income	$120,000
Realized gain on sale of non-trading investments	10,000
Unrealized holding gain arising during the period on non-trading investments	24,000

Instructions

(1) Determine other comprehensive income for 2016.

(2) Compute comprehensive income for 2016.

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Solution 17-136

(1) 2016 other comprehensive income = $34,000 ($10,000 realized gain + $24,000 unrealized holding gain).

(2) 2016 comprehensive income = $154,000 ($120,000 + $34,000).

***Ex. 17-137**—Fair value hedge.

On January 2, 2016, Tylor Co. issued a 4-year, $500,000 note at 6% fixed interest, interest payable semiannually. Tylor now wants to change the note to a variable rate note. As a result, on January 2, 2016, Tylor Co. enters into an interest rate swap where it agrees to receive 6% fixed and pay LIBOR of 5.6% for the first 6 months on $500,000. At each 6-month period, the variable interest rate will be reset. The variable rate is reset to 6.6% on June 30, 2016.

Instructions

(a) Compute the net interest expense to be reported for this note and related swap transaction as of June 30, 2016.

(b) Compute the net interest expense to be reported for this note and related swap transaction as of December 31, 2016.

***Solution 17-137**

(a) and (b)

	6/30/16	12/31/16
Fixed-rate debt	$500,000	$500,000
Fixed rate (6% ÷ 2)	X 3%	X 3%
Semiannual debt payment	$ 15,000	$ 15,000
Swap fixed receipt	(15,000)	(15,000)
Net income effect	$ 0	$ 0
Swap variable rate		
5.6% × ½ × $500,000	$ 14,000	
6.6% × ½ × $500,000	0	$ 16,500
Net interest expense	$ 14,000	$ 16,500

***Ex. 17-138**—Cash flow hedge.

On January 2, 2015, Sloan Company issued a 5-year, $8,000,000 note at LIBOR with interest paid annually. The variable rate is reset at the end of each year. The LIBOR rate for the first year is 6.8%

Sloan Company decides it prefers fixed-rate financing and wants to lock in a rate of 6%. As a result, Sloan enters into an interest rate swap to pay 7% fixed and receive LIBOR based on $8 million. The variable rate is reset to 7.4% on January 2, 2016.

Instructions

(a) Compute the net interest expense to be reported for this note and related swap transactions as of December 31, 2015.

(b) Compute the net interest expense to be reported for this note and related swap transactions as of December 31, 2016.

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***Solution 17-138**

(a) and (b)

	12/31/15	12/31/16
Variable-rate debt	$8,000,000	$8,000,000
Variable rate	X 6.8%	X 7.4%
Debt payment	$ 544,000	$ 592,000
Debt payment	$ 544,000	$ 592,000
Swap receive variable	(544,000)	(592,000)
Net income effect	$ 0	$ 0
Swap payable—fixed	560,000	560,000
Net interest expense	$ 560,000	$ 560,000

PROBLEMS

Pr. 17-139—Trading equity investments.

Korman Company has the following securities in its portfolio of trading equity investments on December 31, 2015:

	Cost	Fair Value
5,000 ordinary shares of Thomas Corp.	$155,000	$139,000
10,000 ordinary shares of Gant	182,000	190,000
	$337,000	$329,000

All of the investments had been purchased in 2015. In 2016, Korman completed the following investment transactions:

March 1 Sold 5,000 ordinary shares of Thomas Corp., @ $31 less fees of $1,500.
April 1 Bought 600 ordinary shares of Werth Stores, @ $45 plus fees of $550.

The Korman Company portfolio of trading equity investments appeared as follows on December 31, 2016:

	Cost	Fair Value
10,000 ordinary shares of Gant	$182,000	$195,500
600 ordinary shares of Werth Stores	27,550	25,500
	$209,550	$221,000

Instructions
Prepare the general journal entries for Korman Company for:
(a) the 2015 adjusting entry.
(b) the sale of the Thomas Corp. shares.
(c) the purchase of the Werth Stores' shares.
(d) the 2016 adjusting entry.

