Intermediate accounting 17th edition answer key

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CHAPTER 19

Accounting for Income Taxes

ASSIGNMENT CLASSIFICATION TABLE (BY TOPIC)

Topics	Questions	Brief Exercises	Exercises	Problems	Concepts for Analysis
1. Reconcile pretax financial income with taxable income.	1, 13		1, 2, 3, 4, 5, 12, 18, 20, 21	1, 2, 3, 4, 8	
2. Identify temporary and permanent differences.	3, 4, 5		4, 5, 6, 7	2, 3, 4	3, 4, 5
3. Determine deferred income taxes and related items—single tax rate.	6, 7, 13	1, 2, 3, 4, 5, 6, 7, 9	1, 3, 4, 5, 7, 8, 12, 14, 15, 19, 21	3, 4, 8, 9	2
4. Classification of deferred taxes.	10, 11, 12	15	7, 11, 16, 18, 19, 20, 21, 22	3, 6	2, 3, 5
5. Determine deferred income taxes and related items—multiple tax rates, expected future income.		10	2, 13, 16, 17, 18, 20, 22	1, 2, 6, 7	1, 6, 7
6. Determine deferred taxes, multiple rates, expected future losses.		10			
7. Carryback and carryforward of NOL.	16, 17, 18,	12, 13, 14	9, 10, 23, 24, 25	5	
8. Change in enacted future tax rate.	14	11	16	2, 7	5, 6
9. Tracking temporary differences through reversal.			8, 17	2, 7	
10. Income statement presentation.	9	8	1, 2, 3, 4, 5, 7, 10, 12, 16, 19, 23, 24, 25	1, 2, 3, 5, 7, 8, 9	
11. Conceptual issues—tax allocation.	1, 2, 8, 19		7		1, 2, 7
12. Valuation allowance—deferred tax asset.	8, 19	7	7, 14, 15, 23, 24, 25		
13. Disclosure and other issues.	15				

101: Cash

Date	Debit	Credit	Balance
Mar 1 ✓	150,000✓		150,000
Mar 2 ✓		6,000✓	144,000
Mar 6 ✓	4,000✓		148,000
Mar 12 ✓		4,200✓	143,800
Mar 19 ✓		5,000✓	138,800
Mar 22 ✓	3,500✓		142,300
Mar 29 ✓		5,100✓	137,200
Mar 31 ✓		500✓	136,700

106: Accounts Receivable

Date	Debit	Credit	Balance
Mar 9 ✓	7,500✓		7,500
Mar 22 ✓		3,500✓	4,000
Mar 25 ✓	3,820✓		7,820

124: Office Supplies

Date	Debit	Credit	Balance
Mar 3 ✓	1,200✓		1,200
Mar 30 ✓	600✓		1,800

128: Prepaid Insurance

Date	Debit	Credit	Balance
Mar 19 ✓	5,000✓		5,000

131: Prepaid Rent

Date	Debit	Credit	Balance
Mar 2 ✓	6,000✓		6,000

163: Office Equipment

Date	Debit	Credit	Balance
Mar 1 ✓	22,000✓		22,000
Mar 3 ✓	3,000✓		25,000

201: Accounts Payable

Date	Debit	Credit	Balance
Mar 3 ✓		4,200✓	4,200
Mar 12 ✓	4,200✓		0
Mar 30 ✓		600✓	600

307: Common Stock

Date	Debit	Credit	Balance
Mar 1 ✓		172,000✓	172,000

319: Dividends

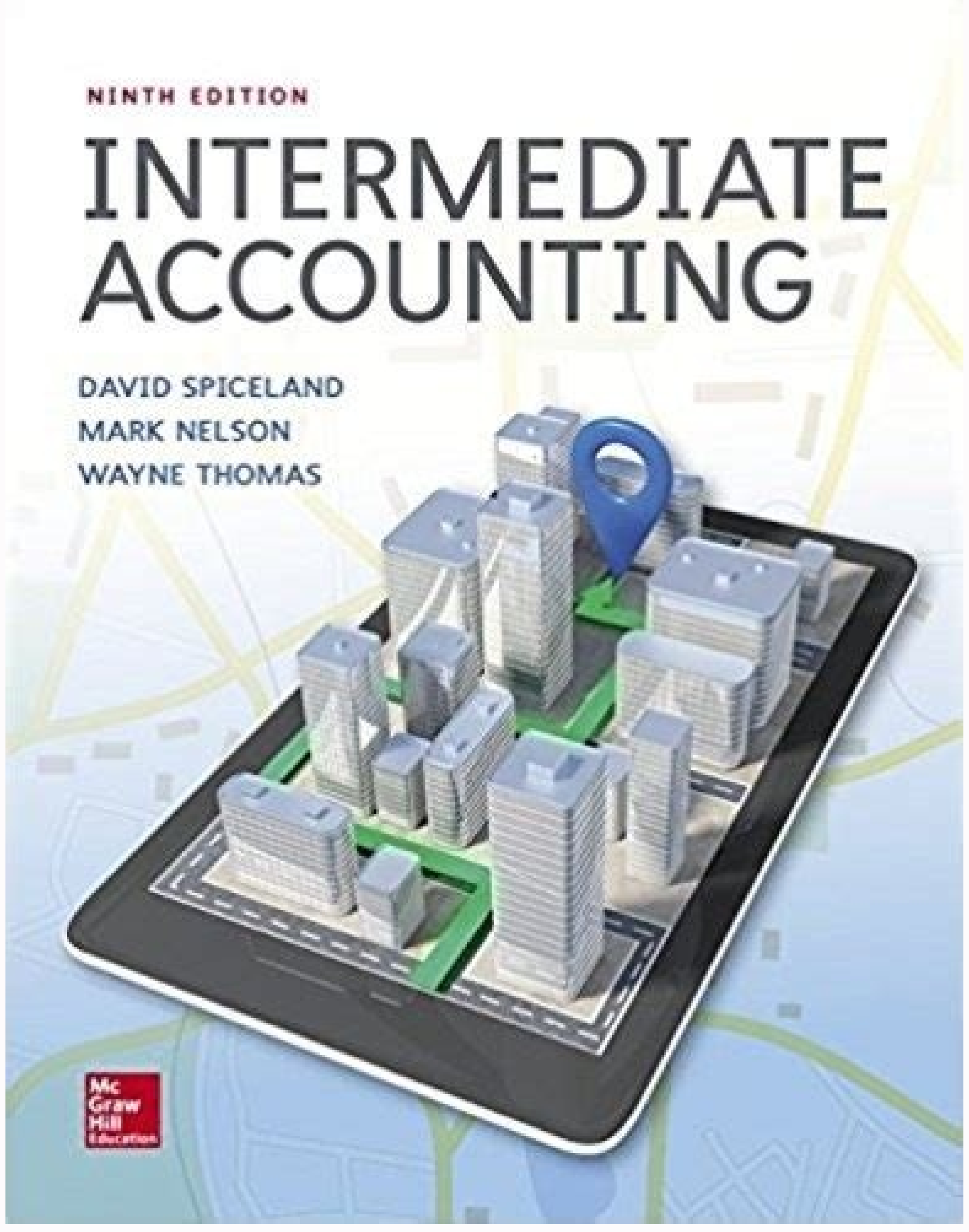
Date	Debit	Credit	Balance
Mar 29 ✓	5,100✓		5,100

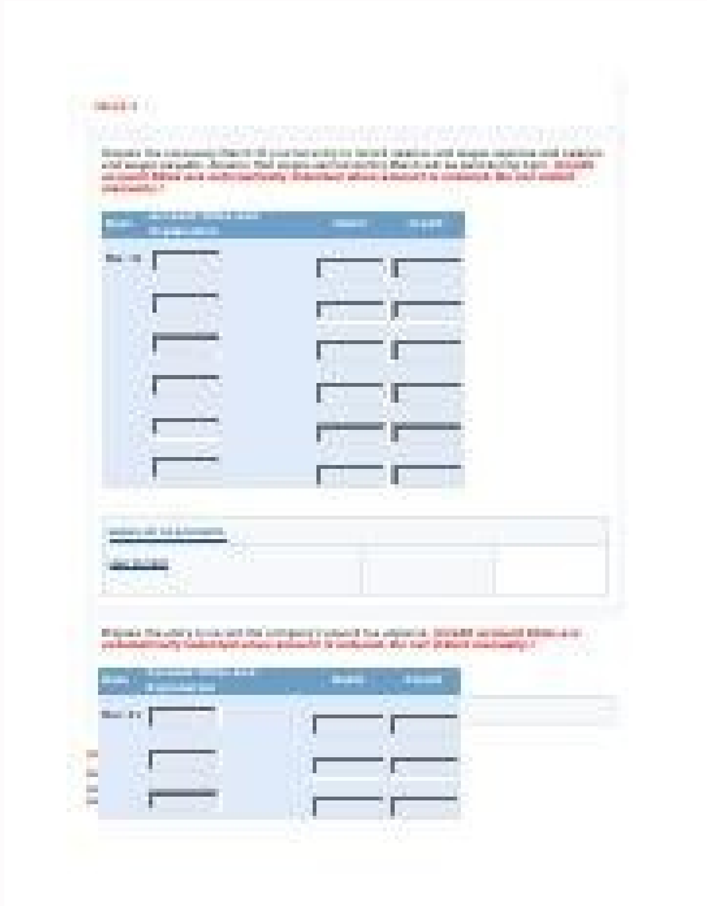
403: Services Revenue

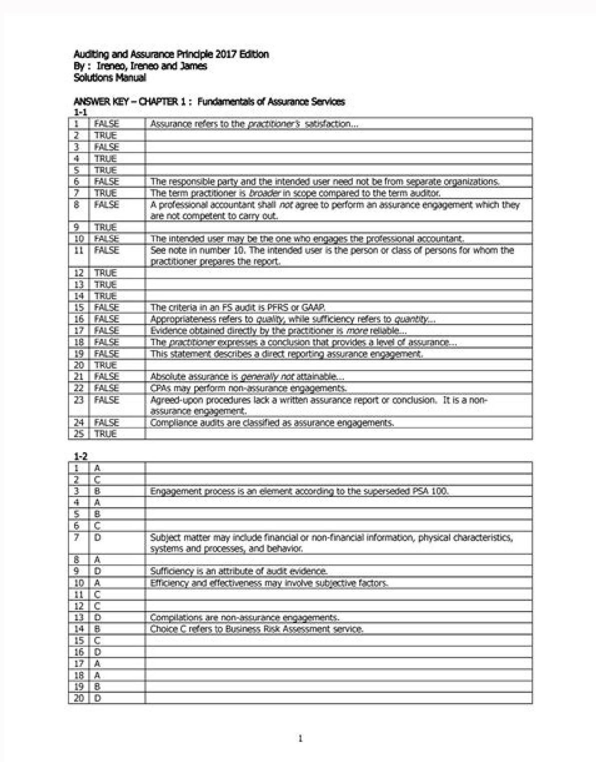
Date	Debit	Credit	Balance
Mar 6 ✓		4,000✓	4,000
Mar 9 ✓		7,500✓	11,500
Mar 25 ✓		3,820✓	15,320

690: Utilities Expense

Date	Debit	Credit	Balance
Mar 31 ✓	500✓		500







Intermediate accounting answer key.

1. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-1 CHAPTER 17 Investments ASSIGNMENT CLASSIFICATIONTABLE (BY TOPIC) Topics Questions Brief Exercises Exercises Problems Concepts for Analysis 1. Debt securities. 1, 2, 3, 13 1 6 (a) Held-to-maturity. 4, 5, 7, 8, 10, 13, 21 1, 3 2, 3, 5 1, 7 (b) Trading. 4, 6, 7, 8, 10, 21 4 1 (c) Available-for-sale. 4, 7, 8, 9, 10, 11, 21 2, 10 4 1, 2, 3, 4, 7 1 2. Bond amortization. 8, 9 1, 2, 3 3, 4, 5 1, 2, 3 3. Equity securities. 1, 12, 16 1 6 (a) Available-for-sale. 7, 10, 11, 15, 21 5, 8 6, 8, 9, 11, 12, 16, 19, 20 3, 5, 6, 8, 9, 10, 11, 12 1, 2, 3 (b) Trading. 6, 7, 8, 10, 14, 15, 21 6 6, 7, 14, 15, 19, 20 6, 8 1, 3 (c) Equity method. 16, 17, 18, 19, 20 7 12, 13, 16, 17 8 4, 5 4. Comprehensive income. 22 9 10 9, 10, 12 5. Disclosures of investments. 18 10 5, 8, 9, 10, 11, 12 6. Fair value option. 25, 26, 27 19, 20, 21 7. Impairments. 24 10 18 3 8. Transfers between categories. 23 8 1, 3, 6 *9. Derivatives. 28, 29, 30, 31, 32, 33, 34, 35 22, 23, 24, 25, 26, 27 13, 14, 15, 16, 17, 18 *10. Variable Interest Entities. 36, 37 *This material is dealt with in an Appendix to the chapter. 2. 17-2 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) ASSIGNMENT CLASSIFICATIONTABLE (BY LEARNING OBJECTIVE) Learning Objectives Questions Brief Exercises Exercises Problems Concepts for Analysis 1. Identify the three categories of debt securities and describe the accounting and reporting treatment for each category. 1, 2, 3, 4, 5, 6, 7 1 CA17-1 2. Understand the procedures for discount and premium amortization on bond investments. 8, 9, 10, 11 1, 2, 3, 4 2, 3, 4, 5, 21 1, 2, 3, 4, 7 3. Identify the categories of equity securities and describe the accounting and reporting treatment for each category. 12, 13, 14, 15 5, 6, 8 1, 6, 7, 8, 9, 11, 12, 14, 15, 16, 19, 20, 21 3, 5, 6, 8, 9, 10, 11, 12 CA17-1, CA17-3, CA17-5 4. Explain the equity method of accounting and compare it to the fair value method for equity securities. 16, 17, 18, 19, 20, 25 7 12, 13, 16, 17 8 CA17-4 5. Describe the accounting for the fair value option and the accounting for impairments of debt and equity investments. 21, 24, 26, 27 10 18, 19, 20, 21 8, 9, 10, 12 CA17-6 6. Describe the reporting of reclassification adjustments and the accounting for transfers between categories. 22, 23 9 10 *7. Describe the uses of, and accounting for derivatives. 28, 29 22, 26 13, 14, 15 3. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-3 *8. Explain how to account for a fair value hedge. 30, 31, 32 23, 25 16, 17, 18 *9. Explain how to account for a cash flow hedge. 33, 34 24, 27 *10. Identify special reporting issues for derivatives. 35, 36, 37 4. 17-4 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) ASSIGNMENT CHARACTERISTICSTABLE Item Description Level of Difficulty Time (minutes) E17-1 Investment classifications. Simple 5–10 E17-2 Entries for held-to-maturity securities. Simple 10–15 E17-3 Entries for held-to-maturity securities. Simple 15–20 E17-4 Entries for available-for-sale securities. Simple 10–15 E17-5 Effective-interest versus straight-line bond amortization. Simple 20–30 E17-6 Entries for available-for-sale and trading securities. Simple 10–15 E17-7 Trading securities entries. Simple 10–15 E17-8 Available-for-sale securities entries and reporting. Simple 5–10 E17-9 Available-for-sale securities entries and financial statement presentation. Simple 10–15 E17-10 Comprehensive income disclosure. 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Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price. (b) A holding gain or loss is the net change in fair value of a security. The holding gain or loss does not include dividend or interest income recognized but not yet received or write-downs for other- than-temporary impairment. (c) A cash flow hedge is a hedge of the exposure to variability in the cash flows of a recognized asset or liability, or of a forecasted transaction, that is attributable to a particular risk. (d) A fair value hedge is a hedge of the exposure to changes in the fair value of a recognized asset or liability, or of an unrecognized firm commitment, that are attributable to a particular risk. CE17-2 According to FASB ASC 235-10-S99-1 (Notes to Financial Statements—SEC Materials): (n) Accounting policies for certain derivative instruments. Disclosures regarding accounting policies shall include descriptions of the accounting policies used for derivative financial instruments and derivative commodity instruments and the methods of applying those policies that materially affect the determination of financial position, cash flows, or results of operation. This description shall include, to the extent material, each of the following items: (1) A discussion of each method used to account for derivative financial instruments and derivative commodity instruments; (2) The types of derivative financial instruments and derivative commodity instruments accounted for under each method; (3) The criteria required to be met for each accounting method used, including a discussion of the criteria required to be met for hedge or deferral accounting and accrual or settlement accounting (e. g., whether and how risk reduction, correlation, designation, and effectiveness tests are applied); (4) The accounting method used if the criteria specified in paragraph (n)(3) of this section are not met; (5) The method used to account for terminations of derivatives designated as hedges or derivatives used to affect directly or indirectly the terms, fair values, or cash flows of a designated item; 7. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-7 CE17-2 (Continued) (6) The method used to account for derivatives when the designated item matures, is sold, is extinguished, or is terminated. In addition, the method used to account for derivatives designated to an anticipated transaction, when the anticipated transaction is no longer likely to occur; and (7) Where and when derivative financial instruments and derivative commodity instruments, and their related gains and losses, are reported in the statements of financial position, cash flows, and results of operations. Instructions to paragraph 4-08(n). 1. For purposes of this paragraph (n), derivative financial instruments and derivative commodity instruments (collectively referred to as “derivatives”) are defined as follows: (i) Derivative financial instruments have the same meaning as defined by generally accepted accounting principles (see Financial Accounting Standards Board (“FASB”), Statement of Financial Accounting Standards No. 119, “Disclosure about Derivative Financial Instruments andFair Value of FinancialInstruments,”(“FAS119”) paragraphs 5–7, (October 1994)), and include futures, forwards, swaps, options, and other financial instruments with similar characteristics. (ii) Derivative commodity instruments include, to the extent such instruments are not derivative financial instruments, commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are permitted by contract or business custom to be settled in cash or with another financial instrument. For purposes of this paragraph, settlement in cash includes settlement in cash of the net change in value of the derivative commodityinstrument (e. g., net cashsettlement based on changes in the price of the underlying commodity). 2. For purposes of paragraphs (n)(2), (n)(3), (n)(4), and (n)(7), the required disclosures should address separately derivatives entered into for trading purposes and derivatives entered into for purposes other than trading. For purposes of this paragraph, trading purposes has the same meaning as defined by generally accepted accounting principles (see, e. g., FAS 119, paragraph 9a (October 1994)). 3. For purposes of paragraph (n)(6), anticipated transactions means transactions (other than transactions involving existing assets or liabilities or transactions necessitated by existing firm commitments) an enterprise expects, but is not obligated, to carry out in the normal course of business (see, e. g., FASB, Statement of Financial Accounting Standards No. 80, “Accounting for Futures Contracts,” paragraph 9, (August 1984)). 4. Registrants should provide disclosures required under paragraph (n) in filings with the Commission that include financial statements of fiscal periods ending after June 15, 1997. [45 FR 63669, Sept. 25, 1980, as amended at 46 FR 56179, Nov. 16, 1981; 50 FR 25215, June 18, 1985; 50 FR 49532, Dec. 3, 1985; 51 FR 3770, Jan. 30, 1986; 57 FR 45293, Oct. 1, 1992; 59 FR 65636, Dec. 20, 1994; 62 FR 6063, Feb. 10, 1997] 8. 17-8 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) CE17-3 According to FASB ASC 323-10-35-20 (Investments—Equity Method and Joint Ventures—Subsequent Measurement): The investor ordinarily shall discontinue applying the equity method if the investment (and net advances) is reduced to zero and shall not provide for additional losses unless the investor has guaranteed obligations of the investee or is otherwise committed to provide further financial support for the investee. CE17-4 According to FASB ASC 815-10-45-4 (Derivatives and Hedging—Other Presentation Matters—Balance Sheet Netting); Unless the conditions in paragraph 210-20-45-1 are met, the fair value of derivative instruments in a loss position shall not be offset against the fair value of derivative instruments in a gain position. Similarly, amounts recognized as accrued receivables shall not be offset against amounts recognized as accrued payables unless a right of setoff exists. 9. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-9 ANSWERS TO QUESTIONS 1. A debt security is an instrument representing a creditor relationship with an entity. Debt securities include U.S. government securities, municipal securities, corporate bonds, convertible debt, and commercialpaper. Trade accounts receivable and loans receivable are not debt securities because they do not meet the definition of a security. An equity security is described as a security representing an ownership interest such as common, preferred, or other capital stock. It also includes rights to acquire or dispose of an ownership interest at an agreed-upon or determinable price, such as warrants, rights, and call options or put options. Convertible debt securities and redeemable preferred stocks are not treated as equity securities. 