# CHAPTER 12

## Investments

### ASSIGNMENT CLASSIFICATION TABLE

| Learning Objectives | Questions | Brief Exercises | Do It! | Exercises | A Problems | B Problems |
|---|---|---|---|---|---|---|
| 1. Discuss why corporations invest in debt and share securities. | 1 | | | 1 | | |
| 2. Explain the accounting for debt investments. | 2, 3, 4 | 1 | 1 | 2, 3 | 1A, 2A | 1B, 2B |
| 3. Explain the accounting for share investments. | 5, 6, 7, 8, 9, 10 | 2, 3 | 2 | 4, 5, 6, 7, 8 | 2A, 3A, 4A, 5A | 2B, 3B, 4B, 5B |
| 4. Describe the use of consolidated financial statements. | 11 | | | 9 | | |
| 5. Indicate how debt and share investments are reported in financial statements. | 12, 13, 14, 15, 16, 17 | 4, 5, 6, 7, 8 | 3 | 8, 10, 11, 12 | 1A, 2A, 3A, 5A, 6A | 1B, 2B, 3B, 5B, 6B |
| 6. Distinguish between short-term and long-term investments. | 18, 19 | 5, 7, 8 | 4 | 10, 11, 12 | 1A, 2A, 3A, 5A, 6A | 1B, 2B, 3B, 5B, 6B |
| *7. Explain the form and content of consolidated financial statements as well as how to prepare them. | 20, 21 | 9, 10 | | 13, 14 | 7A | 7B |

**Note:** All **asterisked** Question, Exercises, and Problems relate to material contained in the appendix to the chapter.

## ASSIGNMENT CHARACTERISTICS TABLE

| Problem Number | Description | Difficulty Level | Time Allotted (min.) |
|---|---|---|---|
| 1A | Journalize debt investment transactions and show financial statement presentation. | Moderate | 30–40 |
| 2A | Journalize investment transactions, prepare adjusting entry, and show statement presentation. | Moderate | 30–40 |
| 3A | Journalize transactions and adjusting entry for share investments. | Moderate | 30–40 |
| 4A | Prepare entries under the cost and equity methods, and tabulate differences. | Simple | 20–30 |
| 5A | Journalize share investment transactions and show statement presentation. | Moderate | 40–50 |
| 6A | Prepare a statement of financial position. | Moderate | 30–40 |
| *7A | Prepare consolidated worksheet and statement of financial position when cost exceeds book value. | Simple | 30–40 |
| 1B | Journalize debt investment transactions and show financial statement presentation. | Moderate | 30–40 |
| 2B | Journalize investment transactions, prepare adjusting entry, and show statement presentation. | Moderate | 30–40 |
| 3B | Journalize transactions and adjusting entry for share investments. | Moderate | 30–40 |
| 4B | Prepare entries under the cost and equity methods, and tabulate differences. | Simple | 20–30 |
| 5B | Journalize share investment transactions and show statement presentation. | Moderate | 40–50 |
| 6B | Prepare a statement of financial position. | Moderate | 30–40 |
| *7B | Prepare consolidated worksheet and statement of financial position when cost exceeds book value. | Simple | 30–40 |

  

# WEYGANDT FINANCIAL ACCOUNTING, IFRS EDITION, 2e
# CHAPTER 12
# INVESTMENTS

| Number | LO | BT | Difficulty | Time (min.) |
|---|---|---|---|---|
| BE1 | 2 | AP | Simple | 2–4 |
| BE2 | 3 | AP | Simple | 3–5 |
| BE3 | 3 | AP | Simple | 3–5 |
| BE4 | 5 | AP | Simple | 2–3 |
| BE5 | 5, 6 | AN | Simple | 2–4 |
| BE6 | 5 | AN | Simple | 2–3 |
| BE7 | 5, 6 | AP | Simple | 2–4 |
| BE8 | 5, 6 | AP | Simple | 3–5 |
| *BE9 | 7 | AP | Simple | 3–5 |
| *BE10 | 7 | AP | Simple | 3–5 |
| DI1 | 2 | AP | Moderate | 6–8 |
| DI2 | 3 | AP | Simple | 6–8 |
| DI3 | 5 | AN | Simple | 4–6 |
| DI4 | 6 | C | Simple | 4–6 |
| EX1 | 1 | C | Simple | 8–10 |
| EX2 | 2 | AP | Moderate | 8–10 |
| EX3 | 2 | AP | Moderate | 8–10 |
| EX4 | 3 | AP | Simple | 8–10 |
| EX5 | 3 | AP | Simple | 6–8 |
| EX6 | 3 | AP | Simple | 8–10 |
| EX7 | 3 | AP | Simple | 6–8 |
| EX8 | 3, 5 | AP | Simple | 8–10 |
| EX9 | 4 | C | Simple | 6–8 |
| EX10 | 5, 6 | AN | Simple | 4–6 |
| EX11 | 5, 6 | AN | Simple | 8–10 |
| EX12 | 5, 6 | AN | Simple | 6–8 |
| *EX13 | 7 | AP | Simple | 3–5 |
| *EX14 | 7 | AP | Simple | 4–6 |
| P1A | 2, 5, 6 | AN | Moderate | 30–40 |
| P2A | 2, 3, 5, 6 | AN | Moderate | 30–40 |
| P3A | 3, 5, 6 | AN | Moderate | 30–40 |

## INVESTMENTS (Continued)

| Number | LO | BT | Difficulty | Time (min.) |
|---|---|---|---|---|
| P4A | 3 | AN | Simple | 20–30 |
| P5A | 3, 5, 6 | AN | Moderate | 40–50 |
| P6A | 5, 6 | AP | Moderate | 30–40 |
| *P7A | 7 | AP | Moderate | 20–30 |
| P1B | 2, 5, 6 | AN | Moderate | 30–40 |
| P2B | 2, 3, 5, 6 | AN | Moderate | 30–40 |
| P3B | 3, 5, 6 | AN | Moderate | 30–40 |
| P4B | 3 | AN | Simple | 20–30 |
| P5B | 3, 5, 6 | AN | Moderate | 40–50 |
| P6B | 5, 6 | AP | Moderate | 30–40 |
| *P7B | 7 | AP | Moderate | 20–30 |
| BYP1 | 4 | C | Simple | 10–15 |
| BYP2 | 4 | AN | Simple | 10–15 |
| BYP3 | — | C | Simple | 10–15 |
| BYP4 | 3 | C | Moderate | 15–20 |
| BYP5 | 5 | C | Simple | 5–10 |
| BYP6 | 5 | E | Simple | 10–15 |

  

# BLOOM'S TAXONOMY TABLE

**Correlation Chart between Bloom's Taxonomy, Learning Objectives and End-of-Chapter Exercises and Problems**

| Learning Objective | Knowledge | Comprehension | Application | Analysis | Synthesis | Evaluation |
|---|---|---|---|---|---|---|
| 1. Discuss why corporations invest in debt and share securities. | Q12-1 | E12-1 | | | | |
| 2. Explain the accounting for debt investments. | Q12-2 | Q12-3<br>Q12-4 | BE12-1 E12-2<br>DI12-1 E12-3 | P12-1A P12-1B<br>P12-2A P12-2B | | |
| 3. Explain the accounting for share investments. | Q12-7 | Q12-5<br>Q12-8<br>Q12-9<br>Q12-10 | Q12-6 E12-5<br>BE12-2 E12-6<br>BE12-3 E12-7<br>DI12-2 E12-8<br>E12-4 | P12-2A P12-2B<br>P12-3A P12-3B<br>P12-4A P12-4B<br>P12-5A P12-5B | | |
| 4. Describe the use of consolidated financial statements. | Q12-11 | E12-9 | | | | |
| 5. Indicate how debt and share investments are reported in financial statements. | Q12-12<br>Q12-17 | Q12-13 | Q12-14<br>Q12-16<br>BE12-4<br>BE12-7<br>BE12-8<br>E12-8<br>P12-6A<br>P12-6B | Q12-15 P12-2A<br>BE12-5 P12-3A<br>BE12-6 P12-5A<br>DI12-3 P12-1B<br>E12-10 P12-2B<br>E12-11 P12-3B<br>E12-12 P12-5B<br>P12-1A | | |
| 6. Distinguish between short-term and long-term investments. | | Q12-18<br>Q12-19<br>DI12-4 | BE12-7<br>BE12-8<br>P12-6A<br>P12-6B | BE12-5 P12-3A<br>E12-10 P12-5A<br>E12-11 P12-1B<br>E12-12 P12-2B<br>P12-1A P12-3B<br>P12-2A P12-5B | | |
| *7. Explain the form and content of consolidated financial statements as well as how to prepare them. | | Q12-20<br>Q12-21 | BE12-9 P12-7A<br>BE12-10 P12-7B<br>E12-13<br>E12-14 | | | |
| Broadening Your Perspective | | Financial Reporting<br>Real-World Focus<br>Decision-Making Across the Organization<br>Communication | | Comparative Analysis | | Ethics Case |

# ANSWERS TO QUESTIONS

**1.** The reasons corporations invest in securities are: (1) excess cash not needed for operations that can be invested, (2) for additional earnings, and (3) strategic reasons.

**2.** (a) The cost of an investment in bonds consists of all expenditures necessary to acquire the bonds, such as the market price of the bonds plus any brokerage fees.
(b) Interest is recorded as it is earned; that is, over the life of the investment in bonds.

**3.** (a) Losses and gains on the sale of debt investments are computed by comparing the cost of the investment to the net proceeds from the sale.
(b) Gains and losses are reported in the income statement under other income and expense.

**4.** Kolkata Company is incorrect. The gain is the difference between the net proceeds, exclusive of interest, and the cost of the bonds. The correct gain is Rs4,500, or [(Rs45,000 – Rs500) – Rs40,000].

