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. Describe 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

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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

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 Q12-4	BE12-1 E12-2 DI12-1 E12-3	P12-1A P12-1B P12-2A P12-2B		
3. Explain the accounting for share investments.	Q12-7	Q12-5 Q12-8 Q12-9 Q12-10	Q12-6 E12-5 BE12-2 E12-6 BE12-3 E12-7 DI12-2 E12-8 E12-4	P12-2A P12-2B P12-3A P12-3B P12-4A P12-4B 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 Q12-17	Q12-13	Q12-14 Q12-16 BE12-4 BE12-7 BE12-8 E12-8 P12-6A P12-6B	Q12-15 P12-2A BE12-5 P12-3A BE12-6 P12-5A DI12-3 P12-1B E12-10 P12-2B E12-11 P12-3B E12-12 P12-5B P12-1A		
6. Distinguish between short-term and long-term investments.		Q12-18 Q12-19 DI12-4	BE12-7 BE12-8 P12-6A P12-6B	BE12-5 P12-3A E12-10 P12-5A E12-11 P12-1B E12-12 P12-2B P12-1A P12-3B P12-2A P12-5B		
*7. Describe the form and content of consolidated financial statements as well as how to prepare them.		Q12-20 Q12-21	BE12-9 P12-7A BE12-10 P12-7B E12-13 E12-14			
Broadening Your Perspective		Financial Reporting Real-World Focus Decision-Making Across the Organization 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 Ltd. 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 SA 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.

Share investments can also be equity method investments if ownership is between 20% and 50%, or consolidated investments if ownership is 50% or more.

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:
Accumulated other comprehensive loss .... € 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 closed out to the account Accumulated Other Comprehensive Income. This account is report as an addition to (or in the case of on accumulated loss, 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 by closing it out to Accumulated Other Comprehensive Income 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 Ltd. 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	50,000	
	Cash		50,000
July 1	Cash	1,600	
	Interest Revenue		1,600

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 €190,000)	47,500	
	Revenue from Share Investments		47,500
31	Cash (25% X €40,000)	10,000	
	Share Investments		10,000

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	R$66,000
Equity	
Accumulated other comprehensive loss	R$ 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—Ord.		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—Ord.		120,000	120,000		0
Retained Earnings		70,000	70,000		0

SOLUTIONS FOR DO IT! REVIEW EXERCISES

DO IT! 12-1

	2017				
(a)	Jan. 1	Debt Investments	50,000	
		Cash		50,000
	Dec. 31	Interest Receivable (£50,000 × 8%)	4,000	
		Interest Revenue		4,000
	2018			
	Jan. 1	Cash	4,000	
		Interest Receivable		4,000
		Cash	28,700	
		Loss on Sale of Debt Investments	1,300	
		Debt Investments (£50,000 × 30/50)		30,000
(b)	Dec. 31	Interest Receivable	1,600	
		Interest Revenue (£20,000 × 8%)		1,600

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..	13,300*	
Fair Value Adjustment—Trading		13,300

***¥11,100 + ¥2,200**

Non-trading securities:

Fair Value Adjustment—Non-Trading	11,850**	
Unrealized Gain or Loss—Equity		11,850

****¥7,750 + ¥4,100**

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)

2017				
Jan.	1	Debt Investments......................................	50,000	
		Cash...		50,000
Dec.	31	Interest Receivable (£50,000 × 8%)..........	4,000	
		Interest Revenue		4,000

EXERCISE 12-2 (Continued)

2018				
Jan.	1	Cash	4,000	
		Interest Receivable		4,000
	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
(b)	Dec. 31	Interest Receivable	800	
		Interest Revenue (£20,000 X 8% X 1/2)		800

EXERCISE 12-3

January 1, 2017		
Debt Investments	70,000	
Cash		70,000
December 31, 2017		
Interest Receivable (€70,000 X 9%)	6,300	
Interest Revenue		6,300
January 1, 2018		
Cash	6,300	
Interest Receivable		6,300
January 1, 2018		
Cash	40,300	
Debt Investments (40/70 X €70,000)		40,000
Gain on Sale of Debt Investments		300