2. The variety in bond features along with the variability in interest rates permits investors to shop for exactly the investment that satisfies their risk, yield, and marketability desires, and permits issuers to create a debt instrument best suited to their needs. 3. Cost includes the total consideration to acquire the investment, including brokerage fees and other costs incidental to the purchase. 4. The three types of classifications are: Held-to-maturity: Debt investments that the companyhas the positive intent and ability to hold to maturity. Trading: Debt investments bought and held primarily for sale in the near term to generate income on short-term price differences. Available-for-sale: Debt investments not classified as held-to-maturity or trading securities. 5. A debt investment should be classified as held-to-maturity only if the company has both: (1) the positive intent and (2) the ability to hold those securities to maturity. 6. Trading securities are reported at fair value, with unrealized holding gains and losses reported as part of net income. Any discount or premium is amortized. 7. Trading and available-for-sale securities should be reported at fair value, whereas held-to-maturity securities should be reported at amortized cost. 8. $3,500,000 X 10% = $350,000; $350,000 ÷ 2 = $175,000. Wheeler would make the following entry: Cash ($4,000,000 X 8% X 1 /2) .... 160,000 Debt Investments.. 15,000 Interest Revenue ($3,500,000 X 10% X 1 /2)................................ 175,000 9. Fair Value Adjustment (available-for-sale) .... 89,000 Unrealized Holding Gain or Loss—Equity [$3,604,000 – ($3,500,000 + $15,000)*] .... 89,000 *See number 8. 10. Unrealized holding gains and losses for trading securities should be included in net income for the current period. Unrealized holding gains and losses for available-for-sale securities should be reported as other comprehensive income and as a separate component of stockholders’ equity. Unrealized holding gains and losses are not recognized for held-to-maturity securities. 10. 17-10 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) Questions Chapter 17 (Continued) 11. (a) Unrealized Holding Gain or Loss—Equity.................................... 60,000 Fair Value Adjustment (available-for-sale) .... 60,000 (b) Unrealized Holding Gain or Loss—Equity.................................... 70,000 Fair Value Adjustment (available-for-sale) .... 70,000 12. Investments in equity securities can be classified as follows: (a) Holdings of less than 20% (fair value method)—investor has passive interest. (b) Holdings between 20% and 50% (equity method)—investor has significant influence. (c) Holdings of more than 50% (consolidated statements)—investor has controlling interest. Holdings of less than 20% are then classified into trading and available-for-sale, assuming determinable fair values. 13. Investments in stock do not have a maturity date and therefore cannot be classified as held-to- maturity securities. 14. Selling price of 10,000 shares at $27.50... $275,000 Less: Brokerage commissions.. (1,770) Proceeds from sale.. 273,230 Cost of 10,000 shares.. (260,000) Gain on sale of investments .... $ 13,230 Cash.. 273,230 Equity Investments.. 260,000 Gain on Sale of Investments.. 13,230 15. Both trading and available-for-sale equity securities are reported at fair value. However, any unrealized holding gain or loss is reported in net income for trading securities but as other comprehensive income and as a separate component of stockholders’ equity for available-for-sale securities. 16. Significant influence over an investee may result from representation on the board of directors, participation in policy-making processes, material intercompany transactions, interchange of managerial personnel, or technological dependency. An investment (direct or indirect) of 20% or more of the voting stockof an investee constitutes significant influence unless there exists evidence to the contrary. 17. Under the equity method, the investment is originally recorded at cost, but is adjusted for changes in the investee’s net assets. The investment account is increased (decreased) by the investor’s proportionate share of the earnings (losses) of the investee and decreased by all dividends received by the investor from the investee. 18. The 20% rule is that an investment (direct or indirect) of 20 percent or more of the voting stock of an investee leads to the presumption that an investor has the ability to exercise significant influence over an investee and the equity method should be used. However, there are other factors, when considered, may indicate that ownership of 20 percent or more may not enable an investor to exercise significant influence. An investor with ownership just below 20% may be able to exercise significant influence based on representation on the board of directors, participation in policy-making processes, material intercompany transactions, interchange of managerial personnel, or technological dependency. Another important consideration is the extent of ownership by an investor in relation to the concentration of other shareholdings 11. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-11 Questions Chapter 17 (Continued) Factors that could lead to a conclusion of no significant ownership, when ownership in above 20percent include: (1) The investee opposes the investor’s acquisition of its stock; (2) The investor and investee sign an agreement under which the investor surrenders significant shareholder rights; (3) The investor’s ownership share does not result in “significant influence” because majority ownership of the investee is concentrated among a small group of shareholders who operate the investee without regard to the views of the investor; (4) The investor tries and fails to obtain representation on the investee’s board of directors. 19. Dividends subsequent to acquisition should be accounted for as a reduction in the Equity Investment received account. 20. Ordinarily, Raleigh Corp. should discontinue applying the equity method and not provide for additional losses beyond the carrying value of $170,000. However, if Raleigh Corp.’s loss is not limited to its investment (due to a guarantee of Borg’s obligations or other commitment to provide further financial support or if imminent return to profitable operations by Borg appears to be assured), it is appropriate for Raleigh Corp. to provide for its entire $186,000 share of the $620,000 loss. 21. Trading securities should be reported at aggregate fair value as current assets. Individual held-to- maturity and available-for-sale securities are classified as current or noncurrent depending upon the circumstances. Held-to-maturity securities generally should be classified as current or noncurrent, based on the maturity date of the individual securities. Debt securities identified as available-for-sale should be classified as current or noncurrent, based on maturities and expectations as to sales and redemptions inthe following year. Equity securities identifiedas available-for-saleshouldbe classified as current if these securities are available for use in current operations. 22. Reclassification adjustments are necessary to insure that double counting does not result when realized gains or losses are reported as part of net income but also are shown as part of other comprehensive income in the current period or in previous periods. 23. When a security is transferred from one category to another, the transfer should be recorded at fair value, which in this case becomes the new basis for the security. Any unrealized gain or loss at the date of the transfer increases or decreases stockholders’ equity. The unrealized gain or loss at the date of the transfer to the trading category is recognized in income. 24. A debt security is impaired when “it is probable that the investor will be unable to collect all amounts due according to the contractual terms.” When an impairment has occurred, the security is written down to its fair value, which is also the security’s new cost basis. The amount of the writedown is accounted for as a realized loss. 25. Fair value is defined as “the price that would be received to sell an assetor paid to transfer a liability in an orderly transaction between market participants at the measurement date.” Fair value is therefore a market-based measure. 26. The fair value option gives companies the option to report most financial instruments at fair value with all gains and losses related to changes in fair value reported in the income statement. This option is applied on an instrument by instrument basis. The fair value option is generally available only at the time a company first purchases the financial asset or incurs a financial liability. If a company chooses to use the fair value option, it must measure this instrument at fair value until the company no longer has ownership. 27. No. The fair value option is generally available only at the time a company first purchases the financial asset or incurs a financial liability. If a company chooses to use the fair value option, it must measure this instrument at fair value until the company no longer has ownership. 12. 17-12 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) Questions Chapter 17 (Continued) *28. An underlying is a special interest rate, security price, commodity price, index of prices or rates, or other market-related variable. Changes in the underlying determine changes in the value of the derivative. Payment is determined by the interaction of the underlying with the face amount and the number of shares,or other units specified in the derivative contract(these elements are referred to as notional amounts). *29. See illustration below: Feature Traditional Financial Instrument (e.g., Trading Security) Derivative Financial Instrument (e.g., Call Option) Payment Provision Stock price times the number of shares. Change in stock price (underlying) times number of shares (notional amount). Initial Investment Investor pays full cost. Initial investment is less than full cost. Settlement Deliver stock to receive cash. Receive cash equivalent, based on changes in stock price times the number of shares. For a traditional financial instrument, an investor generally must pay the full cost, while derivatives require little initial investment. In addition, the holder of a traditional security is exposed to all risks of ownership, while