**5.** The cost of an investment in shares includes all expenditures necessary to acquire the investment. These expenditures include the actual purchase price plus any commissions or brokerage fees.

**6.** The entry is:

| | | |
|---|---|---|
| Share Investments | 63,200 | |
| Cash | | 63,200 |

**7.** (a) Whenever the investor's influence on the operating and financial affairs of the associate is significant, the equity method should be used. The major factor in determining significant influence is the percentage of ownership interest held by the investor in the investee. The general guideline for use of the equity method is 20%–50% ownership interest. Companies are required to use judgment, however, rather than blindly follow the 20%–50% guideline.
(b) Revenue is recognized by the investor as it is earned by the associate.

**8.** Since Rijo Corporation uses the equity method, the income reported by Pippen Packing (€80,000) should be multiplied by Rijo's ownership interest (30%) and the result (€24,000) should be debited to Share Investments and credited to Revenue from Share Investments. Also, of the total dividend declared and paid by Pippen (€10,000) Rijo will receive 30% or €3,000. This amount should be debited to Cash and credited to Share Investments.

**9.** Significant influence over an associate may result from representation on the board of directors, participation in policy-making processes, material intercompany transactions. One must also consider whether the shares held by other shareholders is concentrated or dispersed. An investment (direct or indirect) of 20%–50% of the voting shares of an associate constitutes significant influence unless there exists evidence to the contrary.

 

**10.** Under the cost method, an investment is originally recorded and reported at cost. Dividends are recorded as revenue. In subsequent periods, it is adjusted to fair value and an unrealized gain or loss is recognized and included in income (trading security) or as a separate component of equity (non-trading security). Under the equity method, the investment is originally recorded and reported at cost; subsequently, the investment account is adjusted during each period for the investor's share of the earnings or losses of the associate. The investor's share of the associate's earnings is recognized in the earnings of the investor. Dividends received from the associate are reductions in the carrying amount of the investment.

**11.** Consolidated financial statements present the details of the assets and liabilities controlled by the parent company and the total revenues and expenses of the affiliated companies.

Consolidated financial statements are especially useful to the shareholders, board of directors, and management of the parent company.

**12.** Companies classify debt investments into two categories

1. Trading securities are bought and held primarily for sale in the near term to generate income on short-term price differences.
2. Held-for-collection securities are debt securities that the investor has the intent and ability to hold to maturity.

Share investments are classified either as trading or non-trading securities. Share investments have no maturity date and therefore are never classified as held-for-collection securities.

Investments recorded under the equity method are reported at their carrying value. The carrying value is the cost adjusted for the investor's share of the associate's income and dividends received.

**13.** Tina should report as follows:

| | |
|---|---|
| (1) Under current assets in the statement of financial position: | |
| Short-term investment, at fair value | $70,000 |
| (2) Under other income and expense in the income statement: | |
| Unrealized loss—income | $ 4,000 |

**14.** Tina should report as follows:

| | |
|---|---|
| (1) Under investments in the statement of financial position: | |
| Investments in shares of less than 20% owned companies, at fair value | $70,000 |
| (2) Under equity in the statement of financial position: | |
| Less: Unrealized loss on non-trading securities | $ 4,000 |

**15.** The entry is:

| | | |
|---|---|---|
| Fair Value Adjustment—Non-Trading | 10,000 | |
| Unrealized Gain or Loss—Equity | | 10,000 |

**16.** The entry is:

| | | |
|---|---|---|
| Fair Value Adjustment—Trading | 10,000 | |
| Unrealized Gain—Income | | 10,000 |

**17.** Unrealized Loss—Equity is reported as a deduction from equity. The unrealized loss is not included in the computation of net income.

**18.** Reporting Unrealized Gains (Losses)—Equity in the equity section serves two important purposes: (1) it reduces the volatility of net income due to fluctuations in fair value, and (2) it still informs the financial statement user of the gain or loss that would occur if the securities were sold at fair value.

**19.** No. The investment in Key Corporation shares is a long-term investment because there is no intent to convert the shares into cash within a year or the operating cycle, whichever is longer.

***20.** (a) The parent company's investment in the subsidiary's ordinary shares and the subsidiary's equity account balances are eliminated.

(b) The investment account represents an interest in the assets of the subsidiary. The statement of financial position of the subsidiary lists all its assets and liabilities (the net assets). Therefore, there would be a double counting of net assets. Similarly, there would be a double counting in equity because all the ordinary shares of the subsidiary are owned by the shareholders of the parent.

***21.** The remaining excess of HK$8,000,000 [HK$318,000,000 – (HK$290,000,000 + HK$20,000,000)] should be allocated to goodwill and presented in the consolidated statement of financial position as an intangible asset—Goodwill.

  

# SOLUTIONS TO BRIEF EXERCISES

## BRIEF EXERCISE 12-1

| | | | | |
|---|---|---|---|---|
| Jan. | 1 | Debt Investments | 52,000 | |
| | | Cash | | 52,000 |
| July | 1 | Cash | 2,340 | |
| | | Interest Revenue | | 2,340 |

## BRIEF EXERCISE 12-2

| | | | | |
|---|---|---|---|---|
| Aug. | 1 | Share Investments | 35,700 | |
| | | Cash | | 35,700 |
| Dec. | 1 | Cash | 40,000 | |
| | | Share Investments | | 35,700 |
| | | Gain on Sale of Share Investments | | 4,300 |

## BRIEF EXERCISE 12-3

| | | | | |
|---|---|---|---|---|
| Dec. | 31 | Share Investments (25% X €180,000) | 45,000 | |
| | | Revenue from Share Investments | | 45,000 |
| | 31 | Cash (25% X €50,000) | 12,500 | |
| | | Share Investments | | 12,500 |

## BRIEF EXERCISE 12-4

| | | | | |
|---|---|---|---|---|
| Dec. | 31 | Unrealized Loss—Income | 3,000 | |
| | | Fair Value Adjustment—Trading ($62,000 – $59,000) | | 3,000 |

## BRIEF EXERCISE 12-5

**Statement of Financial Position**

| | |
|---|---|
| **Current assets** | |
| Short-term investments, at fair value | $59,000 |

**Income Statement**

| | |
|---|---|
| **Other income and expense** | |
| Unrealized loss—income | 3,000 |

## BRIEF EXERCISE 12-6

| | | | |
|---|---|---|---|
| Dec. 31 | Unrealized Gain or Loss—Equity | 6,000 | |
| | Fair Value Adjustment— Non-Trading | | 6,000 |

## BRIEF EXERCISE 12-7

**Statement of Financial Position**

| | |
|---|---|
| **Investments** | |
| Investments in shares of less than 20% owned companies, at fair value | $66,000 |
| | |
| **Equity** | |
| Less: Unrealized loss on non-trading securities | $ 6,000 |

## BRIEF EXERCISE 12-8

| | |
|---|---|
| **Investments** | |
| Investments in shares of less than 20% owned companies, at fair value | $115,000 |
| Investment in shares of 20–50% owned company, at equity | 270,000 |
| Total investments | $385,000 |

 

## *BRIEF EXERCISE 12-9

| | Paula Company | Shannon Company | Eliminations Dr. | Eliminations Cr. | Consolidated Data |
|---|---|---|---|---|---|
| Investment in Shannon Ordinary Shares | 190,000 | | | 190,000 | 0 |
| Share Capital | | 120,000 | 120,000 | | 0 |
| Retained Earnings | | 70,000 | 70,000 | | 0 |

## *BRIEF EXERCISE 12-10

| | Paula Company | Shannon Company | Eliminations Dr. | Eliminations Cr. | Consolidated Data |
|---|---|---|---|---|---|
| Investment in Shannon Ordinary Shares | 200,000 | | | 200,000 | 0 |
| Excess of Cost Over Book Value of Subsidiary | | | 10,000 | | 10,000 |
| Share Capital | | 120,000 | 120,000 | | 0 |
| Retained Earnings | | 70,000 | 70,000 | | 0 |

## SOLUTIONS FOR DO IT! REVIEW EXERCISES

### DO IT! 12-1

| | | | | |
|---|---|---|---|---|
| (a) | Jan. 1 | Debt Investments | 50,000 | |
| | | Cash | | 50,000 |
| | July 1 | Cash | 3,000 | |
| | | Interest Revenue (£50,000 × 12% × 6/12) | | 3,000 |
| | July 1 | Cash | 29,200 | |
| | | Loss on Sale of Debt Investments | 800 | |
| | | Debt Investments (£50,000 × 30/50) | | 30,000 |
| (b) | Dec. 31 | Interest Receivable | 1,200 | |
| | | Interest Revenue (£20,000 × 12% × 6/12) | | 1,200 |

### DO IT! 12-2

| | | | | |
|---|---|---|---|---|
| (1) | June 17 | Share Investments [(500,000 × 10%) × $11] | 550,000 | |
| | | Cash | | 550,000 |
| | Sept. 3 | Cash | 16,000 | |
| | | Dividend Revenue | | 16,000 |
| (2) | Jan. 1 | Share Investments [(100,000 × 30% × $18] | 540,000 | |
| | | Cash | | 540,000 |
| | May 15 | Cash | 45,000 | |
| | | Share Investments | | 45,000 |
| | Dec. 31 | Share Investments | 81,000 | |
| | | Revenue from Share Investments | | 81,000 |

  

## DO IT! 12-3

***Trading securities:***

| | | |
|---|---|---|
| **Unrealized Loss—Income** | **13,600*** | |
| **Fair Value Adjustment—Trading** | | **13,600** |

***¥11,400 + ¥2,200**

***Non-trading securities:***

| | | |
|---|---|---|
| **Fair Value Adjustment—Non-Trading** | **11,950**** | |
| **Unrealized Gain or Loss—Equity** | | **11,950** |