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 €2.80)..	7,000	
	Dividend Revenue		7,000
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 €2.90)..	5,800	
	Dividend Revenue		5,800

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 (£36,000 X 25%)	9,000	
		Share Investments		9,000
	31	Share Investments	40,000	
		Revenue from Share Investments (£160,000 X 25%)		40,000

(b)	Investment in Morelli, January 1	£180,000
	Less: Dividend received	9,000
	Plus: Share of reported income	40,000
	Investment in Morelli, December 31	£211,000

EXERCISE 12-8

1.	2017			
	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 Limited, 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

Accumulated other comprehensive loss	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 (€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	
Accumulated other comprehensive loss	€ 6,000

Income Statement

Other income and expense	
Unrealized gain on trading securities	€ 4,000

*EXERCISE 12-13

LENNON ENTERPRISES AND SUBSIDIARY
Worksheet—Consolidated Statement of Financial Position
January 1, 2017

Assets	Lennon Enterprises	Ono Ltd.	Eliminations Dr.	Eliminations Cr.	Consolidated Data
Plant and equipment (net)	300,000	220,000			520,000
Investment in Ono Ltd. 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 Ent.	230,000				230,000
Share capital—Ono Ltd.		80,000	80,000		0
Retained earnings—Lennon Ent.	170,000				170,000
Retained earnings—Ono Ltd.		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 ENTERPRISES AND SUBSIDIARY
Worksheet—Consolidated Statement of Financial Position
January 1, 2017

Assets	Lennon Enterprises	Ono Ltd.	Eliminations Dr.	Eliminations Cr.	Consolidated Data
Plant and equipment (net)	300,000	220,000			520,000
Investment in Ono Ltd. 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 Ent.	230,000				230,000
Share capital—Ono Ltd.		80,000	80,000		0
Retained earnings—Lennon Ent.	170,000				170,000
Retained earnings—Ono Ltd.		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

.

PROBLEM 12-1A

(a)

2017				
Jan.	1	Debt Investments	2,000,000	
		Cash		2,000,000
Dec.	31	Interest Receivable		
		(HK$2,000,000 X .07)	140,000	
		Interest Revenue		140,000
2020				
Jan.	1	Cash	140,000	
		Interest Receivable		140,000
	1	Cash (HK$1,000,000 X 1.05)	1,050,000	
		Debt Investments		1,000,000
		Gain on Sale of Debt		
		Investments		50,000
Dec.	31	Interest Receivable		
		(HK$1,000,000 X .07)	70,000	
		Interest Revenue		70,000

(b)

Statement of Financial Position

Current assets		
Interest receivable	HK$	140,000
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) **2017**

Aug. 1	**Cash (2,000 X £0.70)**	**1,400**	
	Dividend Revenue		**1,400**
Sept. 1	**Cash (2,000 X £8)**	**16,000**	
	Loss on Sale of Share Investments (£18,000 – £16,000)	**2,000**	
	Share Investments (2,000 X £9)		**18,000**
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 £0.70)**	**840**	
	Dividend Revenue		**840**
31	**Cash (3,000 X £1)**	**3,000**	
	Dividend Revenue		**3,000**

Share Investments

2017			**2017**	
Jan. 1	**Balance**	**135,000**	**Sept. 1**	**18,000**
			Oct. 1	**24,000**
2017				
Dec. 31	**Balance**	**93,000**		

PROBLEM 12-3A (Continued)

(b) Dec. 31

Dec. 31	Unrealized Gain or Loss—Equity (£93,000 – £89,400)	3,600	
	Fair Value Adjustment—Non-Trading		3,600

Security	Cost	Fair Value	
Carlene Co. common	£36,000	£38,400	(1,200 × £32)
Riverdale Co. common	27,000	24,000	(3,000 × £ 8)
Raczynski Co. common	30,000	27,000	(1,500 × £18)
	£93,000	£89,400	