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Solution 17-139

(a)	12-31-15		
	Unrealized Holding Gain or Loss—Income	8,000	
	Fair Value Adjustment		8,000
	($337,000 – $329,000)		
(b)	3-1-16		
	Cash [(5,000 × $31) – $1,500]	153,500	
	Loss on Sale of Investments	1,500	
	Equity Investment		155,000
(c)	4-1-16		
	Equity Investments	27,550	
	Cash [(600 × $45) + $550]		27,550
(d)	12-31-16		
	Fair Value Adjustment	19,450	
	Unrealized Holding Gain or Loss—Income		19,450
	[($221,000 – $209,550) + $8,000]		

Pr. 17-140—Trading equity investments.

Perez Company began operations in 2014. Since then, it has reported the following gains and losses for its investments in trading securities on the income statement:

	2014	2015	2016
Gains (losses) from sale of trading investments	$ 15,000	$(20,000)	$ 14,000
Unrealized holding losses on valuation of trading investments	(25,000)	—	(30,000)
Unrealized holding gain on valuation of trading investments	—	10,000	—

At January 1, 2017, Perez owned the following trading securities:

	Cost
BKD Ordinary (15,000 shares)	$450,000
LRF Preference (2,000 shares)	210,000
Drake Convertible bonds (100 bonds)	115,000

During 2017, the following events occurred:
1. Sold 5,000 shares of BKD for $170,000.
2. Acquired 1,000 ordinary shares of Horton for $40 per share. Brokerage fees totaled $1,000.

At 12/31/17, the fair values for Perez's trading investments were:
BKD Ordinary, $28 per share
LRF Preference, $110 per share
Drake Bonds, $1,020 per bond
Horton Ordinary, $42 per share

Instructions
(a) Prepare a schedule which shows the balance in the Fair Value Adjustment at December 31, 2016 (after the adjusting entry for 2016 is made).
(b) Prepare a schedule which shows the aggregate cost and fair values for Perez's trading investments portfolio at 12/31/17.

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(c) Prepare the necessary adjusting entry based upon your analysis in (b) above.

Solution 17-140

(a)	Balance 12/31/14 (result of that year's adjusting entry)	$(25,000)
	Deduct unrealized gain for 2015	10,000
	Add: Unrealized loss for 2016	(30,000)
	Balance at 12/31/16	$(45,000)

(b) Aggregate cost and fair value for trading securities at 12/31/17:

	Cost	Fair Value
BKD Ordinary 10,000 shares	$300,000	$280,000
LRF Preference 2,000 shares	210,000	220,000
Horton Ordinary, 1,000 shares	41,000	42,000
Drake Bonds, 100 bonds	115,000	102,000
Total	$666,000	$644,000

(c) Adjusting entry at 12/31/17:

Fair Value Adjustment		23,000	
Unrealized Holding Gain or Loss—Income			23,000
(Balance at 1/1/17	$45,000		
Balance needed at 12/31/17	22,000		
Recovery	$23,000)		

Pr. 17-141—Non-trading equity investments.

During the course of your examination of the financial statements of Doppler Corporation for the year ended December 31, 2016, you found a new account, "Investments." Your examination revealed that during 2016, Doppler began a program of investments, and all investment-related transactions were entered in this account. Your analysis of this account for 2016 follows:

Doppler Corporation
Analysis of Investments
For the Year Ended December 31, 2016

Date—2016		Debit	Credit
	(a)		
	Harmon Company Ordinary Shares		
Feb. 14	Purchased 4,000 shares @ $55 per share.	$220,000	
July 26	Received 400 ordinary shares of Harmon Company as a share dividend. (Memorandum entry in general ledger.)		
Sept. 28	Sold the 400 ordinary shares of Harmon Company received July 26 @ $70 per share.		$28,000
	(b)		
		Debit	Credit
	Taber Inc., Ordinary Shares		
Apr. 30	Purchased 20,000 shares @ $40 per share.	$800,000	
Oct. 28	Received dividend of $1.20 per share.		$24,000

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Pr. 17-141 (cont.)

Additional information:

1. The fair value for each security as of the 2016 date of each transaction follow:

Security	Feb. 14	Apr. 30	July 26	Sept. 28	Dec. 31
Harmon Co.	$55		$62	$70	$74
Taber Inc.		$40			32
Doppler Corp.	25	28	30	33	35

2. All of the investments of Doppler are nominal in respect to percentage of ownership (5% or less).

3. Each investment is considered by Doppler's management to be non-trading.

Instructions

(1) Prepare any necessary correcting journal entries related to investments (a) and (b).