most derivatives are not exposed to all risks associated with ownership in the underlying. For example, the intrinsic value of a call option only can increase in value. Finally, unlike a traditional financial instrument, the holder of a derivative could realize a profit without ever having to take possession of the underlying. This feature is referred to as net settlement and serves to reduce the transaction costs associated with derivatives. *30. The purpose of a fair value hedge is to offset the exposure to changes in the fair value of a recognized asset or liability or of an unrecognized firm commitment. *31. The unrealized holding gain or loss on available-for-sale securities should be reported as income when this security is designated as a hedged item in a qualifying fair value hedge. If the hedge meets the special hedge accounting criteria (designation, documentation, and effectiveness), the unrealized holding gain or loss is reported as income. *32. This is likely a setting where the company is hedging the fair value of a fixed-rate debt obligation. The fixed payments received on the swap will offset fixed payments on the debt obligation. As a result, if interest rates decline, the value of the swap contract increases (a gain), while at the same time the fixed-rate debt obligation increases (a loss). The swap is an effective risk management tool in this setting because its value is related to the same underlying (interest rates) that will affect the value of the fixed-rate bond payable. Thus, if the value of the swap goes up, it offsets the loss in the value of the debt obligation. *33. A cash flow hedge is used to hedge exposure to cash flow risk, which is exposure to the variability in cash flows. The cash flows received on the hedging instrument (derivative) will offset the cash flows received on the hedged item. Generally, the hedged item is a transaction that is planned some time in the future (an anticipated transaction). *34. Derivatives used in cashflow hedges are accounted for at fair value on the balance sheet but gains or losses are recorded in equity as part of other comprehensive income. *35. A hybrid security is a security that has characteristics of both debt and equity and often is a combination of traditional and derivative financial instruments. A convertible bond is a hybrid security because it is comprised of a debt security, referred to as the host security, combined with an option to convert the bond to shares of common stock, the embedded derivative. 13. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-13 Questions Chapter 17 (Continued) *36. The voting-interest model is when a company owns more than 50% of another company. The risk- and-reward model is when a company is involved substantially in the economics of another company. If one of these two conditions exist, the consolidation should occur. *37. A variable-interest entity (VIE) is an entity that has one of the following characteristics: (a) Insufficient equity investment at risk. Stockholders are assumed to have sufficient capital investment to support the entity's operations. If thinly capitalized, the entity is considered a VIE and is subject to the risk-and-reward model. (b) Stockholders lack decision-making rights. In some cases, stockholders do not have the influence to control the company's destiny. (c) Stockholders do not absorb the losses or receive the benefits of a normal stockholder. In some entities, stockholders are shielded from losses related to their primary risks, or their returns are capped or must be shared by other parties. 14. 17-14 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) SOLUTIONS TO BRIEF EXERCISES BRIEF EXERCISE 17-1 (a) Debt Investments.................... 74,086 Cash.................... 74,086 (b) Cash ($80,000 X .09).................... 7,200 Debt Investments.................... 949 Interest Revenue ($74,086 X .11).................... 8,149 BRIEF EXERCISE 17-2 (a) Debt Investments (available-for-sale).................... 74,086 Cash.................... 74,086 (b) Cash ($80,000 X .09).................... 7,200 Debt Investments (available-for-sale).................... 949 Interest Revenue ($74,086 X .11).................... 8,149 (c) Fair Value Adjustment (available-for-sale).................... 465 Unrealized HoldingGain or Loss—Equity [($74,086 + $949) – $75,500].................... 465 BRIEF EXERCISE 17-3 (a) Debt Investments.................... 65,118 Cash.................... 65,118 (b) Cash ($60,000 X .08 X 6/12).................... 2,400 Debt Investments (held-to-maturity).................... 446 Interest Revenue ($65,118 X .06 X 6/12).................... 1,954 15. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-15 BRIEF EXERCISE 17-4 (a) Debt Investments (trading).................... 50,000 Cash.................... 50,000 (b) Cash.................... 2,000 Interest Revenue.................... 2,000 (c) Unrealized Holding Gain or Loss—Income.................... 2,600 Fair Value Adjustment(trading) ($50,000 – $47,400).................... 2,600 BRIEF EXERCISE 17-5 (a) Equity Investments (available-for-sale).................... 13,200 Cash.................... 13,200 (b) Cash.................... 1,300 Dividend Revenue (400 X $3.25).................... 1,300 (c) Fair Value Adjustment (available-for-sale).................... 600 Unrealized HoldingGain or Loss—Equity [(400 X $34.50) – $13,200].................... 600 BRIEF EXERCISE 17-6 (a) Equity Investments (trading).................... 13,200 Cash.................... 13,200 (b) Cash.................... 1,300 Dividend Revenue (400 X $3.25).................... 1,300 (c) Fair Value Adjustment (trading).................... 600 Unrealized HoldingGain or Loss—Income [(400 X $34.50) – $13,200].................... 600 16. 17-16 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) BRIEF EXERCISE 17-7 Equity Investments.................... 300,000 Cash.................... 300,000 Equity Investments.................... 54,000 Investment Income (30% X $180,000).................... 54,000 Cash.................... 18,000 Equity Investments (30% X $60,000).................... 18,000 BRIEF EXERCISE 17-8 Fair Value Adjustment (available-for-sale).................... 500 Unrealized HoldingGain or Loss—Equity.................... 500 BRIEF EXERCISE 17-9 (a) Other comprehensive income (loss) for 2011: ($10.9) million (b) Comprehensiveincomefor 2011: $1,234.8 million or ($1,245.7 – $10.9) (c) Accumulated other comprehensive income: $46.3 million or ($57.2 – $10.9) Note to instructor: In 2011,Starbucks also reportedforeign currency tran- slationadjustments,whichaffectedaccumulatedothercomprehensive income. BRIEF EXERCISE 17-10 Loss on Impairment.................... 10,000 Debt Investments.................... 10,000 In this case, an impairment has occurred and the individual security should be written down. If Hillsborough has already recognized an unrealized holding loss—equity,an additionalentry is needed to reverse this amount as well as eliminate the fair value adjustment (available-for-sale) account. 17. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-17 SOLUTIONS TO EXERCISES EXERCISE 17-1 (5–10 minutes) (a) 1. (b) 2. (c) 1. (d) 2. (e) 3. (f) 4. EXERCISE 17-2 (10–15 minutes) (a) January 1, 2013 Debt Investments.................... 300,000 Cash.................... 300,000 (b) December 31,2013 Cash.................... 36,000 Interest Revenue.................... 36,000 (c) December 31,2014 Cash.................... 36,000 Interest Revenue.................... 36,000 EXERCISE 17-3 (15–20 minutes) (a) January 1, 2013 Debt Investments.................... 322,744.44 Cash.................... 322,744.44 (b) Schedule of InterestRevenue and Bond Premium Amortization Effective-Interest Method 12% Bonds Sold to Yield 10% Date Cash Received Interest Revenue Premium Amortized Carrying Amount of Bonds 1/1/13 — — — $322,744.44 12/31/13 $36,000 $32,274.44 $3,725.56 319,018.88 12/31/14 36,000 31,901.89 4,098.11 314,920.77 12/31/15 36,000 31,492.08 4,507.92 310,412.85 12/31/16 36,000 31,041.29 4,958.71 305,454.14 12/31/17 36,000 30,545.86* 5,454.14 300,000.00 *Rounded by 45¢. 18. 17-18 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-3 (Continued) (c) December 31,2013 Cash.................... 36,000 Debt Investments.................... 3,725.56 Interest Revenue.................... 32,274.40 (d) December 31,2014 Cash.................... 36,000 Debt Investments.................... 4,098.11 Interest Revenue.................... 31,901.89 EXERCISE 17-4 (10-15 minutes) (a) January 1, 2013 Debt Investments (available-for-sale).................... 322,744.44 Cash.................... 322,744.44 (b) December 31,2013 Cash.................... 36,000 Debt Investments (available-for-sale).................... 3,725.56 Interest Revenue ($322,744.44 X .10).................... 32,274.44 Fair Value Adjustment (available-for-sale).................... 1,481.12 Unrealized HoldingGain or Loss—Equity ($320,500.00 – $319,018.88).................... 1,481.12 (c) December 31,2014 Unrealized Holding Gain or Loss—Equity.................... 7,401.89 Fair Value Adjustment (available-for-sale).................... 7,401.89 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-19 EXERCISE 17-4 (Continued) Amortized Cost Fair Value Unrealized Gain (Loss) Available-for-sale bonds $314,920.77 $309,000.00 $(5,920.77) Previousfair value adjustment—Dr. 1,481.12 Fair value adjustment—Cr. $(7,401.89) EXERCISE 17-5 (20–30 minutes) (a) Schedule of InterestRevenue and Bond DiscountAmortization Straight-line Method 9% Bond Purchased to Yield 12% Date Cash Received Interest Revenue Bond Discount Amortization Carrying Amount of Bonds 1/1/13 — — — $185,589 12/31/13 $18,000 $22,804 *$4,804* 190,393 12/31/14 18,000 22,804 4,804 195,197 12/31/15 18,000 22,803** 4,803 200,000 **($200,000 – $185,589)÷ 3 = $4,804 **Rounded by $1. (b) Schedule of InterestRevenue and Bond DiscountAmortization Effective-Interest Method 9% Bond Purchased to Yield 12% Date Cash Received Interest Revenue Bond Discount Amortization Carrying Amount of Bonds 1/1/13 — — — $185,589.00 12/31/13 $18,000 $22,270.68* $4,270.68 189,859.68 12/31/14 18,000 22,783.16 4,783.16 194,642.84 12/31/15 18,000 23,357.16** 5,357.16 200,000.00 **$185,589 X .12 = $22,270.68 **Rounded by $.02. 20. 17-20 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-5 (Continued) (c) December 31, 2014 Cash.................... 18,000.00 Debt Investments.................... 4,804.00 Interest Revenue.................... 22,804.00 (d) December 31,2014 Cash.................... 18,000.00 Debt Investments.................... 4,783.16 Interest Revenue.................... 22,783.16 EXERCISE 17-6 (10–15 minutes) (a) Fair Value Adjustment (trading).................... 5,000 Unrealized Holding Gain or Loss—Income.... 5,000 (b) Fair Value Adjustment (available-for-sale).................... 5,000 Unrealized Holding Gain or Loss—Equity...... 5,000 (c) The Unrealized HoldingGain or Loss—Incomeaccountis reportedin the income statement under Other Revenues and Gains. The Unrealized Holding Gain or Loss—Equity account is reported as a part of other comprehensive income and as a componentofstockholders'equity until realized. The Securities Fair Value Adjustment account is added to the cost of the Debt Investment account to arrive at fair value. EXERCISE 17-7 (10–15 minutes) (a) December 31,2013 Unrealized Holding Gain or Loss—Income........... 1,400 Fair Value Adjustment (trading).................... 1,400 (b) During 2014 Cash.................... 9,400 Loss on Sale of Investments.................... 600 Equity Investments (trading).................... 10,000 21. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-21 EXERCISE 17-7 (Continued) (c) December 31,2014 Securities Cost Fair Value Unrealized Gain (Loss) Clemson Corp.stock $20,000 $19,100 ($ (900) Buffaloes Co. stock 20,000 20,500 (500) Totalof portfolio $40,000 $39,600 ((400) Previousfair value adjustmentbalance—Cr. ((1,400) Fair value adjustment—Dr. ($1,000) Fair Value Adjustment (trading).................... 