****¥7,750 + ¥4,200**

## DO IT! 12-4

| Item | Financial statement | Category |
|---|---|---|
| 1. Loss on sale of investments in shares. | Income statement | Other income and expense |
| 2. Unrealized gain on non-trading securities. | Statement of financial position | Equity |
| 3. Fair value adjustment—trading. | Statement of financial position | Current assets |
| 4. Interest earned on investments in bonds. | Income statement | Other income and expense |
| 5. Unrealized loss on trading securities. | Income statement | Other income and expense |

# SOLUTIONS TO EXERCISES

## EXERCISE 12-1

1. **Companies purchase investments in debt or share securities because they have excess cash, to generate earnings from investment income, or for strategic reasons.**

2. **A corporation would have excess cash that it does not need for operations due to seasonal fluctuations in sales and as a result of economic cycles.**

3. **The typical investment when investing cash for short periods of time is low-risk, high liquidity, short-term securities such as government-issued securities.**

4. **The typical investments when investing cash to generate earnings are debt securities and share securities.**

5. **A company would invest in securities that provide no current cash flows for speculative reasons. They are speculating that the investment will increase in value.**

6. **The typical share investment when investing cash for strategic reasons is shares of companies in a related industry or in an unrelated industry that the company wishes to enter.**

## EXERCISE 12-2

| | | | | | |
|---|---|---|---|---|---|
| (a) | Jan. | 1 | Debt Investments | 50,000 | |
| | | | Cash | | 50,000 |
| | July | 1 | Cash ($50,000 X 8% X 1/2) | 2,000 | |
| | | | Interest Revenue | | 2,000 |
| | | 1 | Cash | 33,500 | |
| | | | Debt Investments ($50,000 X 3/5) | | 30,000 |
| | | | Gain on Sale of Debt Investments ($33,500 – $30,000) | | 3,500 |

  

## EXERCISE 12-2 (Continued)

| | | | | |
|---|---|---|---|---|
| (b) | Dec. 31 | Interest Receivable | 800 | |
| | | Interest Revenue ($20,000 X 8% X 1/2) | | 800 |

## EXERCISE 12-3

| | | |
|---|---|---|
| **January 1, 2014** | | |
| Debt Investments | 70,000 | |
| Cash | | 70,000 |
| **July 1, 2014** | | |
| Cash (€70,000 X 12% X 6/12) | 4,200 | |
| Interest Revenue | | 4,200 |
| **December 31, 2014** | | |
| Interest Receivable | 4,200 | |
| Interest Revenue | | 4,200 |
| **January 1, 2015** | | |
| Cash | 4,200 | |
| Interest Receivable | | 4,200 |
| **January 1, 2015** | | |
| Cash | 40,100 | |
| Debt Investments (40/70 X €70,000) | | 40,000 |
| Gain on Sale of Debt Investments | | 100 |

## EXERCISE 12-4

(a)

| | | | | |
|---|---|---|---|---|
| Feb. | 1 | Share Investments | 6,200 | |
| | | Cash | | 6,200 |
| July | 1 | Cash (600 X $1) | 600 | |
| | | Dividend Revenue | | 600 |
| Sept. | 1 | Cash | 4,300 | |
| | | Share Investments ($6,200 X 3/6) | | 3,100 |
| | | Gain on Sale of Share Investments ($4,300 – $3,100) | | 1,200 |
| Dec. | 1 | Cash (300 X $1) | 300 | |
| | | Dividend Revenue | | 300 |

(b) Dividend revenue and the gain on sale of share investments are reported under other income and expense in the income statement.

## EXERCISE 12-5

| | | | | |
|---|---|---|---|---|
| Jan. | 1 | Share Investments | 142,100 | |
| | | Cash | | 142,100 |
| July | 1 | Cash (2,500 X €3) | 7,500 | |
| | | Dividend Revenue | | 7,500 |
| Dec. | 1 | Cash | 31,200 | |
| | | Share Investments (€142,100 X 1/5) | | 28,420 |
| | | Gain on Sale of Share Investments | | 2,780 |
| Dec. | 31 | Cash (2,000 X €3) | 6,000 | |
| | | Dividend Revenue | | 6,000 |

  

## EXERCISE 12-6

| | | |
|---|---|---|
| **February 1** | | |
| Share Investments | 15,400 | |
| Cash (500 X $30.80) | | 15,400 |
| **March 20** | | |
| Cash | 2,850 | |
| Loss on Sale of Share Investments | 230 | |
| Share Investments ($15,400 X 100/500) | | 3,080 |
| **April 25** | | |
| Cash (400 X $1.00) | 400 | |
| Dividend Revenue | | 400 |
| **June 15** | | |
| Cash | 7,310 | |
| Share Investments ($15,400 X 200/500) | | 6,160 |
| Gain on Sale of Share Investments | | 1,150 |
| **July 28** | | |
| Cash (200 X $1.25) | 250 | |
| Dividend Revenue | | 250 |

## EXERCISE 12-7

(a)

| | | | |
|---|---|---|---|
| Jan. 1 | Share Investments | 180,000 | |
| | Cash | | 180,000 |
| Dec. 31 | Cash (₤60,000 X 25%) | 15,000 | |
| | Share Investments | | 15,000 |
| 31 | Share Investments | 50,000 | |
| | Revenue from Share Investments (₤200,000 X 25%) | | 50,000 |

(b)

| | |
|---|---|
| Investment in Morelli, January 1 | ₤180,000 |
| Less: Dividend received | 15,000 |
| Plus: Share of reported income | 50,000 |
| Investment in Morelli, December 31 | ₤215,000 |

 

## EXERCISE 12-8

1\. 2014

| | | | |
|---|---|---|---|
| Mar. 18 | Share Investments.................................. | 390,000 | |
| | Cash (200,000 X 15% X $13)........... | | 390,000 |
| June 30 | Cash.......................................................... | 9,000 | |
| | Dividend Revenue ($60,000 X 15%)........................... | | 9,000 |
| Dec. 31 | Fair Value Adjustment—Non-Trading.... | 60,000 | |
| | Unrealized Gain or Loss—Equity ($450,000 – $390,000) .................. | | 60,000 |

2\.

| | | | |
|---|---|---|---|
| Jan. 1 | Share Investments.................................. | 81,000 | |
| | Cash (30,000 X 30% X $9)................ | | 81,000 |
| June 15 | Cash.......................................................... | 9,000 | |
| | Share Investments ($30,000 X 30%)........................... | | 9,000 |
| Dec. 31 | Share Investments.................................. | 24,000 | |
| | Revenue from Share Investments ($80,000 X 30%)........................... | | 24,000 |

## EXERCISE 12-9

(a) Since Edna owns more than 50% of the ordinary shares of Damen Corporation, Edna is called the parent company. Damen is the subsidiary (affiliated) company. Because of its share ownership, Edna has a controlling interest in Damen.

(b) When a company owns more than 50% of the ordinary shares of another company, consolidated financial statements are usually prepared. Consolidated financial statements present the total assets and liabilities controlled by the parent company. They also present the total revenues and expenses of the affiliated companies.

(c) Consolidated financial statements are useful because they indicate the magnitude and scope of operations of the companies under common control.

  

## EXERCISE 12-10

(a) Dec. 31 Unrealized Loss—Income ............................ 4,000
Fair Value Adjustment—Trading........... 4,000

(b) **Statement of Financial Position**

Current assets
Short-term investments, at fair value...................... CHF49,000

**Income Statement**

Other income and expense
Unrealized loss on trading securities ..................... CHF 4,000

## EXERCISE 12-11

(a) Dec. 31 Unrealized Gain or Loss—Equity ................. 4,000
Fair Value Adjustment—Non-Trading .. 4,000

(b) **Statement of Financial Position**

Investments
Investments in shares of less than 20% owned companies, at fair value ...................................... CHF49,000

Equity
Less: Unrealized loss on non-trading securities .................................................... CHF 4,000

 

**EXERCISE 12-11 (Continued)**

**(c) Dear Ms. Devonshire:**

**Investments which are classified as trading (held for sale in the near term) are reported at fair value in the statement of financial position, with unrealized gains or losses reported in net income. Share investments which are classified as non-trading (held longer than trading) are also reported at fair value, but unrealized gains or losses are reported in the equity section.**

**Fair value is used as a reporting basis because it represents the cash realizable value of the securities. Unrealized gains or losses on trading investments are reported in the income statement because of the likelihood that the securities will be sold at fair value in the near term. Unrealized gains or losses on non-trading securities are reported in equity rather than in income because there is a significant chance that future changes in fair value will reverse unrealized gains or losses. So as to not distort income with these fluctuations, they are reported directly in equity.**

**I hope that the preceding discussion clears up any misunderstandings. Please contact me if you have any questions.**

**Sincerely,**

**Student**

## EXERCISE 12-12

(a) Fair Value Adjustment—Trading

| | | |
|---|---|---|
| Fair Value Adjustment—Trading ($124,000 – $120,000) | 4,000 | |
| Unrealized Gain—Income | | 4,000 |
| | | |
| Unrealized Gain or Loss—Equity | 6,000 | |
| Fair Value Adjustment—Non-Trading | | 6,000 |

(b)

**Statement of Financial Position**

| | |
|---|---|
| Current assets | |
| Short-term investments, at fair value | $124,000 |
| Investments | |
| Investments in shares of less than 20% owned companies, at fair value | 94,000 |
| Equity | |
| Less: Unrealized loss on non-trading securities | $ 6,000 |

**Income Statement**

| | |
|---|---|
| Other income and expense | |
| Unrealized gain on trading securities | $ 4,000 |