(2) Prepare the entry, if necessary, to record the proper valuation of the non-trading equity investment portfolio as of December 31, 2016.

Solution 17-141

(1) (a) Harmon — original purchase 4,000 shares
share dividend 400 shares
total holding 4,400 shares

Total cost of $220,000 ÷ Total shares of 4,400 = $50 cost per share

Sold 400 shares

Correct entry:

Cash (400 × $70)	28,000	
Equity Investments (400 × $50)		20,000
Gain on Sale of Investments		8,000

Entry made:

Cash	28,000	
Equity Investments		28,000

Correction:

Equity Investments	8,000	
Gain on Sale of Investments		8,000

(b) Taber—should record cash dividend as dividend income.

Correct entry:

Cash	24,000	
Dividend Revenue		24,000

Entry made:

Cash	24,000	
Equity Investments		24,000

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Solution 17-141 (cont.)

Correction:

Equity Investments	24,000	
Dividend Revenue		24,000
(To properly record dividends under fair value method)		

(2) Valuation at End of Year:

	Quantity	Cost	Fair Value	Increase (Decrease)
Harmon	4,000 shares	$ 200,000	$296,000	$ 96,000
Taber	20,000 shares	800,000	640,000	(160,000)
		$1,000,000	$936,000	$ (64,000)

Year-end Adjustment:

Unrealized Holding Gain or Loss—Equity	64,000	
Fair Value Adjustment		64,000

***Pr. 17-142**—Derivative financial instrument.

Hummel Co. purchased a put option on Olney ordinary shares on July 7, 2015, for $100. The put option is for 200 shares, and the strike price is $30. The option expires on January 31, 2016. The following data are available with respect to the put option:

Date	Market Price of Olney Shares	Time Value of Put Option
September 30, 2015	$32 per share	$53
December 31, 2015	$31 per share	21
January 31, 2016	$33 per share	0

Instructions

Prepare the journal entries for Hummel Co. for the following dates:

(a) July 7, 2015—Investment in put option on Olney shares.

(b) September 30, 2015— Hummel prepares financial statements.

(c) December 31, 2015— Hummel prepares financial statements.

(d) January 31, 2016—Put option expires.

***Solution 17-142**

July 7, 2015

(a)	Put Option	100	
	Cash		100

September 30, 2015

(b)	Unrealized Holding Gain or Loss—Income	47	
	Put Option ($100 – $53)		47

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Solution 17-142 (cont.)

	December 31, 2015		
(c)	Unrealized Holding Gain or Loss—Income	32	
	Put Option ($53 – $21)		32
	January 31, 2016		
(d)	Loss on Settlement of Put Option	21	
	Put Option ($21 – $0)		21

***Pr. 17-143**—Free-standing derivative.

Welch Co. purchased a put option on Reese ordinary shares on January 7, 2016, for $215. The put option is for 300 shares, and the strike price is $51. The option expires on July 31, 2016. The following data are available with respect to the put option:

Date	Market Price of Reese Shares	Time Value of Put Option
March 31, 2016	$48 per share	$120
June 30, 2016	$50 per share	54
July 6, 2016	$46 per share	16

Instructions

Prepare the journal entries for Welch Co. for the following dates:

(a) January 7, 2016—Investment in put option on Reese shares.

(c) March 31, 2016— Welch prepares financial statements.

(d) June 30, 2016— Welch prepares financial statements.

(e) July 6, 2016— Welch settles the call option on the Reese shares.

***Solution 17-143**

	January 7, 2016		
(a)	Put Option	215	
	Cash		215
	March 31, 2016		
(b)	Put Option	900	
	Unrealized Holding Gain or Loss—Income ($3 × 300)		900
	Unrealized Holding Gain or Loss—Income	95	
	Put Option ($215 – $120)		95
	June 30, 2016		
(c)	Unrealized Holding Gain or Loss—Income	600	
	Put Option ($2 × 300)		600
	Unrealized Holding Gain or Loss—Income	66	
	Put Option ($120 – $54)		66

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Solution 17-143 (cont.)

		July 6, 2016	
(d)	Unrealized Holding Gain or Loss—Income	38	
	Put Option ($54 – $16)		38
	Cash (300 × $5)	1,500	
	Gain on Settlement of Put Option		1,184
	Put Option*		316

*Value of Put Option settlement:

Put Option	
215	
900	95
	600
	66
	38
316	

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