1,000 Unrealized Holding Gain or Loss—Income........ 1,000 EXERCISE 17-8 (5–10 minutes) The unrealized gains and losses resulting from changes in the fair value of available-for-sale securities are recorded in an unrealized holding gain or loss account that is reported as other comprehensive income and as a separate component of stockholders' equity until realized. Therefore, the following adjusting entry should be made at the year-end: Unrealized Holding Gain or Loss—Equity.................... 8,000 Fair Value Adjustment (available-for-sale).................... 8,000 Unrealized Holding Gain or Loss—Equity is reported as other comprehen- sive income and as a separate component in stockholders' equity and not included in net income. The Fair Value Adjustment (available-for-sale) account is a valuation account to the related investment account. 22. 17-22 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-9 (10–15 minutes) (a) The portfolio should be reported at the fair value of $54,500. Since the cost of the portfolio is $53,000,the unrealizedholding gain is $1,500,of which $400 is already recognized. Therefore, the December 31, 2013 adjusting entry should be: Fair Value Adjustment (available-for-sale).................... 1,100 Unrealized Holding Gain or Loss—Equity............ 1,100 (b) The unrealizedholding gain of $1,500(includingthe previousbalance of $400) should be reported as an addition to stockholders' equity and the Fair Value Adjustment (available-for-sale) account balance of $1,500 should be added to the cost of the investment account. STEFFI GRAF, INC. Balance Sheet As of December 31, 2013 Currentassets: Equity investments $54,500 Stockholders'equity: Common stock xxx,xxx Additional paid-in capital xxx,xxx Retained earnings xxx,xxx xxx,xxx Add: Accumulated other comprehensive income 1,500* Total stockholders' equity $xxx,xxx *Note: The unrealizedholding gain could also be disclosed. (c) Computationof realized gain or loss on sale of stock: Net proceeds from sale of security A $15,100 Cost of security A 17,500 Loss on sale of stock ($ 2,400) January 20,2014 Cash.................... 15,100 Loss on Sale of Investments.................... 2,400 Equity Investments (available-for-sale)............ 17,500 23. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-23 EXERCISE 17-10 (20–25 minutes) (a) STEFFIGRAF, INC. Statementof Comprehensive Income For the Year Ended December 31,2013 Net income $120,000 Other comprehensiveincome Unrealized holding gain 1,100 Comprehensive income $121,100 (b) STEFFIGRAF, INC. Statementof Comprehensive Income For the Year Ended December 31,2014 Net income $140,000 Other comprehensiveincome Holding gains $40,000 Add: Reclassificationadjustmentfor loss included in net income 2,400 42,400 Comprehensive income $182,400 Accumulatedother comprehensive income: Beginning balance, January 1, 2014 $1,100 Currentperiod other comprehensive income $40,000 Amount reclassified from accumulated other comprehensive income 2,400 Unrealized holding gain 42,400 Ending balance, December 31, 2014 $43,400 EXERCISE 17-11 (20–25 minutes) (a) The total purchaseprice of these investments is: Sanchez: (10,000 X $33.50)+ $1,980 = $336,980 Vicario: (5,000 X $52.00)+ $3,370 = $263,370 WTA: (7,000 X $26.50)+ $4,910 = $190,410 The purchase entries will be: January 15,2014 Equity Investments (available-for-sale).............. 336,980 Cash.................... 336,980 24. 17-24 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-11 (Continued) April 1, 2014 Equity Investments (available-for-sale)............... 263,370 Cash.................... 263,370 September 10,2014 Equity Investments (available-for-sale)............... 190,410 Cash.................... 190,410 (b) Gross selling price of 4,000 shares at $35 $140,000 Less: Commissions, taxes, and fees (3,850) Net proceeds from sale 136,150 Cost of 4,000 shares ($336,980 X 0.4) (134,792) Gain on sale of stock $ 1,358 May 20, 2014 Cash.................... 136,150 Equity Investments (available-for-sale)......... 134,792 Gain on Sale of Investments.................... 1,358 (c) Securities Cost Fair Value Unrealized Gain (Loss) Sanchez Co. $202,188* $180,000(1) $(22,188) Vicario Co. 263,370 275,000(2) (11,630 WTA Co. 190,410 196,000(3) 5,590 Totalportfolio value $655,968 $651,000 (4,968) Previousfair value adjustmentbalance 0 Fair value adjustment—Cr. $ (4,968) *$336,980X 0.6 = $202,188. (1) (6,000 X $30) (2) (5,000 X $55) (3) (7,000 X $28) December 31,2014 Unrealized Holding Gain or Loss—Equity............ 4,968 Fair Value Adjustment (available-for-sale).................... 4,968 25. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-25 EXERCISE 17-12 (15–20 minutes) Situation 1: Journalentries by Conchita Cosmetics: To record purchase of20,000 shares ofMartinez Fashion ata costof $13 per share: March 18, 2014 Equity Investments (available-for-sale).................... 260,000 Cash.................... 260,000 To recordthe dividendrevenuefrom Martinez Fashion: June 30, 2014 Cash.................... 7,500 Dividend Revenue ($75,000 X 10%).................... 7,500 To recordthe investmentat fair value: December 31, 2014 Fair Value Adjustment (available-for-sale).................... 40,000 Unrealized Holding Gain or Loss—Equity............... 40,000* *($15 – $13) X 20,000 shares= $40,000 Situation 2: Journalentries by Monica,Inc.: To record the purchase of 30% of Seles Corporation's common stock: January 1, 2014 Equity Investments (Seles Corp.).................... 81,000 Cash [(30,000 X 30%) X $9].................... 81,000 Since Monica, Inc. obtained significant influence over Seles Corp., Monica, Inc. now employs the equity method of accounting. To recordthe receiptof cash dividends from Seles Corporation: June 15, 2014 Cash ($36,000 X 30%).................... 10,800 Equity Investments (Seles Corp.).................... 10,800 26. 17-26 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-12 (Continued) To recordMonica'sshare(30%)ofSeles Corporation's netincomeof$85,000: December 31, 2014 Equity Investments (Seles Corp.).................... 25,500 (30% X $85,000) Investment Income.................... 25,500 EXERCISE 17-13 (10–15 minutes) (a) $110,000,the increaseto the Investmentaccount. (b) If the dividend payoutratio is 40%, then 40% of the net income is their share of dividends = $44,000. (c) Their share is 25%,so, TotalNet Income X 25% = $110,000 TotalNet Income = $110,000 ÷ 25% = $440,000 (d) $44,000 ÷ 25% = $176,000 or $440,000 X 40% = $176,000 EXERCISE 17-14 (10–15 minutes) 1. Equity Investments(trading) (200 shares X $40).................... 8,000 Cash.................... 8,000 2. Cash (100 shares X $45).................... 4,500 Gain on Sale of Investments.................... 500 Equity Investments(trading) (100 X $40).................... 4,000 3. Unrealized Holding Gain or Loss—Income............ 500 Fair Value Adjustment (trading) ($40–$35) X 100.................... 500 27. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-27 EXERCISE 17-15 (15–20 minutes) (a) Unrealized Holding Gain or Loss—Income............. 7,900 Fair Value Adjustment (trading).................... 7,900 (b) Cash [(1,500 X $45) – $1,200].................... 66,300 Loss on Sale of Investments.................... 7,200 Equity Investments (trading).................... 73,500 (c) Equity Investments(trading) [(700 X $75) + $1,300].................... 53,800 Cash.................... 53,800 (d) Securities Cost Fair Value Unrealized Gain (Loss) Wallace Corp., Common $180,000 $175,000 $ (5,000) Earnhart Corp., Common 53,800 50,400 (3,400) Martin Inc., Preferred 60,000 58,000 (2,000) Total portfolio $293,800 $283,400 (10,400) Previous fair value adjustment—Cr. (7,900) Fair value adjustment—Cr. $ (2,500) Unrealized Holding Gain or Loss—Income..... 2,500 Fair Value Adjustment (trading)............... 2,500 EXERCISE 17-16 (15–20 minutes) (a) December 31,2013 Equity Investments (available-for-sale).......... 1,200,000 Cash.................... 1,200,000 June 30, 2014 Cash.................... 42,500 Dividend Revenue.................... 42,500 December 31,2014 Cash.................... 42,500 Dividend Revenue.................... 42,500 28. 17-28 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-16 (Continued) Fair Value Adjustment (available-for-sale)..... 150,000 Unrealized HoldingGain or Loss— Equity.................... 150,000 $27 X 50,000 = $1,350,000 $1,350,000 – $1,200,000 = $150,000 (b) December 31,2013 Equity Investments (Kulikowski).................... 1,200,000 Cash.................... 1,200,000 June 30, 2014 Cash.................... 42,500 Equity Investments (Kulikowski Inc.)............ 42,500 December 31,2014 Cash.................... 42,500 Equity Investments (Kulikowski Inc.)............ 42,500 Equity Investment (Kulikowski Inc.).................... 146,000 Investment Income.................... 146,000 (20% X $730,000) (c) Fair Value Method Equity Method Investmentamount(balancesheet) $1,350,000 *$1,261,000* Dividend revenue (income statement) 85,000 0 Investmentincome (income statement) 146,000 *$1,200,000 + $146,000 – $42,500– $42,500 29. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-29 EXERCISE 17-17 (10–15 minutes) Equity Investments (Edwards Co.).................... 180,000 Cash.................... 180,000 Cash ($20,000 X .30).................... 6,000 Equity Investments (Edwards Co.).................... 6,000 Equity Investments (Edwards Co.).................... 24,000 Investment Income.................... 24,000 (.30 X $80,000) EXERCISE 17-18 (15–20 minutes) (a) Loss on Impairment ($800,000 – $720,000).......... 80,000 Debt Investments (available-for-sale)........... 80,000 (b) The new cost basis is $720,000. GAAP indicates that the difference between the carrying amount and the maturity value should not be recorded. If the bonds are impaired, it is inappropriate to increase the asset back up to its original maturity value. (c) Fair Value Adjustment (available-for-sale).................... 40,000 Unrealized HoldingGain or Loss—Equity ($760,000 – $720,000).................... 40,000 EXERCISE 17-19 (15-20 Minutes) (a) Unrealized HoldingGain or Loss—Income ($100,000 – $80,000).................... 20,000 Equity Investments (Arroyo Company).......... 20,000 (b) Fair Value Adjustment (available-for-sale)........... 50,000 Unrealized HoldingGain or Loss—Equity ($300,000 – $250,000).................... 50,000 (c) Fair Value Adjustment (trading).................... 10,000 Unrealized HoldingGain or Loss—Income ($190,0000 – $180,000).................... 10,000 30. 17-30 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) EXERCISE 17-20 (15-20 minutes) (a) Net income before security gains or losses............. $905,000 Sale of Investmentin Woods Inc. stock ($195,000 – $180,000).................... 15,000 Investmentin Arroyo Companystock ($140,000 – $80,000).................... 60,000 Net income.................... $980,000 (b) Equity Investments(Arroyo Company) ($140,000 – $80,000).................... 60,000 Unrealized Holding Gain or Loss—Income....... 60,000 EXERCISE 17-21 (15-20 minutes) (a) Net income before security gains and losses.......... $100,000 Investment in debt securities ($41,000 – $40,000).... 1,000 Investmentin Chen Company stock ($910,000 – $800,000).................... 110,000 Bonds payable ($220,000 – $195,000).................... 25,000 Net income.................... $236,000 (b) Bonds Payable.................... 25,000 Unrealized HoldingGain or Loss—Income ($220,000 – $195,000).................... 25,000 *EXERCISE 17-22 (15–20 minutes) (a) Call Option.................... 300 Cash.................... 300 (b) Unrealized Holding Gain or Loss—Income.......... 100 Call Option ($300 – $200).................... 100 Call Option.................... 