## *EXERCISE 12-13

**LENNON COMPANY AND SUBSIDIARY**
**Worksheet—Consolidated Statement of Financial Position**
**January 1, 2014**

| Assets | Lennon Company | Ono Inc. | Eliminations Dr. | Eliminations Cr. | Consolidated Data |
|---|---|---|---|---|---|
| Plant and equipment (net) | 300,000 | 220,000 | | | 520,000 |
| Investment in Ono Inc. ordinary shares | 220,000 | | | 220,000 | 0 |
| Current assets | 60,000 | 50,000 | | | 110,000 |
| Totals | 580,000 | 270,000 | | | 630,000 |
| **Equity and liabilities** | | | | | |
| Share capital—Lennon Co. | 230,000 | | | | 230,000 |
| Share capital—Ono Inc. | | 80,000 | 80,000 | | 0 |
| Retained earnings—Lennon Co. | 170,000 | | | | 170,000 |
| Retained earnings—Ono Inc. | | 140,000 | 140,000 | | 0 |
| Current liabilities | 180,000 | 50,000 | | | 230,000 |
| Totals | 580,000 | 270,000 | 220,000 | 220,000 | 630,000 |

## *EXERCISE 12-14

**LENNON CORPORATION AND SUBSIDIARY**
**Worksheet—Consolidated Statement of Financial Position**
**January 1, 2014**

| Assets | Lennon Corporation | Ono Inc. | Eliminations Dr. | Eliminations Cr. | Consolidated Data |
|---|---|---|---|---|---|
| Plant and equipment (net) | 300,000 | 220,000 | | | 520,000 |
| Investment in Ono Inc. ordinary shares | 225,000 | | | 225,000 | 0 |
| Current assets | 55,000 | 50,000 | | | 105,000 |
| Excess of cost over book value | | | 5,000 | | 5,000 |
| Totals | 580,000 | 270,000 | | | 630,000 |
| **Equity and liabilities** | | | | | |
| Share capital—Lennon Co. | 230,000 | | | | 230,000 |
| Share capital—Ono Inc. | | 80,000 | 80,000 | | 0 |
| Retained earnings—Lennon Co. | 170,000 | | | | 170,000 |
| Retained earnings—Ono Inc. | | 140,000 | 140,000 | | 0 |
| Current liabilities | 180,000 | 50,000 | | | 230,000 |
| Totals | 580,000 | 270,000 | 225,000 | 225,000 | 630,000 |

# SOLUTIONS TO PROBLEMS

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## PROBLEM 12-1A

(a)

| | | | | |
|---|---|---|---|---|
| 2014 | | | | |
| Jan. | 1 | Debt Investments | 2,000,000 | |
| | | Cash | | 2,000,000 |
| July | 1 | Cash (HK$2,000,000 X .08 X 1/2) | 80,000 | |
| | | Interest Revenue | | 80,000 |
| Dec. | 31 | Interest Receivable | 80,000 | |
| | | Interest Revenue | | 80,000 |
| 2017 | | | | |
| Jan. | 1 | Cash | 80,000 | |
| | | Interest Receivable | | 80,000 |
| | 1 | Cash (HK$1,000,000 X 1.06) | 1,060,000 | |
| | | Debt Investments | | 1,000,000 |
| | | Gain on Sale of Debt Investments | | 60,000 |
| July | 1 | Cash (HK$1,000,000 X .08 X 1/2) | 40,000 | |
| | | Interest Revenue | | 40,000 |
| Dec. | 31 | Interest Receivable | 40,000 | |
| | | Interest Revenue | | 40,000 |

  

## PROBLEM 12-1A (Continued)

(b) **Statement of Financial Position**

| | |
|---|---|
| **Current assets** | |
| **Interest receivable** | **HK$ 80,000** |
| | |
| **Investments** | |
| **Debt investments, at fair value** | **HK$2,000,000** |

## PROBLEM 12-2A

| | | | | |
|---|---|---|---|---|
| (a) | Feb. 1 | Share Investments | 32,400 | |
| | | Cash | | 32,400 |
| | Mar. 1 | Share Investments | 20,400 | |
| | | Cash | | 20,400 |
| | Apr. 1 | Debt Investments | 50,000 | |
| | | Cash | | 50,000 |
| | July 1 | Cash ($.60 X 600) | 360 | |
| | | Dividend Revenue | | 360 |
| | Aug. 1 | Cash ($57 X 200) | 11,400 | |
| | | Share Investments [($32,400 ÷ 600) X 200] | | 10,800 |
| | | Gain on Sale of Share Investments | | 600 |
| | Sept. 1 | Cash ($1 X 800) | 800 | |
| | | Dividend Revenue | | 800 |
| | Oct. 1 | Cash ($50,000 X 7% X 1/2) | 1,750 | |
| | | Interest Revenue | | 1,750 |
| | 1 | Cash | 49,000 | |
| | | Loss on Sale of Debt Investments ($50,000 – $49,000) | 1,000 | |
| | | Debt Investments | | 50,000 |

**Share Investments**

| | | | |
|---|---|---|---|
| Feb. 1 | 32,400 | Aug. 1 | 10,800 |
| Mar. 1 | 20,400 | | |
| Dec. 31 Bal. | 42,000 | | |

**Debt Investments**

| | | | |
|---|---|---|---|
| Apr. 1 | 50,000 | Oct. 1 | 50,000 |
| Dec. 31 Bal. | 0 | | |

  

**PROBLEM 12-2A (Continued)**

| | | | | |
|---|---|---|---|---|
| **(b)** | **Dec. 31** | **Unrealized Loss—Income..........................** | **800** | |
| | | **Fair Value Adjustment—Trading** | | |
| | | **($42,000 – $41,200) .........................** | | **800** |

| **Security** | **Cost** | **Fair Value** | |
|---|---|---|---|
| **Superior ordinary shares** | **$21,600** | **$22,000** | **(400 X $55)** |
| **Pawlik ordinary shares** | **20,400** | **19,200** | |
| | **$42,000** | **$41,200** | **(800 X $24)** |

**(c) Current assets**

**Short-term investments, at fair value ..............................  $41,200**

**(d)**

| **Income Statement Account** | **Category** |
|---|---|
| **Dividend Revenue** | **Other income and expense** |
| **Gain on Sale of Share Investments** | **Other income and expense** |
| **Interest Revenue** | **Other income and expense** |
| **Loss on Sale of Debt Investments** | **Other income and expense** |
| **Unrealized Loss—Income** | **Other income and expense** |

# PROBLEM 12-3A

(a)

| | | | |
|---|---|---|---|
| | 2014 | | |
| July 1 | Cash (5,000 X £1) | 5,000 | |
| | Dividend Revenue | | 5,000 |
| | | | |
| Aug. 1 | Cash (2,000 X £0.50) | 1,000 | |
| | Dividend Revenue | | 1,000 |
| | | | |
| Sept. 1 | Cash (1,500 X £8) | 12,000 | |
| | Loss on Sale of Share Investments (£13,500 – £12,000) | 1,500 | |
| | Share Investments (1,500 X £9) | | 13,500 |
| | | | |
| Oct. 1 | Cash (800 X £33) | 26,400 | |
| | Share Investments (800 X £30) | | 24,000 |
| | Gain on Sale of Share Investments (£26,400 – £24,000) | | 2,400 |
| | | | |
| Nov. 1 | Cash (1,500 X £1) | 1,500 | |
| | Dividend Revenue | | 1,500 |
| | | | |
| Dec. 15 | Cash (1,200 X £0.50) | 600 | |
| | Dividend Revenue | | 600 |
| | | | |
| 31 | Cash (3,500 X £1) | 3,500 | |
| | Dividend Revenue | | 3,500 |

**Share Investments**

| | | | | | |
|---|---|---|---|---|---|
| 2014 | | | 2014 | | |
| Jan. 1 | Balance | 135,000 | Sept. 1 | | 13,500 |
| | | | Oct. 1 | | 24,000 |
| 2014 | | | | | |
| Dec. 31 | Balance | 97,500 | | | |

  

**PROBLEM 12-3A (Continued)**

| | | | | |
|---|---|---|---|---|
| **(b)** | **Dec. 31** | **Unrealized Gain or Loss—Equity (£97,500 – £93,400)** | **4,100** | |
| | | **Fair Value Adjustment—Non-Trading** | | **4,100** |

| Security | Cost | Fair Value | |
|---|---|---|---|
| Carlene Co. common | £36,000 | £38,400 | (1,200 × £32) |
| Riverdale Co. common | 31,500 | 28,000 | (3,500 × £ 8) |
| Raczynski Co. common | 30,000 | 27,000 | (1,500 × £18) |
| | £97,500 | £93,400 | |

**(c) Investments**

| | |
|---|---|
| Investments in shares of less than 20% owned companies, at fair value | £ 93,400 |

**Equity**

| | |
|---|---|
| Share capital—ordinary | £1,500,000 |
| Retained earnings | 1,000,000 |
| Less: Unrealized loss on non-trading securities | 4,100 |
| Total equity | £2,495,900 |

## PROBLEM 12-4A

| | | | | | |
|---|---|---|---|---|---|
| (a) | Jan. | 1 | Share Investments................................ | 800,000 | |
| | | | Cash ............................................. | | 800,000 |
| | Mar. | 15 | Cash...................................................... | 13,500 | |
| | | | Dividend Revenue | | |
| | | | (45,000 X $0.30) ......................... | | 13,500 |
| | June | 15 | Cash...................................................... | 13,500 | |
| | | | Dividend Revenue......................... | | 13,500 |
| | Sept. | 15 | Cash...................................................... | 13,500 | |
| | | | Dividend Revenue......................... | | 13,500 |
| | Dec. | 15 | Cash...................................................... | 13,500 | |
| | | | Dividend Revenue......................... | | 13,500 |
| | | 31 | Fair Value Adjustment—Trading......... | 280,000 | |
| | | | Unrealized Gain—Income | | |
| | | | [$800,000 – ($24 X 45,000)]....... | | 280,000 |
| (b) | Jan. | 1 | Share Investments................................ | 800,000 | |
| | | | Cash ............................................. | | 800,000 |
| | Mar. | 15 | Cash...................................................... | 13,500 | |
| | | | Share Investments........................ | | 13,500 |
| | June | 15 | Cash...................................................... | 13,500 | |
| | | | Share Investments........................ | | 13,500 |
| | Sept. | 15 | Cash...................................................... | 13,500 | |
| | | | Share Investments........................ | | 13,500 |
| | Dec. | 15 | Cash...................................................... | 13,500 | |
| | | | Share Investments........................ | | 13,500 |