(c) Investments

Investments in shares of less than 20% owned companies, at fair value	£ 89,400

Equity

Share capital—ordinary	£1,500,000
Retained earnings	1,000,000
Accumulated other comprehensive loss	3,600
Total equity	£2,496,400

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		54,800	
	Share Investments			52,000
	Gain on Sale of Share Investments			2,800
28	Share Investments		31,680	
	Cash (400 X R$79.20)			31,680
30	Cash		1,470	
	Dividend Revenue (R$1.05 X 1,400)			1,470
Feb. 8	Cash		480	
	Dividend Revenue (R$0.40 X 1,200)			480
18	Cash (R$26.30 X 1,200)		31,560	
	Loss on Sale of Share Investments		2,040	
	Share Investments			33,600
July 30	Cash		1,400	
	Dividend Revenue (R$1.00 X 1,400)			1,400
Sept. 6	Share Investments		49,200	
	Cash (R$82 X 600)			49,200
Dec. 1	Cash		1,350	
	Dividend Revenue (R$1.35 X 1,000)			1,350

(b)

Share Investments

1/1 Bal.	169,600	1/20	52,000
1/28	31,680	2/18	33,600
9/6	49,200		
12/31 Bal.	164,880		

PROBLEM 12-5A (Continued)

(c)	Dec. 31	Unrealized Gain or Loss—Equity	3,280	
		Fair Value Adjustment—Non-Trading (R$164,880 – R$161,600)..................		3,280
		Accumulated Other Comprehensive Income	3,280	
		Unrealized Gain or Loss—Equity.........		3,280

Security	Cost	Fair Value	
Elderberry Corporation ordinary	R$ 84,000	R$ 89,600	(1,400 X R$64)
Hachito Corporation ordinary	80,880	72,000	(1,000 X R$72)
	R$164,880	R$161,600	

(d) Investments

Investments in shares of less than 20% owned companies, at fair value..	R$161,600

Equity

Total share capital and retained earnings..................	xxxxx
Accumulated other comprehensive loss....................	3,280
Total equity	R$ xxxxx

PROBLEM 12-6A

RADAR INDUSTRIES LTD.
Statement of Financial Position
December 31, 2017

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 INDUSTRIES LTD.
Statement of Financial Position (Continued)
December 31, 2017

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	
Accumulated other comprehensive income		8,000	€1,741,000
Non-current liabilities			
Bonds payable, 10%, due 2023			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)

2017			
Dec. 31	Share Investments	1,218,000	
	Current Assets		1,218,000

(b)

LIU LIMITED AND SUBSIDIARY
Worksheet—Consolidated Statement of Financial Position
December 31, 2017

Assets	Liu Limited	Yang Plastics	Eliminations Dr.	Eliminations Cr.	Consolidated Data
Plant and equipment (net)	2,100,000	676,000	84,000		2,860,000
Investment in Yang Plastics ordinary shares	1,218,000			1,218,000	0
Current assets	262,000	435,500			697,500
Excess of cost over book value of subsidiary			115,000		115,000
Totals	3,580,000	1,111,500			3,672,500
Equity and liabilities					
Share capital—Liu Limited	1,950,000				1,950,000
Share capital—Yang Plastics		525,000	525,000		0
Retained earnings—Liu Limited	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	1,218,000	1,218,000	3,672,500

*PROBLEM 12-7A (Continued)

(c)

LIU LIMITED AND SUBSIDIARY
Consolidated Statement of Financial Position
December 31, 2017

Assets		
Goodwill (¥199,000 − ¥84,000)		¥ 115,000
Plant and equipment, net (¥2,776,000 + ¥84,000)		2,860,000
Current assets		697,500
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)

2017				
Jan.	1	Debt Investments	400,000	
		Cash		400,000
Dec.	31	Interest Receivable (£400,000 X .06)	24,000	
		Interest Revenue		24,000
2020				
Jan.	1	Cash	24,000	
		Interest Receivable		24,000
	1	Cash (£240,000 X 1.12)	268,800	
		Debt Investments		240,000
		Gain on Sale of Debt Investments		28,800
Dec.	31	Interest Receivable (£160,000 X .06)	9,600	
		Interest Revenue		9,600