3,000 Unrealized HoldingGain or Loss—Income (1,000 X $3).................... 3,000 (c) Unrealized HoldingGain: $2,900 ($3,000 – $100) 31. 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Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-31 *EXERCISE 17-23 (20–25 minutes) (a) 6/30/14 (b) 12/31/14 Fixed-ratedebt $100,000 $100,000 Fixed rate (6% ÷ 2) 3% 3% Semiannualdebtpayment 3,000 3,000 Swap fixed receipt 3,000 3,000 Net income effect $ 0 $ 0 Swap variable rate 5.7% X 1/2 X $100,000 $ 2,850 6.7% X 1/2 X $100,000 0 $ 3,350 Net interestexpense $ 2,850 $ 3,350 Note to instructor: An interest rate swap in which a company changes its interest payments from fixed to variable is a fair value hedge because the changes in fair value of both the derivative and the hedged liability offset one another. *EXERCISE 17-24 (20–25 minutes) (a) 12/31/14 (b) 12/31/13 Variable-ratedebt $10,000,000 $10,000,000 Variable rate X5.8% X6.6% Debt payment $ 580,000 $ 660,000 Debt payment 580,000 660,000 Swap variable received (580,000) (660,000) Net income effect $ 0 $ 0 Swap payable—fixed ($10,000 X 6%) 600,000 600,000 Net interestexpense $ 600,000 $ 600,000 Note to instructor: An interest swap in which a company changes its interest paymentsfromvariableto fixedis a cashflow hedgebecauseinterestcosts are always the same. 32. 17-32 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) *EXERCISE 17-25 (15–20 minutes) (a) Interest Expense.................... 75,000 Cash (7.5% X $1,000,000).................... 75,000 (b) Cash.................... 13,000 Interest Expense.................... 13,000 (c) Swap Contract.................... 48,000 Unrealized Holding Gain or Loss—Income..... 48,000 (d) Unrealized Holding Gain or Loss—Income............. 48,000 Notes Payable.................... 48,000 *EXERCISE 17-26 (20–25 minutes) (a) August 15, 2013 Call Option.................... 360 Cash.................... 360 (b) September 30,2013 Call Option.................... 3,200 Unrealized Holding Gain or Loss—Income.......... 3,200 ($8 X 400) Unrealized Holding Gain or Loss—Income.................... 180 Call Option ($360 – $180).................... 180 (c) December 31,2013 Unrealized Holding Gain or Loss—Income.................... 800 Call Option ($2 X 400).................... 800 Unrealized Holding Gain or Loss—Income.................... 115 Call Option ($180 – $65).................... 115 33. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-33 *EXERCISE 17-26 (Continued) (d) January 15,2014 Unrealized Holding Gain or Loss—Income.................... 35 Call Option ($65 – $30).................... 35 Cash (400 X $7).................... 2,800 Gain on Settlement of Call Option*.................... 370 Call Option**.................... 2,430 **Computation of Gain: $370 (400 shares X $1) – $30 **Value of Call Option at settlement: Call Option 360 180 3,200 800 115 35 2,430 *EXERCISE 17-27 (25–30 minutes) (a) May 1, 2014 Memorandum entryto indicate entering into the futures contract. (b) June 30, 2014 Futures Contract.................... 4,000 Unrealized HoldingGain or Loss—Equity [($520 – $500) X 200 ounces].................... 4,000 (c) September 30,2014 Futures Contract.................... 1,000 Unrealized HoldingGain or Loss—Equity [($525 – $520) X 200 ounces].................... 1,000 34. 17-34 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) *EXERCISE 17-27 (Continued) (d) October 5, 2014 Inventory.................... 105,000 Cash ($525 X 200 ounces).................... 105,000 Cash.................... 5,000 Futures Contract.................... 5,000 [($525 – $500)X 200 ounces] Note to instructor: In practice, futures contracts are settled on a daily basis; for our purposes, we show only one settlement for the entire amount. (e) December 15,2014 Cash.................... 250,000 Sales Revenue.................... 250,000 Cost of Goods Sold.................... 140,000 Inventory (Finished goods).................... 140,000 Unrealized Holding Gain or Loss—Equity............ 5,000 Cost of Goods Sold ($4,000 + $1,000).......... 5,000 (f) HART GOLF CO. PartialIncome Statement For the Quarter EndedDecember 31,2014 Sales revenue $250,000 Cost of goods sold 135,000* Gross profit $115,000 *Cost of inventory $140,000 Less: Futures contract adjustment (5,000) Cost of goods sold $135,000 35. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-35 TIME AND PURPOSE OF PROBLEMS Problem 17-1 (Time 20–30 minutes) Purpose—the student is required to prepare journal entries and adjusting entries covering a three-year period for debt investments first classified as held-to-maturity and then classified as available-for-sale. Bond premium amortization is also involved. Problem 17-2 (Time 30–40 minutes) Purpose—The student is required to prepare journal entries and adjusting entries for available-for-sale debt investments,along with an amortizationscheduleanda discussionoffinancialstatementpresentation. Problem 17-3 (Time 25–30 minutes) Purpose—to provide the student with an understanding of the differentiation in accounting treatments for debt and equity security investments. The student is required to prepare the necessary journal entries to properly reflect transactions relating to available-for-sale debt and equity investments. Problem 17-4 (Time 25–35 minutes) Purpose—the student is required to distinguish between the existence of a bond premium or discount. The student is also required to prepare the adjusting entries at two year-ends for available-for-sale debt investments. Problem 17-5 (Time 25–35 minutes) Purpose—the student is required to prepare journal entries for the sale and purchase of available-for- sale equity investments along with the year-end adjusting entry for unrealized holding gains or losses and to discuss the financial statement presentation. Problem 17-6 (Time 25–35 minutes) Purpose—the student is required to prepare during-the-year and year-end entries for trading equity investments and to explain how the entries would differ if the securities were classified as available-for- sale. Problem 17-7 (Time 25–35 minutes) Purpose—the student is required to prepare during-the-year and year-end entries for available-for-sale debt investments and to explain how the entries would differ if the securities were classified as held-to- maturity. Problem 17-8 (Time 20–30 minutes) Purpose—to provide the student with an understanding of the accounting for trading and available-for- sale equity investments. The student is required to apply the fair value method to both classes of securities and describe how they would be reflected in the body and notes to the financial statements. There is also a requirement involving the equity method. Problem 17-9 (Time 20–30 minutes) Purpose—to provide the student with an understanding of the proper accounting treatment with respect to available-for-sale equity investments and the resulting effect of a reclassification from available-for- sale to trading status. The student is required to discuss the descriptions and amounts which would be reported on the face of the balance sheet with regard to these investments, plus prepare any necessary note disclosures. Problem 17-10 (Time 20–30 minutes) Purpose—to provide the student with an opportunity to prepare entries for available-for-sale transactions and to report the results in a comprehensive income statement and a balance sheet. 36. 17-36 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) Time and Purpose of Problems (Continued) Problem 17-11 (Time 30–40 minutes) Purpose—to provide the student with an understanding of the reporting problems associated with available-for-sale equity investments. Description and amounts that should be reported on a company's comparative financial statements are then required. Problem 17-12 (Time 20–30 minutes) Purpose—to provide the student with an understanding of the reporting problems associated with available-for-sale equity investments. Description and amounts that should be reported on a company's comparative financial statements are then required. *Problem17-13 (Time 20–25 minutes) Purpose—the student is required to prepare the entries at purchase, throughout the life, and at expiration for a stand-alone derivative (call option). *Problem 17-14 (Time 20–25 minutes) Purpose—the student is required to prepare the entries at purchase, throughout the life, and at expiration for a stand-alone derivative (put option). *Problem 17-15 (Time 20–25 minutes) Purpose—the student is required to prepare the entries at purchase, throughout the life, and at expiration for a stand-alone derivative (put option). *Problem 17-16 (Time 30-40 minutes) Purpose—the student is provided with an opportunity to prepare the entries for a fair value hedge in the context of an interest rate swap, including how the effects of the swap will be reported in the financial statements. *Problem 17-17 (Time 25–35 minutes) Purpose—the student is provided with an opportunity to prepare the entries for a cash flow hedge in the context of an option contract on the purchase of inventory, including how the effects of the hedge will be reported in the financial statements. *Problem 17-18 (Time 25–35 minutes) Purpose—the student is provided with an opportunity to prepare the entries for a fair value hedge in the context of the use of a put option to hedge an available-for-sale security, including how the effects for the hedging instrument and hedged item will be reported in the financial statements. 37. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-37 SOLUTIONS TO PROBLEMS PROBLEM 17-1 (a) December 31, 2012 Debt Investments.................... 108,660 Cash.................... 108,660 (b) December 31, 2013 Cash.................... 7,000 Debt Investments.................... 1,567 Interest Revenue.................... 5,433 (c) December 31, 2015 Cash.................... 7,000 Debt Investments.................... 1,728 Interest Revenue.................... 5,272 (d) December 31, 2012 Debt Investments (available-for-sale)........... 108,660 Cash.................... 108,660 (e) December 31, 2013 Cash.................... 7,000 Debt Investments (available-for-sale).. 1,567 Interest Revenue.................... 5,433 Unrealized HoldingGain or Loss—Equity ($107,093 – $106,500).................... 593 Fair Value Adjustment (available-for-sale).................... 593 38. 17-38 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-1 (Continued) (f) December 31, 2015 Cash.................... 7,000 Debt Investments (available-for-sale)... 1,728 Interest Revenue.................... 5,272 Debt Investments (available-for-sale) Amortized Cost Fair Value Unrealized Gain (Loss) SpanglerCompany,7% bonds $103,719 $105,650 $1,931 Previousfair value adjustment—Dr. 2,053* Fair value adjustment—Cr. $ (122) *($107,500 – $105,447) Unrealized Holding Gain or Loss—Equity.................... 122 Fair Value Adjustment (available-for-sale)......... 122 39. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-39 PROBLEM 17-2 (a) January 1, 2014 purchase entry: Debt Investments (available-for-sale).................... 369,114 Cash.................... 369,114 (b) The amortization schedule is as follows: Schedule of Interest Revenue and Bond Discount Amortization—Effective-Interest Method 8% Bonds Purchased to Yield 10% Date Interest Receivable Or Cash Received Interest Revenue Bond Discount Amortization Carrying Amount of Bonds 1/1/14 $369,114 7/1/14 16,000 $ 18,456 $ 2,456 371,570 12/31/14 16,000 18,579 2,579 374,149 7/1/15 16,000 18,707 2,707 376,856 12/31/15 16,000 18,843 2,843 379,699 7/1/16 16,000 18,985 2,985 382,684 12/31/16 16,000 19,134 3,134 385,818 7/1/17 16,000 19,291 3,291 389,109 12/31/17 16,000 19,455 3,455 392,564 7/1/18 16,000 19,628 3,628 396,192 12/31/18 16,000 19,808* 3,808 400,000 Total $160,000 $190,886 $30,886 *$2 difference due to rounding. (c) Interestentries: July 1, 2014 Cash.................... 16,000 Debt Investments (available-for-sale).................... 