  

**PROBLEM 12-4A (Continued)**

| | | | |
|---|---|---|---|
| Dec. 31 | Share Investments ............................... | 96,000 | |
| | Revenue from Share Investments ($320,000 X 30%) ...................... | | 96,000 |

(c)

| | Cost Method | Equity Method |
|---|---|---|
| Share Investments | $1,080,000* | $842,000** |
| Unrealized Gain—Income | 280,000 | |
| Dividend Revenue | 54,000 | 0 |
| Revenue from Share Investments | 0 | 96,000 |

*$24 X 45,000 shares
**$800,000 + $96,000 – $54,000

## PROBLEM 12-5A

| | | | | |
|---|---|---|---|---|
| (a) | Jan. 20 | Cash | 54,400 | |
| | | Share Investments | | 52,000 |
| | | Gain on Sale of Share Investments | | 2,400 |
| | 28 | Share Investments | 31,680 | |
| | | Cash (400 X R$79.20) | | 31,680 |
| | 30 | Cash | 1,610 | |
| | | Dividend Revenue (R$1.15 X 1,400) | | 1,610 |
| | Feb. 8 | Cash | 480 | |
| | | Dividend Revenue (R$0.40 X 1,200). | | 480 |
| | 18 | Cash (R$26.70 X 1,200) | 32,040 | |
| | | Loss on Sale of Share Investments | 1,560 | |
| | | Share Investments | | 33,600 |
| | July 30 | Cash | 1,400 | |
| | | Dividend Revenue (R$1.00 X 1,400). | | 1,400 |
| | Sept. 6 | Share Investments | 73,800 | |
| | | Cash (R$82 X 900) | | 73,800 |
| | Dec. 1 | Cash | 1,950 | |
| | | Dividend Revenue (R$1.50 X 1,300) | | 1,950 |

(b)

Share Investments

| | | | |
|---|---|---|---|
| 1/1 Bal. | 169,600 | 1/20 | 52,000 |
| 1/28 | 31,680 | 2/18 | 33,600 |
| 9/6 | 73,800 | | |
| 12/31 Bal. | 189,480 | | |

## PROBLEM 12-5A (Continued)

| | | | | |
|---|---|---|---|---|
| (c) | Dec. 31 | Unrealized Gain or Loss—Equity................. | 6,280 | |
| | | Fair Value Adjustment—Non-Trading (R$189,480 – R$183,200).................. | | 6,280 |

| Security | Cost | Fair Value | |
|---|---|---|---|
| Elderberry Corporation ordinary | R$ 84,000 | R$ 89,600 | (1,400 X R$64) |
| Hachito Corporation ordinary | 105,480 | 93,600 | (1,300 X R$72) |
| | R$189,480 | R$183,200 | |

(d) Investments

| | |
|---|---|
| Investments in shares of less than 20% owned companies, at fair value .......................................... | R$183,200 |

Equity

| | |
|---|---|
| Total share capital and retained earnings .................. | xxxxx |
| Less: Unrealized loss on non-trading securities.......................................................... | 6,280 |
| Total equity .......................................................... | R$ xxxxx |

## PROBLEM 12-6A

**RADAR CORPORATION**
**Statement of Financial Position**
**December 31, 2014**

| | | | |
|---|---|---|---|
| **Assets** | | | |
| **Intangible assets** | | | |
| Goodwill | | | $200,000 |
| **Property, plant, and equipment** | | | |
| Land | | $390,000 | |
| Buildings | $950,000 | | |
| Less: Accumulated depr.—buildings | 180,000 | 770,000 | |
| Equipment | 275,000 | | |
| Less: Accumulated depr.—Equipment | 52,000 | 223,000 | 1,383,000 |
| **Investments** | | | |
| Investments in shares of less than 20% owned companies, at fair value | | 286,000 | |
| Investment in shares of 20%–50% owned company, at equity | | 380,000 | 666,000 |
| **Current assets** | | | |
| Prepaid Insurance | | 16,000 | |
| Inventory | | 170,000 | |
| Accounts receivable | 140,000 | | |
| Less: Allowance for doubtful accounts | 6,000 | 134,000 | |
| Short-term investments, at fair value | | 180,000 | |
| Cash | | 42,000 | 542,000 |
| **Total assets** | | | $2,791,000 |

  

## PROBLEM 12-6A (Continued)

**RADAR CORPORATION**
**Statement of Financial Position (Continued)**
**December 31, 2014**

**Equity and Liabilities**

| | | | |
|---|---|---|---|
| **Equity** | | | |
| Share capital—ordinary, $10 par value, 500,000 shares authorized 150,000 shares issued and outstanding | $1,500,000 | | |
| Share premium—ordinary | 130,000 | $1,630,000 | |
| Retained earnings | | 103,000 | |
| Add: Unrealized gain on Non-trading securities | | 8,000 | $1,741,000 |
| **Non-current liabilities** | | | |
| Bonds payable, 10%, due 2020 | | | 540,000 |
| **Current liabilities** | | | |
| Notes payable | | 70,000 | |
| Accounts payable | | 240,000 | |
| Income taxes payable | | 120,000 | |
| Dividends payable | | 80,000 | 510,000 |
| Total equity and liabilities | | | $2,791,000 |

# *PROBLEM 12-7A

(a)

| | | | |
|---|---|---|---|
| | 2014 | | |
| Dec. 31 | Share Investments | 1,225,000 | |
| | Current Assets | | 1,225,000 |

(b)

**LIU CORPORATION AND SUBSIDIARY**
**Worksheet—Consolidated Statement of Financial Position**
**December 31, 2014**

| Assets | Liu Corporation | Yang Plastics | Eliminations Dr. | Eliminations Cr. | Consolidated Data |
|---|---|---|---|---|---|
| Plant and equipment (net) | 2,100,000 | 676,000 | 86,000 | | 2,862,000 |
| Investment in Yang Plastics ordinary shares | 1,225,000 | | | 1,225,000 | 0 |
| Current assets | 255,000 | 435,500 | | | 690,500 |
| Excess of cost over book value of subsidiary | | | 120,000 | | 120,000 |
| Totals | 3,580,000 | 1,111,500 | | | 3,672,500 |
| **Equity and liabilities** | | | | | |
| Share capital—Liu Corporation | 1,950,000 | | | | 1,950,000 |
| Share capital—Yang Plastics | | 525,000 | 525,000 | | 0 |
| Retained earnings—Liu Corporation | 1,052,000 | | | | 1,052,000 |
| Retained earnings—Yang Plastics | | 494,000 | 494,000 | | 0 |
| Current liabilities | 578,000 | 92,500 | | | 670,500 |
| Totals | 3,580,000 | 1,111,500 | 1,225,000 | 1,225,000 | 3,672,500 |

  

(c)

**LIU CORPORATION AND SUBSIDIARY**
**Consolidated Statement of Financial Position**
**December 31, 2014**

**Assets**

| | | |
|---|---|---|
| Goodwill (¥206,000 − ¥86,000) | | ¥ 120,000 |
| Plant and equipment, net (¥2,776,000 + ¥86,000) | | 2,862,000 |
| Current assets | | 690,500 |
| Total assets | | ¥3,672,500 |

**Equity and Liabilities**

| | | |
|---|---|---|
| Equity | | |
| Share capital—ordinary | ¥1,950,000 | |
| Retained earnings | 1,052,000 | ¥3,002,000 |
| Current liabilities | | 670,500 |
| Total equity and liabilities | | ¥3,672,500 |

## PROBLEM 12-1B

(a)

| | | | |
|---|---|---|---|
| **2014** | | | |
| **Jan. 1** | **Debt Investments** | **400,000** | |
| | **Cash** | | **400,000** |
| | | | |
| **July 1** | **Cash ($400,000 X .09 X 1/2)** | **18,000** | |
| | **Interest Revenue** | | **18,000** |
| | | | |
| **Dec. 31** | **Interest Receivable** | **18,000** | |
| | **Interest Revenue** | | **18,000** |
| | | | |
| **2017** | | | |
| **Jan. 1** | **Cash** | **18,000** | |
| | **Interest Receivable** | | **18,000** |
| | | | |
| **1** | **Cash ($200,000 X 1.14)** | **228,000** | |
| | **Debt Investments** | | **200,000** |
| | **Gain on Sale of Debt Investments** | | **28,000** |
| | | | |
| **July 1** | **Cash ($200,000 X .09 X 1/2)** | **9,000** | |
| | **Interest Revenue** | | **9,000** |
| | | | |
| **Dec. 31** | **Interest Receivable** | **9,000** | |
| | **Interest Revenue** | | **9,000** |

  

## PROBLEM 12-1B (Continued)

**(b)** **Statement of Financial Position**

| | |
|---|---|
| **Current assets** | |
| **Interest receivable....................................................** | **$ 18,000** |
| | |
| **Investments** | |
| **Debt investments, at fair value .................................** | **$400,000** |