(b)

Statement of Financial Position

Current assets

Interest receivable	£ 24,000

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)

	2017		
Aug. 1	Cash (4,000 X €0.50)	2,000	
	Dividend Revenue		2,000
Sept. 1	Cash (1,500 X €8.50)	12,750	
	Share Investments (1,500 X €6)		9,000
	Gain on Sale of Share Investments		3,750
Oct. 1	Cash (600 X €30)	18,000	
	Share Investments (600 X €24)		14,400
	Gain on Sale of Share Investments (€18,000 – €14,400)		3,600
Nov. 1	Cash (3,000 X €1)	3,000	
	Dividend Revenue		3,000
Dec. 15	Cash (3,400 X €0.60)	2,040	
	Dividend Revenue		2,040
31	Cash (3,500 X €1)	3,500	
	Dividend Revenue		3,500

Share Investments

2017			2017	
Jan. 1	Balance	186,000	Sept. 1	9,000
			Oct. 1	14,400
2017				
Dec. 31	Balance	162,600		

PROBLEM 12-3B (Continued)

(b)	**Dec. 31**	**Unrealized Gain or Loss—Equity (€162,600 – €159,700)**	**2,900**	
		Fair Value Adjustment—Non-Trading		**2,900**

Security	Cost	Fair Value	
Trowbridge Co. ordinary	€ 81,600	€ 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)
	€162,600	€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
Accumulated other comprehensive loss	2,900
Total equity	€3,197,100

PROBLEM 12-4B

(a)

2017				
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)

2017				
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

PROBLEM 12-4B (Continued)

(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

			Debit	Credit
(a)	Jan. 7	Cash (700 X €56)	39,200	
		Share Investments		35,000
		Gain on Sale of Share Investments		4,200
	10	Share Investments	23,550	
		Cash (300 X €78.50)		23,550
	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	945	
		Dividend Revenue (€1.05 X 900)		945
	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	23,550	2/10	22,400
9/1	60,000		
12/31 Bal.	125,550		

PROBLEM 12-5B (Continued)

(c)	**Dec. 31**	**Unrealized Gain or Loss—Equity ....**	**3,150**	
		Fair Value Adjustment—Non-Trading (€125,550 – €122,400)..........................		**3,150**
		Accumulated Other Comprehensive Income	**3,150**	
		Unrealized Gain or Loss—Equity...........		**3,150**

Security	**Cost**	**Fair Value**	
Ukraine OAO Ordinary Shares	**€ 42,000**	**€ 43,200**	**(900 X €48)**
Vanucci SpA Ordinary Shares	**83,550**	**79,200**	**(1,100 X €72)**
	€125,550	**€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**
Accumulated other comprehensive loss.....................	**3,150**
Total equity	**€ xxxxx**

PROBLEM 12-6B

REDLANDS ENTERPRISES AG
Statement of Financial Position
December 31, 2017

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 ENTERPRISES AG
Statement of Financial Position (Continued)
December 31, 2017

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 2027		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..	700,000	
	Current Assets..		700,000

(b)

PATEL COMPANY LTD. AND SUBSIDIARY
Worksheet—Consolidated Statement of Financial Position
December 31, 2017

Assets	Patel Company	Singh Company	Eliminations Dr.	Eliminations Cr.	Consolidated Data
Plant and equipment (net)	1,882,000	351,000	25,000		2,258,000
Investment in Singh Company ordinary shares	700,000			700,000	0
Current assets	778,000	379,000			1,157,000
Excess of cost over book value of subsidiary			35,000		35,000
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	700,000	700,000	3,450,000

*PROBLEM 12-7B (Continued)

(c)

PATEL COMPANY LTD. AND SUBSIDIARY
Consolidated Statement of Financial Position
December 31, 2017

Assets		
Goodwill (€60,000 − €25,000)		€ 35,000
Plant and equipment, net		
(€2,233,000 + €25,000)		2,258,000
Current assets		1,157,000
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: 5/26/2016

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.