2,456 Interest Revenue.................... 18,456 December 31, 2014 Interest Receivable.................... 16,000 Debt Investments (available-for-sale).................... 2,579 Interest Revenue.................... 18,579 40. 17-40 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-2 (Continued) (d) December 31, 2015 adjusting entry: Securities Available-for-Sale Portfolio Cost Fair Value Unrealized Gain (Loss) Aguirre (total portfolio value) * $379,699* $372,726 $ (6,973) Previousfair value adjustment—Dr. 3,375 Fair value adjustment— Cr. $(10,348) *This is the amortized costof the bonds on December 31, 2015.See (b) schedule. December 31, 2015 Unrealized Holding Gain or Loss—Equity........... 10,348 Fair Value Adjustment (available-for-sale).................... 10,348 (e) January 1, 2016 sale entry: Selling price of bonds.................... $370,726 Less: Amortized cost (see schedule from (b)).... (379,699) Realized loss on sale of investment (available-for-sale).................... $ (8,973) January 1, 2016 Cash.................... 370,726 Loss on Sale of Investments.................... 8,973 Debt Investments (available-for-sale)........... 379,699 41. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-41 PROBLEM 17-3 (a) Debt Investments (available-for-sale).................... 162,000* Equity Investments (available-for-sale)................ 37,400 Interest Revenue ($50,000 X .12 X 4/12).................... 2,000 Investments.................... 201,400 *[$110,000 + ($50,000 X 1.04)] (Note to instructor: Somestudentsmay debitInterestReceivableatdate of purchase instead of Interest Revenue. This procedure is correct, assumingthat when the cash is receivedfor the interest,an appropriate credit to Interest Receivable is recorded.) (b) December 31, 2014 Interest Receivable.................... 8,025 Debt Investments (available-for-sale)........... 51 Interest Revenue.................... 7,974 [Accrued interest [$50,000 X .12 X 10/12 = $5,000 [Premium amortization [6/236 X $2,000 = (51) [Accrued interest [$110,000 X .11 X 3/12 = 3,025 $7,974] (c) December 31, 2014 Available-for-Sale Portfolio Securities Cost Fair Value Unrealized Gain (Loss) Sharapova Company stock $ 37,400 $ 31,800 $ (5,600) U.S. governmentbonds 110,000 124,700 14,700 McGrath Companybonds 51,949* 58,600 6,651 Total $199,349 $215,100 15,751 Previousfair value adjustmentbalance 0 Fair value adjustment—Dr. $15,751 *($50,000 X 1.04) – $51 42. 17-42 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-3 (Continued) Fair Value Adjustment (available-for-sale)......... 15,751 Unrealized Holding Gain or Loss—Equity... 15,751 (d) July 1, 2015 Cash ($119,200 + $3,025).................... 122,225 Debt Investments (available-for-sale)........... 110,000 Interest Revenue ($110,000 X .11 X 3/12)..... 3,025 Gain on Sale of Investments.................... 9,200 43. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-43 PROBLEM 17-4 (a) The bonds were purchased at a discount.Thatis, they were purchased at less than their face value because the bonds' amortized cost increased from $491,150 to $550,000. (b) December 31, 2014 Fair Value Adjustment (available-for-sale).............. 4,850 Unrealized Holding Gain or Loss—Equity........ 4,850 Available-for-Sale Portfolio Amortized Cost Fair Value Unrealized Gain (Loss) Debt Investment $491,150 $497,000 $5,850 Previousfair value adjustment—Dr. 1,000 Fair value adjustment—Dr. $4,850 (c) December 31, 2015 Unrealized Holding Gain or Loss—Equity............... 16,292 Fair Value Adjustment (available-for-sale)....... 16,292 Available-for-Sale Portfolio Amortized Cost Fair Value Unrealized Gain (Loss) Debt Investment $519,442 $509,000 $(10,442) Previous fair value adjustment—Dr. 5,850 Fair value adjustment—Cr. needed to bring balance to $10,442 Cr. $(16,292) 44. 17-44 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-5 (a) Gross selling price of 3,000 shares at $22............. $66,000 Less: Commissions, taxes, and fees.................... (2,150) Net proceeds from sale.................... 63,850 Cost of 3,000 shares.................... (58,500) Gain on sale of investments.................... $ 5,350 January 15, 2015 Cash.................... 63,850 Equity Investments (available-for-sale).......... 58,500 Gain on Sale of Investments.................... 5,350 (b) The total purchaseprice is: (1,000 X $33.50)+ $1,980 = $35,480. The purchase entrywill be: April 17, 2015 Equity Investments (available-for-sale).................... 35,480 Cash.................... 35,480 (c) Available-for-Sale Portfolio—December 31, 2015 Securities Cost Fair Value Unrealized Gain (Loss) MunterLtd. $580,000 $610,000 ($30,000 King Co. 255,000 240,000 (15,000) Castle Co. 35,480 29,000 (6,480) Totalof portfolio $870,480 $879,000 (8,520 Previousfair value adjustmentbalance—Cr. (10,100) Fair value adjustment—Dr. $18,620 December 31, 2015 Fair Value Adjustment (available-for-sale)............ 18,620 Unrealized Holding Gain or Loss—Equity...... 18,620 (d) The unrealized holding gains or losses should be reported on the bal- ance sheet under the title "accumulated other comprehensive income" as a separate component of stockholders' equity. 45. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-45 PROBLEM 17-6 (a) (1) October 10, 2014 Cash (5,000 X $54).................... 270,000 Gain on Sale of Investments.................... 55,000 Equity Investments (trading).................... 215,000 (2) November 2, 2014 Equity Investments (trading).................... 163,500 Cash (3,000 X $54.50).................... 163,500 (3) At September 30, 2014, McElroy had the following fair value adjustment: Trading SecuritiesPortfolio—September30, 2014 Securities Cost Fair Value Unrealized Gain (Loss) Horton, Inc. common $215,000 $200,000 ($(15,000) Monty,Inc. preferred 133,000 140,000 (7,000) OakwoodCorp.common 180,000 179,000 ((1,000) Totalof portfolio $528,000 $519,000 ((9,000) Previousfair value adjustment balance (0) Fair value adjustment—Cr. ($ (9,000) 46. 17-46 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-6 (Continued) At December 31, 2014, McElroy had the following fair value adjustment: Trading SecuritiesPortfolio—December31, 2014 Securities Cost Fair Value Unrealized Gain (Loss) Monty,Inc. preferred $133,000 $106,000 ($(27,000) OakwoodCorp.common 180,000 193,000 13,000) Patriotcommon 163,500 132,000 ((31,500) Totalof portfolio $476,500 $431,000 (45,500) Previousfair value adjustment balance—Cr. (9,000) Fair value adjustment—Cr. ($(36,500) The entry on December 31, 2014 is therefore as follows: Unrealized Holding Gain or Loss—Income...... 36,500 Fair Value Adjustment (trading)................ 36,500 (b) The entries would be the same except that instead of debiting and crediting accountsassociatedwith tradingsecurities,the accounts used would be associated with available-for-sale securities. In addition, the Unrealized Holding Gain or Loss—Equity account is used instead of Unrealized Holding Gain or Loss—Income. The Unrealized Holding Loss—Equity is includedin othercomprehensive incomeandthenwould be reported on the balance sheet in Accumulated comprehensive income. 47. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-47 PROBLEM 17-7 (a) February1 Debt Investments (available-for-sale).................... 300,000 Interest Revenue (4/12 X .10 X $300,000)................ 10,000 Cash.................... 310,000 April 1 Cash.................... 15,000 Interest Revenue ($300,000 X .10 X 6/12)......... 15,000 July 1 Debt Investments (available-for-sale).................... 200,000 Interest Revenue (1/12 X .09 X $200,000)................ 1,500 Cash.................... 201,500 September 1 Cash [($60,000 X 99%) + ($60,000 X .10 X 5/12)]..... 61,900 Loss on Sale of Investments.................... 600 Debt Investments (available-for-sale)............. 60,000 InterestRevenue (5/12 X .10 X $60,000 = $2,500).................... 2,500 October 1 Cash [($300,000 – $60,000) X .10 X 6/12]................ 12,000 Interest Revenue.................... 12,000 December 1 Cash ($200,000 X 9% X 6/12).................... 9,000 Interest Revenue.................... 9,000 48. 17-48 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-7 (Continued) December 31 Interest Receivable.................... 7,500 Interest Revenue.................... 7,500 (3/12 X $240,000X .10 = $6,000) (1/12 X $200,000X .09 = $1,500) ($6,000 + $1,500 = $7,500) December 31 Unrealized Holding Gain or Loss—Equity............ 26,000 Fair Value Adjustment (available-for-sale).... 26,000 Available-for-Sale Portfolio Security Cost Fair Value Unrealized Gain (Loss) Gibbons Co. $240,000 $228,000* $(12,000) Sampson,Inc. 200,000 186,000** (14,000) Total $440,000 $414,000 $(26,000) *$240,000 X 95% **$200,000 X 93% (Note to instructor: Somestudentsmay debitInterestReceivableatdate of purchase instead of Interest Revenue. This procedure is correct, assumingthat when the cash is receivedfor the interest,an appropriate credit to Interest Receivable is recorded.) (b) All the entries would be the same except the account title Debt Investments (held-to-maturity)wouldbeusedinsteadofDebtInvestments (available-for-sale). In addition, held-to-maturity securities would be carriedat amortized costand notvalued atfair value at year-end,so the last entry would not be made. 49. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-49 PROBLEM 17-8 (a) 1. Investmentin trading securities: Unrealized Holding Gain or Loss—Income........... 80,000 Fair Value Adjustment (trading).................... 80,000 2. Investmentin available-for-salesecurities: Fair Value Adjustment (available-for-sale)........... 725,000 Unrealized Holding Gain or Loss—Equity..... 725,000 Computations: 1. Security Cost Fair Value Unrealized Gain (Loss) Delaney Motors $1,400,000 $1,600,000 ($(200,000 Patrick Electric 1,000,000 720,000 ((280,000) Totalof portfolio $2,400,000 $2,320,000 ($ (80,000) 2. Computationof Unrealized Gain or Loss in 2013 Security Cost Fair Value Unrealized Gain (Loss) Norton Ind. $22,500,000 $21,500,000 (($1,000,000) Computationof Unrealized Gain or Loss in 2014 Security Cost Fair Value Unrealized Gain (Loss) Norton Ind. $22,500,000 $22,225,000 $ (275,000) PreviousFair Value Adjustment(Cr) (1,000,000) Fair Value Adjustment (Dr) $ 725,000 50. 17-50 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-8 (Continued) (b) The unrealized holding loss on the valuation of Brooks' trading securities is reported on the income statement. The loss would appearin the "Other expenses and losses" section of the income statement. The Fair Value Adjustment is a valuation account and it will be used to show the reduction in the fair value of the trading securities. The trading securities portfolio is disclosed in the balance sheetas a currentasset and reported at its fair value. The unrealizedholding gain onthe valuationofBrooks'available-for-sale securitiesis reportedas other comprehensiveincome and as a separate component of stockholders' equity. The Fair Value Adjustment account is used to report the increase in fair value of the available-for-sale securities.The fair valueof the securities is reported in the Investments section of the balance sheet. It should be noted that a combined statement of income and comprehensive income, a statement of comprehensive income, or a statement of stockholders' equity would report the components of comprehensive income. The note disclosures for the available-for-sale securities include the aggregate fair value, gross unrealized holding gains, and gross un- realized holding losses. Any change in the net unrealized holding gain or loss account should also be disclosed. The disclosure for trading securitiesincludesthe changein net unrealized holding gains or losses which was included in earnings. (c) Equity Investments (Norton Industries).................... 125,000 Investment Income ($500,000 X 25%) .... 