## PROBLEM 12-2B

(a)

| | | | | |
|---|---|---|---|---|
| Feb. | 1 | Share Investments | 30,800 | |
| | | Cash | | 30,800 |
| Mar. | 1 | Share Investments | 20,300 | |
| | | Cash | | 20,300 |
| Apr. | 1 | Debt Investments | 40,000 | |
| | | Cash | | 40,000 |
| July | 1 | Cash (₺0.60 X 500) | 300 | |
| | | Dividend Revenue | | 300 |
| Aug. | 1 | Cash | 20,700 | |
| | | Gain on Sale of Share Investments | | 2,220 |
| | | Share Investments [(₺30,800 ÷ 500) X 300] | | 18,480 |
| Sept. | 1 | Cash (₺1 X 600) | 600 | |
| | | Dividend Revenue | | 600 |
| Oct. | 1 | Cash (₺40,000 X 9% X 1/2) | 1,800 | |
| | | Interest Revenue | | 1,800 |
| | 1 | Cash | 44,000 | |
| | | Debt Investments | | 40,000 |
| | | Gain on Sale of Debt Investments (₺44,000 – ₺40,000) | | 4,000 |

**Share Investments**

| | | | |
|---|---|---|---|
| Feb. 1 | 30,800 | Aug. 1 | 18,480 |
| Mar. 1 | 20,300 | | |
| Dec. 31 Bal. | 32,620 | | |

**Debt Investments**

| | | | |
|---|---|---|---|
| Apr. 1 | 40,000 | Oct. 1 | 40,000 |
| Dec. 31 Bal. | 0 | | |

 

## PROBLEM 12-2B (Continued)

(b) Dec. 31 Unrealized Loss—Income........................ 2,020
Fair Value Adjustment—Trading..... 2,020

| Security | Cost | Fair Value | |
|---|---|---|---|
| Joy ordinary | ₺12,320 | ₺13,200 | (200 X ₺66) |
| Aurelius ordinary | 20,300 | 17,400 | (600 X ₺29) |
| | ₺32,620 | ₺30,600 | |

(c) Current assets
Short-term investments, at fair value............................... ₺30,600

(d)

| Income Statement Account | Category |
|---|---|
| Dividend Revenue | Other income and expense |
| Gain on Sale of Share Investments | Other income and expense |
| Interest Revenue | Other income and expense |
| Gain on Sale of Debt Investments | Other income and expense |
| Unrealized Loss—Income | Other income and expense |

## PROBLEM 12-3B

(a)

| | | | |
|---|---|---|---|
| **2014** | | | |
| July 1 | Cash (5,000 X $1) | 5,000 | |
| | Dividend Revenue | | 5,000 |
| | | | |
| Aug. 1 | Cash (4,000 X $0.50) | 2,000 | |
| | Dividend Revenue | | 2,000 |
| | | | |
| Sept. 1 | Cash (1,500 X $8) | 12,000 | |
| | Share Investments (1,500 X $6) | | 9,000 |
| | Gain on Sale of Share Investments | | 3,000 |
| | | | |
| Oct. 1 | Cash (600 X $30) | 18,000 | |
| | Share Investments (600 X $25) | | 15,000 |
| | Gain on Sale of Share Investments ($18,000 – $15,000) | | 3,000 |
| | | | |
| Nov. 1 | Cash (3,000 X $1) | 3,000 | |
| | Dividend Revenue | | 3,000 |
| | | | |
| Dec. 15 | Cash (3,400 X $0.50) | 1,700 | |
| | Dividend Revenue | | 1,700 |
| | | | |
| 31 | Cash (3,500 X $1) | 3,500 | |
| | Dividend Revenue | | 3,500 |

**Share Investments**

| | | | | |
|---|---|---|---|---|
| 2014 | | | 2014 | |
| Jan. 1 | Balance | 190,000 | Sept. 1 | 9,000 |
| | | | Oct. 1 | 15,000 |
| 2014 | | | | |
| Dec. 31 | Balance | 166,000 | | |

  

(b) Dec. 31 Unrealized Gain or Loss—Equity
($166,000 – $159,700) ................................ 6,300
Fair Value Adjustment—
Non-Trading ...................................... 6,300

| Security | Cost | Fair Value | |
|---|---|---|---|
| Trowbridge Co. ordinary | $ 85,000 | $ 78,200 | (3,400 X $23) |
| Holly Co. ordinary | 21,000 | 24,500 | (3,500 X $7) |
| Oriental Motors Co. ordinary | 60,000 | 57,000 | (3,000 X $19) |
| | $166,000 | $159,700 | |

(c) Investments

| | |
|---|---|
| Investments in shares of less than 20% owned companies, at fair value ................................................ | $ 159,700 |

Equity

| | |
|---|---|
| Share capital—ordinary...................... | $2,000,000 |
| Retained earnings .............................. | 1,200,000 |
| Less: Unrealized loss on non-trading securities.................................. | 6,300 |
| Total equity .................................. | $3,193,700 |

## PROBLEM 12-4B

(a)

| | | | | |
|---|---|---|---|---|
| 2014 | | | | |
| Jan. | 1 | Share Investments | 1,100,000 | |
| | | Cash | | 1,100,000 |
| June | 30 | Cash | 20,000 | |
| | | Dividend Revenue (40,000 X $0.50) | | 20,000 |
| Dec. | 31 | Cash | 20,000 | |
| | | Dividend Revenue (40,000 X $0.50) | | 20,000 |
| | 31 | Fair Value Adjustment—Non-Trading | 100,000 | |
| | | Unrealized Gain or Loss—Equity [$1,100,000 – ($30 X 40,000)] | | 100,000 |

(b)

| | | | | |
|---|---|---|---|---|
| 2014 | | | | |
| Jan. | 1 | Share Investments | 1,100,000 | |
| | | Cash | | 1,100,000 |
| June | 30 | Cash | 20,000 | |
| | | Share Investments | | 20,000 |
| Dec. | 31 | Cash | 20,000 | |
| | | Share Investments | | 20,000 |
| | 31 | Share Investments | 120,000 | |
| | | Revenue from Share Investments ($600,000 X 20%) | | 120,000 |

  

(c)

| | Cost Method | Equity Method |
|---|---|---|
| Share Investments | $1,200,000* | $1,180,000** |
| Unrealized Gain—Equity | 100,000 | |
| Dividend Revenue | 40,000 | 0 |
| Revenue from Share Investments | 0 | 120,000 |

*$30 X 40,000 shares
**$1,100,000 + $120,000 – $40,000

 

## PROBLEM 12-5B

(a)

| Date | Account | Debit | Credit |
|---|---|---|---|
| Jan. 7 | Cash (700 X €55) | 38,500 | |
| | Share Investments | | 35,000 |
| | Gain on Sale of Share Investments | | 3,500 |
| 10 | Share Investments | 23,640 | |
| | Cash (300 X €78.80) | | 23,640 |
| 26 | Cash | 1,035 | |
| | Dividend Revenue (€1.15 X 900) | | 1,035 |
| Feb. 2 | Cash | 320 | |
| | Dividend Revenue (€0.40 X 800) | | 320 |
| 10 | Cash (€26 X 800) | 20,800 | |
| | Loss on Sale of Share Investments | 1,600 | |
| | Share Investments | | 22,400 |
| July 1 | Cash | 900 | |
| | Dividend Revenue (€1.00 X 900) | | 900 |
| Sept. 1 | Share Investments | 60,000 | |
| | Cash (€75 X 800) | | 60,000 |
| Dec. 15 | Cash | 1,650 | |
| | Dividend Revenue (€1.50 X 1,100) | | 1,650 |

(b)

**Share Investments**

| | | | |
|---|---|---|---|
| 1/1 Bal. | 99,400 | 1/7 | 35,000 |
| 1/10 | 23,640 | 2/10 | 22,400 |
| 9/1 | 60,000 | | |
| 12/31 Bal. | 125,640 | | |

 

## PROBLEM 12-5B (Continued)

| | | | | |
|---|---|---|---|---|
| (c) | Dec. 31 | Unrealized Gain or Loss—Equity .................... | 3,240 | |
| | | Fair Value Adjustment—Non-Trading | | |
| | | (€125,640 – €122,400) .......................... | | 3,240 |

| Security | Cost | Fair Value | |
|---|---|---|---|
| Ukraine Corporation Ordinary Shares | € 42,000 | € 43,200 | (900 X €48) |
| Vanucci Corporation Ordinary Shares | 83,640 | 79,200 | (1,100 X €72) |
| | €125,640 | €122,400 | |

(d) **Investments**

| | |
|---|---|
| Investments in shares of less than 20% owned companies, at fair value ............................................ | €122,400 |

**Equity**

| | |
|---|---|
| Total share capital and retained earnings ..................... | xxxxx |
| Less: Unrealized loss on non-trading securities ............................................................ | 3,240 |
| Total equity ............................................................ | € xxxxx |

 

## PROBLEM 12-6B

### REDLANDS CORPORATION
### Statement of Financial Position
### December 31, 2014

**Assets**

| | | | |
|---|---|---|---|
| **Intangibles** | | | |
| Goodwill | | | CHF300,000 |
| | | | |
| **Property, plant, and equipment** | | | |
| Land | | CHF780,000 | |
| Buildings | CHF1,350,000 | | |
| Less: Accumulated Depreciation—buildings | 270,000 | 1,080,000 | |
| Equipment | 415,000 | | |
| Less: Accumulated depreciation—equipment | 80,000 | 335,000 | 2,195,000 |
| | | | |
| **Investments** | | | |
| Investment in shares of 20%–50% owned company, at equity | | | 900,000 |
| | | | |
| **Current assets** | | | |
| Prepaid insurance | | 25,000 | |
| Inventory | | 255,000 | |
| Accounts receivable | 135,000 | | |
| Less: Allowance for doubtful accounts | 10,000 | 125,000 | |
| Short-term investments, at fair value | | 280,000 | |
| Cash | | 210,000 | 895,000 |
| **Total assets** | | | CHF4,290,000 |

  