COMPREHENSIVE PROBLEM (Continued)

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.	6/12/16	Cash	100,000	
			Buildings	200,000	
			Share Capital—Ordinary		120,000
			Share Premium—Ordinary		180,000

7/21/16	**Cash..**	**900,000**	
	Share Capital—Ordinary.......		**180,000**
	Share Premium—Ordinary ...		**720,000**
7/27/17	**Share Dividends**		
	(150,000 X .10 X €3)..................	**45,000**	
	Ordinary Share Dividends		
	Distributable		**30,000**
	Share Premium—Ordinary ...		**15,000**
7/31/17	**No entry**		
8/15/17	**Ordinary Share Dividends**		
	Distributable............................	**30,000**	
	Share Capital—Ordinary.......		**30,000**
12/4/17	**Cash Dividends**		
	(165,000 X €0.05)	**8,250**	
	Dividends Payable		**8,250**
12/14/17	**No entry**		
12/24/17	**Dividends Payable ....**	**8,250**	
	Cash		**8,250**

2. Shares Issued and Outstanding

Date	**Event**	**Number of Shares Issued**	**Total Shares Issued and Outstanding**
6/12/16	**Issuance to Incorporators**	**60,000**	**60,000**
7/21/16	**Issuance to Marino**	**90,000**	**150,000**
8/15/17	**Share dividend issuance**	**15,000**	**165,000**

Part IV

(d) 1.	**1/1/18**	**Cash...**	**548,000**	
		Bonds Payable		**548,000**

2.	12/31/18	Interest Expense	41,200	
		Bonds Payable (€52,000 ÷ 10)		5,200
		Interest Payable (€600,000 X .06)		36,000
3.	1/1/19	Interest Payable	36,000	
		Cash		36,000
4.	12/31/19	Interest Expense	41,200	
		Bonds Payable (€52,000 ÷ 10)..............................		5,200
		Interest Payable (€600,000 X .06)		36,000

Part V

(e)	(1)	2016	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
		2017	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)

2018	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	

MC12 MATCHA CREATIONS

(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.

MC12 (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 Matcha & 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**

MC12 (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 Matcha & 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) TSMC made the following statement about what was included on its consolidated financial statement:

Basis of Consolidation

The consolidated financial statements incorporate the financial statements of TSMC and entities controlled by TSMC (its subsidiaries). Control is achieved when the Company:

- **has power over the investee;**
- **is exposed, or has rights. to variable returns from its involvement with the investee; and**
- **has the ability to use its power to affect its returns.**

The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Company has less than a majority of the voting rights of an investee, it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally.

Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statement of profit or loss and other comprehensive income from the date the Company obtains control unit the date when the Company ceases to control the subsidiary.

(b) TSMC's Consolidated Statement of Cash Flows shows that NT$31,582.4 (31,525.9 + 56.5) million was spent for the purchase of financial assets and NT$246,137.4 million for property and equipment during the year.

BYP 12-2 COMPARATIVE ANALYSIS PROBLEM

(a)

		Petra Foods	Nestlé
1.	Cash provided (used) for investing activities	US$610,025 thousand	(CHF1,606) million
2.	Cash used for capital expenditures (spending)	35,371	4,928

(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) 29 analysts rated this company.
(b) 7/29 or 24% of the analysts rated it a strong buy.
(c) Average rating 2.2 on a scale of 1.0 (strong buy) to 5.0 (strong sell).
(d) Average rating: No change.
(e) Earnings surprise: 1.39%

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 Ltd. 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 Industries 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) Percentage increase from 2012 to 2013:

(1) Short-term marketable securities: ($26,287 – $18,383) ÷ $18,383 = 43.0%

(2) Long-term marketable securities: ($106,215 – $92,122) ÷ $92,122 = 15.3%

(b)

(1) Purchases of marketable securities during the year: $148,489 million.

(2) Payments for business acquisitions, net of cash acquired: $496 million.