125,000 Cash ($100,000 X 25%).................... 25,000 Equity Investments (Norton Industries) .... 25,000 With 25% ownership, Brooks has significant influence and should apply the equity method. No fair value adjustments are recorded under the equity method. 51. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-51 PROBLEM 17-9 (a) Available-for-Sale Portfolio Securities Cost Fair Value Unrealized Gain (Loss) Frank,Inc. $ 22,000 $ 32,000 ($(10,000) Ellis Corp. 115,000 95,000 (20,000) Mendota Company 124,000 96,000 ((28,000) Totalof portfolio $261,000 $223,000 ($(38,000) Balance Sheet—December 31, 2014 Long-term investments: Equity Investments (available-for-sale).......... $261,000 Less: Fair value adjustment .... 38,000 Equity Investments(available-for-sale), at fair value.................... $223,000 Stockholders'equity: Common stock.................... $ xx Paid-in capital in excessof par— common stock.................... xx Retained earnings.................... xx Accumulated other comprehensive loss........ (38,000) Total stockholders' equity .... $ xx (b) Available-for-Sale Portfolio Securities Cost Fair Value Unrealized Gain (Loss) Ellis Corp. $115,000 $140,000 ($ 25,000 Mendota Company 174,000* 138,000** ((36,000) Totalof portfolio $289,000 $278,000 ($(11,000) Previousfair value adjustmentbalance—Cr. ((38,000) Fair Value Adjustment—Dr. ($27,000 *(4,000 X $31) + (2,000 X $25) **[(4,000 + 2,000)X $23] 52. 17-52 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-9 (Continued) Balance Sheet—December 31, 2015 Long-term investments: Equity investments(available-for-sale), at cost.................... $289,000 Less: Fair value adjustment.................... 11,000 Equity investments(available-for-sale), at fair value.................... $278,000 Stockholders'equity: Common stock.................... $ xx Paid-in capital in excessof par— common stock .... xx Retained earnings .... xx Accumulated other comprehensive loss.... (11,000) Total stockholders' equity.................... $ xx The Frank security is transferredto the trading security categoryat fair value, which is the new cost basis of the security. The unrealized holding loss of $6,000 [($11 – $8) X 2,000] is recognized in earnings at the date of the transfer. 53. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-53 PROBLEM 17-10 (a) January 1, 2014 Fair value of available-for-sale securities................ $240,000 Accumulated other comprehensive income .... (30,000) Cost basis.................... $210,000 December 31, 2014 Fair value of available-for-sale securities................ $190,000 Cost basis.................... (140,000) Accumulated other comprehensive income .... $ 50,000 Cash ($70,000 + $30,000).................... 100,000 Gain on Sale of Investments.................... 30,000 Equity Investments (available-for-sale)........... 70,000* *($210,000 – $140,000) (b) ACKER INC. Statement of Comprehensive Income For the Year Ended December 31, 2014 Net income.................... $35,000 Other comprehensiveincome Unrealized holding gain.................... 20,000 Comprehensive income.................... $55,000 Acker will provide the following disclosure for Accumulatedother comprehensiveincome: Beginning balance, January 1, 2014 $30,000 Currentperiod other comprehensive income $50,000** Amount reclassified from accumulated other comprehensive income 30,000 Unrealized holding gain 20,000 Ending balance, December 31, 2014 $50,000 54. 17-54 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-10 (Continued) **Accumulated other comprehensive income 12/31/14.................... $50,000 Accumulated other comprehensive income 1/1/14.................... 30,000 Increase in unrealized holding gain .... 20,000 Realized holding gain .... 30,000 Total holding gains arising during period .... $50,000 (c) ACKER INC. Balance Sheet As of December 31, 2014 Assets Stockholders'Equity Cash $155,000* Common stock $260,000 Equity investments (available-for-sale) 190,000 Retained earnings Accumulatedother 35,000 comprehensiveincome 50,000 Totalassets $345,000 Totalequity $345,000 *Beginning balance .... $ 50,000 Dividend revenue.................... 5,000 Cash proceeds on sale .... 100,000 $155,000 55. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-55 PROBLEM 17-11 (a) 1. 3/1/14 Cash.................... 1,800 Dividend Revenue (900 X $2)...... 1,800 2. 4/30/14 Cash .... 3,300 Gain on Sale of Investments .... 600* Equity Investments (available-for-sale).................... 2,700 *(300 X ($11 – $9)) 3. 5/15/14 Equity Investments(available- for-sale).................... 1,600 Cash (100 X $16).................... 1,600 4. 12/31/14 Fair Value Adjustment(available- for-sale).................... 8,500 Unrealized HoldingGain or Loss—Equity.................... 8,500 Security Cost Fair Value Unrealized Gain (Loss) Evers Comp.($15,000+ $1,600) $16,600 $18,700(1) $ 2,100 Rogers Comp. 18,000 17,100(2) (900) ChanceComp.($4,500– $2,700) 1,800 1,600(3) (200) Totalof portfolio $36,400 $37,400 $ 1,000 Previousfair value adjustmentbal.—Cr. (7,500) Fair value adjustment—Dr. $ 8,500 (1) [(1,000 + 100) X $17] (2) (900 X $19) (3) [(500 – 300) X $8] 5. 2/1/15 Cash .... 1,600 Losson Sale of Investments [200 X ($8 – $9)].................... 200 Equity Investments (available-for-sale).................... 1,800 6. 3/1/15 Cash .... 1,800 Dividend Revenue.................... 1,800 56. 17-56 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-11 (Continued) 7. 12/21/15 Dividend Receivable .... 3,300 Dividend Revenue (1,100 X $3).... 3,300 8. 12/31/15 Fair Value Adjustment (available-for-sale).................... 4,200 Unrealized HoldingGain or Loss—Equity.................... 4,200 Security Cost Fair Value Unrealized Gain (Loss) Evers Comp. $16,600 $20,900(1) $4,300 Rogers Comp. 18,000 18,900(2) 900 Totalof portfolio $34,600 $39,800 $5,200 Previousfair value adjustmentbal.—Dr. 1,000 Fair value adjustment—Dr. $4,200 (1) (1,100 X $19) (2) (900 X $21) (b) PartialBalance Sheetas of December 31, 2014 December 31, 2015 CurrentAssets Dividend receivable $ 0 $ 3,300 Investments Equity investments(available- for-sale),at fair value 37,400 39,800 Stockholders'equity Accumulatedother comprehensive income 1,000 5,200 57. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-57 PROBLEM 17-12 (a) Balance Sheet Equity Investments (available-for-sale), at fair value.......... $123,000 (Reported as currentor noncurrentbasedon intent) Unrealized Holding Loss (available-for-sale).................... $ 4,000 ($127,000 – $123,000)(reported as a separate componentof stockholders'equity as a deductionand identified as accumulated other comprehensive loss) Income Statement No effect (b) Balance Sheet Equity Investments (available-for- sale), at fair value.......... $94,000 (Reported as currentor noncurrentbasedon intent) Unrealized Holding Loss (available-for-sale).................... $42,000 ($136,000 – $94,000)(reported as a separate componentof stockholders'equity as a deductionand identified as accumulated other comprehensive loss) Income Statement Other Expensesand Losses Loss on Sale of Investments.................. $1,800* *The entry made to recognize the loss on sale is as follows: Cash.................... 38,200 Loss on Sale of Investments.................... 1,800 Equity Investments (available-for-sale).... 40,000 58. 17-58 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) PROBLEM 17-12 (Continued) (c) Balance Sheet Equity investments (available-for-sale), at fair value.......... $88,000 (Reported as currentor noncurrentbasedon intent) Unrealized holding gain (available-for-sale).................... $ 8,000 ($88,000– $80,000)(reportedas a separate component of stockholders'equity as an addition and identified as accumulated other comprehensive gain) Income Statement Other expensesand losses Loss on Sale of Investments ($8,100 + $2,700).......... $10,800 The entry made to recordthe sale of Lindsay Jones'stock was: Cash.................... 39,900 Loss on Sale of Investments.................... 8,100 Equity Investments(available-for-sale) ($15,000 + $33,000).................... 48,000 (d) (1) Statementof Comprehensive Income Reports unrealized holding loss of $4,000 as part of comprehen- sive income. (2) Statementof Comprehensive Income Unrealized holding loss.................... $38,000* * ($42,000 – $4,000) 59. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-59 *PROBLEM 17-13 (a) July 7, 2014 Call Option .... 240 Cash.................... 240 (b) September 30, 2014 Call Option .... 1,400 Unrealized HoldingGain or Loss—Income ($7 X 200).................... 1,400 Unrealized Holding Gain or Loss—Income........... 60 Call Option ($240–$180).................... 60 (c) December 31, 2014 Unrealized Holding Gain or Loss—Income........... 400 Call Option ($2 X 200).................... 400 Unrealized Holding Gain or Loss—Income........... 115 Call Option ($180 – $65).................... 115 (d) January 4, 2015 Call Option ($1 X $200).................... 200 Unrealized Holding Gain or Loss—Income..... 200 Unrealized Holding Gain or Loss—Income........... 35 Call Option ($65 – $30).................... 35 Cash (200 X $6).................... 1,200 Loss on Settlement of Call Option .... 30 Call Option*.................... 1,230 *Value of Call Option at Settlement: Call Option 240 1,400 60 200 400 115 35 1,230 60. 17-60 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) *PROBLEM 17-14 (a) July 7, 2014 Put Option.................... 240 Cash .... 240 (b) September 30, 2014 Unrealized Holding Gain or Loss—Income............ 115 Put Option ($240 – $125).................... 115 (c) December 31, 2014 Unrealized Holding Gain or Loss—Income............ 75 Put Option ($125 – $50).................... 75 (d) January 31, 2015 Loss on Settlement of Put Option .... 50 Put Option ($50 – $0).................... 50 61. Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) 17-61 *PROBLEM 17-15 (a) January 7, 2014 Put Option .... 360 Cash.................... 360 (b) March31, 2014 Put Option .... 2,000 Unrealized HoldingGain or Loss—Income ($5 X 400).................... 2,000 Unrealized Holding Gain or Loss—Income........... 160 Put Option ($360 – $200).................... 160 (c) June 30, 2014 Unrealized Holding Gain or Loss—Income........... 800 Put Option ($2 X 400).................... 800 Unrealized Holding Gain or Loss—Income........... 110 Put Option ($200 – $90).................... 110 (d) July 6, 2014 Put Option ($5 X $400).................... 2,000 Unrealized Holding Gain or Loss—Income..... 2,000 Unrealized Holding Gain or Loss—Income........... 65 Put Option ($90 – $25).................... 65 Cash (400 X $8).................... 3,200 Loss on Settlement of Put Option .... 25 Put Option*.................... 3,225 *Value of Put Option at settlement: Put Option 360 2,000 160 2,000 800 110 65 3,225 62. 17-62 Copyright © 2013 John Wiley & Sons, Inc. Kieso, Intermediate Accounting, 15/e, Solutions Manual (For Instructor Use Only) *PROBLEM 17-16 (a) (1) No entry necessary at the date of the swap because the fair value of the swap at inception is zero. (2) June 30, 2015 Interest Expense.................... 400,000 Cash (8% X $10,000,000 X 1/2).................... 400,000 (3) June 30, 2015 Cash .... 50,000 Interest Expense.................... 50,000 InterestReceived (Paid) Swap receivable (8% X $10,000,000 X 1/2)....... $ 400,000 Payable at LIBOR (7% X 10,000,000 X 1/2)....... (350,000) Cash settlement.................... 50,000 (4) June 30, 2015 Notes Payable.................... 200,000 Unrealized Holding Gain or Loss—Income .. 200,000 (5) June 30, 2015 Unrealized Holding Gain or Loss—Income........ 200,000 Swap Contract.................... 200,000 (b) Financial statement presentation as of December 31, 2014 Balance Sheet Liabilities Notes Payable $10,000,000 Income Statement No effect

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