## PROBLEM 12-6B (Continued)

**REDLANDS CORPORATION**
**Statement of Financial Position (Continued)**
**December 31, 2014**

**Equity and Liabilities**

| | | |
|---|---|---|
| **Equity** | | |
| Share capital—ordinary, CHF5 par value, 500,000 shares authorized, 440,000 shares issued and outstanding | CHF2,200,000 | |
| Share premium—ordinary | 300,000 | |
| Retained earnings | 480,000 | CHF2,980,000 |
| **Non-current liabilities** | | |
| Bonds payable, 10%, due 2024 | | 570,000 |
| **Current liabilities** | | |
| Notes payable | 110,000 | |
| Accounts payable | 375,000 | |
| Income taxes payable | 180,000 | |
| Dividends payable | 75,000 | 740,000 |
| **Total equity and liabilities** | | CHF4,290,000 |

# *PROBLEM 12-7B

(a)

| | | | |
|---|---|---|---|
| Dec. 31 | Share Investments | 710,000 | |
| | Current Assets | | 710,000 |

(b)

**PATEL COMPANY AND SUBSIDIARY**
**Worksheet—Consolidated Statement of Financial Position**
**December 31, 2014**

| Assets | Patel Company | Singh Company | Eliminations Dr. | Eliminations Cr. | Consolidated Data |
|---|---|---|---|---|---|
| Plant and equipment (net) | 1,882,000 | 351,000 | 20,000 | | 2,253,000 |
| Investment in Singh Company ordinary shares | 710,000 | | | 710,000 | 0 |
| Current assets | 768,000 | 379,000 | | | 1,147,000 |
| Excess of cost over book value of subsidiary | | | 50,000 | | 50,000 |
| Totals | 3,360,000 | 730,000 | | | 3,450,000 |
| **Equity and Liabilities** | | | | | |
| Share capital—Patel Company | 1,947,000 | | | | 1,947,000 |
| Share capital—Singh Company | | 360,000 | 360,000 | | 0 |
| Retained earnings—Patel Company | 543,000 | | | | 543,000 |
| Retained earnings—Singh Company | | 280,000 | 280,000 | | 0 |
| Current liabilities | 870,000 | 90,000 | | | 960,000 |
| Totals | 3,360,000 | 730,000 | 710,000 | 710,000 | 3,450,000 |

  

***PROBLEM 12-7B (Continued)**

**(c)**

**PATEL COMPANY AND SUBSIDIARY**
**Consolidated Statement of Financial Position**
**December 31, 2014**

| | | |
|---|---|---|
| **Assets** | | |
| Goodwill ($70,000 − $20,000) | | $ 50,000 |
| Plant and equipment, net | | |
| ($2,233,000 + $20,000) | | 2,253,000 |
| Current assets | | 1,147,000 |
| Total assets | | $3,450,000 |
| **Equity and Liabilities** | | |
| Equity | | |
| Share capital—ordinary | $1,947,000 | |
| Retained earnings | 543,000 | $2,490,000 |
| Current liabilities | | 960,000 |
| Total equity and liabilities | | $3,450,000 |

# COMPREHENSIVE PROBLEM: CHAPTERS 11 TO 12

## Part I

(a) To: Mindy Feldkamp, Oscar Lopez, and Lori Melton

From: Joe Student

Date: 5/26/2013

Re: Analysis of Partnership vs. Corporate Form of Business Organization

I have examined your situation regarding the establishment of your business. Before discussing my recommendations, I would like to briefly review the advantages and disadvantages of partnerships and corporations.

The primary advantages of a partnership over a corporation are:

1. Partnerships are more easily formed than corporations. Partnerships can be formed simply by the voluntary agreement of two or more individuals. Forming a corporation requires preparing and filing documents with governmental agencies, paying incorporation fees, etc.

2. Income from a partnership is subject to less tax than income from a corporation. Even though partnerships are required to file information tax returns (returns that show financial information, but do not require any payment of taxes), they are not considered taxable entities. A partner's share of partnership income is taxed only on the partner's personal income tax return. Corporations are taxable entities and pay taxes on corporate income. In addition, any dividends distributed by corporations to individuals are subject to personal income tax on the personal income tax return. This is known as double taxation.

3. Partnerships have more flexibility in decision making. The decision-making process used in a partnership is determined by the partners, whereas some decisions required in corporations must follow formal procedures described in the bylaws of the corporation.

  

**The primary advantages of a corporation over a partnership are:**

1. **Mutual agency does not exist in a corporation. This means that the owners of a corporation (shareholders) do not have the power to bind the corporation beyond their authority. For example, a shareholder who is not employed by the firm cannot enter into contracts or other agreements on behalf of the corporation. Owners of a partnership (partners) are bound by the actions of their partners, even when partners act beyond the scope of their authority. This is true as long as the actions seem appropriate for the business.**

2. **The owners of a corporation have limited liability. When the corporation's assets are not sufficient to pay creditors' claims, the personal assets of the shareholders are protected from the corporation's creditors. In a partnership, once the assets of the partnership have been used to pay creditors' claims, the personal assets of the partners can be taken to satisfy the creditors' demands. A special type of partnership, a limited partnership, protects the personal assets of limited partners, but at least one partner's assets are still at risk. This partner is called a general partner.**

3. **The life of a corporation is unlimited. When ownership changes occur (e.g., shareholders buy or sell shares), the corporation continues to exist as a legal entity. When ownership changes occur in a partnership (e.g., existing partner leaves, new partner is added), the old partnership no longer exists as a legal entity. A new partnership can be formed and the business can continue, but the original partnership must be dissolved.**

**After examining your situation, I believe that you would be wise to choose the corporate form of business organization. There are two reasons for this recommendation. The first reason is that the venture you are about to undertake will require significant capital and, generally, capital is more easily raised via a corporation than a partnership. The other reason is that you will be protected from unlimited liability if you incorporate as opposed to forming a partnership. Given the potential risk of starting a venture of this kind, I believe it is in your best interest to protect your personal assets by using the corporate form of organization.**

**I wish you the best in your new endeavor and please call upon me when you are in need of further assistance.**

## COMPREHENSIVE PROBLEM (Continued)

### Part II

(b) Equity financing option:

| Positives | Negatives |
|---|---|
| No fixed interest payments required | Control of the corporation is lost |
| | Difficulty of finding an interested investor |
| | Earnings per share are lower |

Debt financing option:

| Positives | Negatives |
|---|---|
| Control stays with three incorporators | Interest payments quickly drain cash |
| No need for additional investor | |
| Earnings per share are higher | |

Shares outstanding before financing 60,000 shares

| | Equity Financing | Debt Financing |
|---|---|---|
| Income before interest and taxes | $300,000 | $300,000 |
| Interest expense | — | 126,000 |
| Income before taxes | 300,000 | 174,000 |
| Tax expense | 96,000 | 55,680 |
| Net income | $204,000 | $118,320 |
| Shares outstanding after financing | 200,000 | 60,000 |
| Earnings per share | $ 1.02 | $ 1.97 |

### Part III

| | | | | Debit | Credit |
|---|---|---|---|---|---|
| (c) | 1. | 6/12/13 | Cash | 100,000 | |
| | | | Buildings | 200,000 | |
| | | | Share Capital—Ordinary | | 120,000 |
| | | | Share Premium—Ordinary | | 180,000 |

  

| | | | |
|---|---|---|---|
| 7/21/13 | Cash ............................................ | 900,000 | |
| | Share Capital—Ordinary ...... | | 180,000 |
| | Share Premium—Ordinary... | | 720,000 |
| 7/27/14 | Share Dividends (150,000 X .10 X $3) .................. | 45,000 | |
| | Ordinary Share Dividends Distributable...................... | | 30,000 |
| | Share Premium—Ordinary... | | 15,000 |
| 7/31/14 | No entry | | |
| 8/15/14 | Ordinary Share Dividends Distributable ............................. | 30,000 | |
| | Share Capital—Ordinary ...... | | 30,000 |
| 12/4/14 | Cash Dividends (165,000 X $0.05) ...................... | 8,250 | |
| | Dividends Payable................ | | 8,250 |
| 12/14/14 | No entry | | |
| 12/24/14 | Dividends Payable ........................ | 8,250 | |
| | Cash......................................... | | 8,250 |

2. Shares Issued and Outstanding

| Date | Event | Number of Shares Issued | Total Shares Issued and Outstanding |
|---|---|---|---|
| 6/12/13 | Issuance to Incorporators | 60,000 | 60,000 |
| 7/21/13 | Issuance to Marino | 90,000 | 150,000 |
| 8/15/14 | Share dividend issuance | 15,000 | 165,000 |

<u>Part IV</u>

| | | | |
|---|---|---|---|
| (d) 1. 6/1/15 | Cash ............................................ | 548,000 | |
| | Bonds Payable..................... | | 548,000 |

**COMPREHENSIVE PROBLEM (Continued)**

| | | | | |
|---|---|---|---|---|
| 2. | 12/1/15 | Interest Expense | 20,600 | |
| | | Bonds Payable ($52,000 ÷ 20) | | 2,600 |
| | | Cash ($600,000 X .03) | | 18,000 |
| | | | | |
| 3. | 12/31/15 | Interest Expense | 3,433 | |
| | | Bonds Payable [($52,000 ÷ 20) ÷ 6] | | 433 |
| | | Interest Payable [($600,000 X .03) ÷ 6] | | 3,000 |
| | | | | |
| 4. | 6/1/16 | Interest Payable | 3,000 | |
| | | Interest Expense ($20,600 – $3,433) | 17,167 | |
| | | Cash | | 18,000 |
| | | Bonds Payable ($2,600 – $433) | | 2,167 |

**Part V**

| | | | | | |
|---|---|---|---|---|---|
| (e) | (1) | 2013 | Share Investments | 900,000 | |
| | | | Cash | | 900,000 |
| | | | | | |
| | | | Share Investments | 18,000 | |
| | | | Revenue from Share Investments (.6* X $30,000) | | 18,000 |
| | | | *90,000 ÷ 150, 000 | | |
| | | | | | |
| | | | Cash | 1,260 | |
| | | | Share Investments (.6 X $2,100) | | 1,260 |
| | | | | | |
| | | 2014 | Share Investments | 42,000 | |
| | | | Revenue from Share Investments (.6 X $70,000) | | 42,000 |
| | | | | | |
| | | | Cash | 12,000 | |
| | | | Share Investments (.6 X $20,000) | | 12,000 |

  

**COMPREHENSIVE PROBLEM (Continued)**

| | | Debit | Credit |
|---|---|---|---|
| 2015 | Share Investments ........................ | 63,000 | |
| | Revenue from Share Investments (.6 X $105,000).................... | | 63,000 |
| | Cash ............................................. | 30,000 | |
| | Share Investments (.6 X $50,000)...................... | | 30,000 |

(2) Share Investments

| | |
|---:|---:|
| 900,000 | |
| 18,000 | 1,260 |
| 42,000 | 12,000 |
| 63,000 | 30,000 |
| 979,740 | |

## CCC12 CONTINUING COOKIE CHRONICLE

**(a) 1. The amount of influence you would have in The Beanery would determine how you would account for the investment. Given that you would own 30% of the ordinary shares of The Beanery, it would be assumed (unless there was evidence to the contrary) that you could exert significant influence over the day-to-day operations of the business. This is especially so given the small number of shareholders. Significant influence over an associate may also result from representation on the board of directors, participation in policy-making processes, material intercompany transactions, interchange of managerial personnel, or technological dependency.**

**Assuming significant influence existed, the investment would be accounted for using the equity method of accounting. However, in this case, the Thornton sisters will still exercise majority control and may not be willing to let an investor participate in the decision-making process. If this did occur, significant influence may not exist and the investment would be accounted for using the cost method.**

**2. One of the major advantages of going ahead with this investment would be the strategic advantage of the horizontal and vertical integration that would occur. Not only would you eliminate a competitor but you both could learn the business of roasting beans while taking advantage of the expertise the Thornton sisters have developed with respect to the operation of their coffee shop.**

  

**CCC12 (Continued)**

**(a) (Continued)**

3. **There would be disadvantages associated with this investment as well. For example, there may be a significant time investment required by both of you especially since both of the Thornton sisters are very busy and would like the investor to take over some of the responsibilities of running the business. Also, the Thornton sisters will still exercise majority control and may not be willing to let an investor participate in the decision-making process. Finally, if the investment did not work out, it may be difficult to find another investor to purchase the shares held by Cookie & Coffee Creations.**

**(b)**

| | | |
|---|---|---|
| **Share Investments ...............................................** | **15,000** | |
| **Cash ...........................................................** | | **15,000** |

**(c)**

**Cost Method**

| | | |
|---|---|---|
| **Cash.....................................................................** | **7,500** | |
| **Dividend Revenue ($25,000 X 30%) .............** | | **7,500** |

**Equity Method**

| | | |
|---|---|---|
| **Share Investments ...............................................** | **15,000** | |
| **Revenue from Share Investments** | | |
| **($50,000 X 30%) .......................................** | | **15,000** |
| | | |
| **Cash ($25,000 X 30%)............................................** | **7,500** | |
| **Share Investments .......................................** | | **7,500** |

**CCC12 (Continued)**

**(d) Because the investment in The Beanery is a strategic investment, it would be classified as a long-term investment in the non-current assets section of Cookie & Coffee Creations' statement of financial position. If the investment were accounted for using the cost method, it would be recorded at its original cost of $15,000. If the investment were accounted for using the equity method, it would be accounted for at its original cost plus a proportionate share of The Beanery's income, less a proportionate share of any dividends paid by The Beanery. For the current year the investment would be at $22,500 ($15,000 + $15,000 – $7,500).**

  

## BYP 12-1 FINANCIAL REPORTING PROBLEM

(a) Samsung made the following statement about what was included on its consolidated financial statement:

The consolidated financial statements include the accounts of SEC (Samsung Electronics Co., Ltd) and its controlled subsidiaries (collectively referred to as "the Company"). Controlled subsidiaries generally include those companies over which the company exercises control. Control over an entity is presumed to exist when the Company owns, directly or indirectly through subsidiaries, over 50% of the voting rights of the entity, the Company has the power to govern the operating and financial policies of the entity through agreement or the Company has the power to appoint or remove the majority of the members of the board of the entity.

(b) Samsung's Consolidated Statement of Cash Flows shows that ₩21,619,244 million was spent for the purchase of property and equipment during the year.

 

## BYP 12-2 COMPARATIVE ANALYSIS PROBLEM

(a)

| | Zetar | Nestlé |
|---|---|---|
| 1. Cash provided (used) for investing activities | £4,092 thousand | CHF14,549 million |
| 2. Cash used for capital expenditures (spending) | 3,789 | 4,576 |

(b) In Note 1 to the consolidated financial statements, Nestlé states that the consolidated financial statements comprise those of Nestlé S.A., and of its affiliated companies, including joint ventures and associates (the Group).

The Group's referable operating segments are;

- Zone Europe
- Zone Americas
- Zone Asia, Oceania and Africa
- Nestlé Waters
- Nestlé Nutrition
- Other

  

## BYP 12-3 REAL-WORLD FOCUS

**Answers will vary depending on company chosen. The following sample solution is provided for Medtronic, Inc.**

**(a) 30 analysts rated this company.**
**(b) 5/30 or 16 2/3% of the analysts rated it a strong buy.**
**(c) Average rating 2.5 on a scale of 1.0 (strong buy) to 5.0 (strong sell).**
**(d) Average rating: No change.**

## BYP 12-4 DECISION-MAKING ACROSS THE ORGANIZATION

**The dollar amount received upon the sale of the UMW Company shares was $1,468,000. Since Kemper Corporation has a 30% interest in UMW, the equity method should be used to report dividends and net income. A reconstruction of the correct entries can be prepared for the acquisition, the equity method treatment of dividends and revenue, and the sale. A plug figure for cash will balance the entry for the sale. These entries are provided below.**

**Both the shareholder and the president are correct. Since the equity method adjusts the investment account for the earnings of the associate, the "very profitable" UMW investment balance has increased during the period the shares were held. The shares were sold at less than their current investment balance and thus a loss was recognized. Shareholder Kerwin is correct in labeling this a very profitable company and in noting that a loss was recognized on the sale.**

**President Chavez is correct in that the investment was sold at a higher figure than the $1,300,000 purchase price. The key to the dilemma is to note that the selling price was less than the carrying amount of the investment. The carrying amount has increased due to the recognition of UMW income during the time the shares were held.**

**Entries for the investment in UMW Company:**

| | | |
|---|---|---|
| **Acquisition** | | |
| Share Investments | 1,300,000 | |
| Cash | | 1,300,000 |
| | | |
| **Previous Years—Equity Method** | | |
| Share Investments | 372,000 | |
| Revenue from Share Investments ($1,240,000 X 30%) | | 372,000 |
| | | |
| Cash | 132,000 | |
| Share Investments ($440,000 X 30%) | | 132,000 |

  

**BYP 12-4 (Continued)**

**This Year—Equity Method**

| | | |
|---|---|---|
| Share Investments | 156,000 | |
| Revenue from Share Investments ($520,000 X 30%) | | 156,000 |
| | | |
| Cash | 48,000 | |
| Share Investments ($160,000 X 30%) | | 48,000 |

**Sale of the UMW Company Shares**

| | | |
|---|---|---|
| Cash (Cash is a plug.) | 1,468,000 | |
| Loss on Sale of Investments | 180,000 | |
| Share Investments | | 1,648,000* |

*$1,300,000 + ($372,000 + $156,000) – ($132,000 + $48,000)

 

## BYP 12-5 COMMUNICATION ACTIVITY

**Dear Mr. Scholes:**

**I am writing this memo to make suggestions regarding the appropriate treatment for the two securities you are holding in your portfolio. Assuming that your investment in Longley Corporation does not represent a significant interest in that firm, it should be accounted for as a non-trading security because it is a share investment that you do not intend on selling in the near future. You will not report any gains or losses on this investment in your income statement until you sell it. On the other hand, your debt investment should be accounted for as a trading security since you purchased it with the intent to generate a short-term profit. Unrealized gains and losses at your statement of financial position date should be reported in other income and expense on the income statement.**

  

## BYP 12-6 ETHICS CASE

(a) Classifying the securities as they propose will indeed have the effect on net income that they say it will. Classifying all the gains as trading securities will cause all the gains to flow through the income statement this year and classifying the losses as non-trading securities will defer the losses from this year's income statement. Classifying the gains and losses just the opposite will have the opposite effect.

(b) What each proposes is unethical since it is knowingly not in accordance with IFRS. The financial statements are fraudulently, not fairly, stated. The affected stakeholders are other members of the company's officers and directors, the independent auditors (who may detect these misstatements), the shareholders, and prospective investors.

(c) The act of selling certain securities (those with gains or those with losses) is management's choice and is not per se unethical. Accounting standards allow the sale of selected securities so long as the method of assigning cost adopted by the company is consistently applied. If the officers act in the best interest of the company and its stakeholders, and in accordance with IFRS, and not in their self-interest, their behavior is probably ethical. Knowingly engaging in unsound and poor business and accounting practices that waste assets or that misstate financial statements is unethical behavior.

 

## GAAP FINANCIAL REPORTING PROBLEM

### GAAP 12-1

(a) Tootsie Roll purchased $2,902 thousand of trading securities in 2010. In addition, they purchased $9,301 of available for sale securities in 2010.

(b) If the decline is judged to be other than temporary, a company writes down the cost basis of the security to fair value. The company accounts for the write-down as a realized loss. Therefore, it includes the amount in net income.

(c) Per Note 1, the company's 50% interest in two foreign companies is accounted for using the equity method. The company records an increase in its investment to the extent of its share of earnings, and reduces its investment to the extent of losses and dividends received. No dividends were paid in 2010, 2009 and 2008.

  