Practice Set BONDS PAYABLE

I. ISSUING BONDS AT PAR

Business continued good, but cash was short, and paying off the $50,000 note to Bank B was proving difficult. The shortage was solved by issuing at Par on Dec. 31, 2002, bonds valued at $80,000 with interest at 14% paid semiannually with a maturity of 4 years. Make the first year's entries and the entry to pay off the bonds.

	DR.	CR.

II. ISSUING BONDS AT A DISCOUNT

During 2006, business continued good, but cash was again in short supply, and $80,000 in bonds were soon to be paid. It was decided to raise $100,000 in cash with a 3-year bond issue. Market conditions and the financial strength of the company indicated 10% interest paid semiannually would sell the entire issue. Unfortunately, market conditions worsened, business slowed, and the bonds sold on Dec. 31 to yield 12% semiannually. The amount received was the present value of 6 interest payments of $5,000 ($100,000)(.05) plus the present value of the $100,000 to be paid in 3 years. Interest was the market rate of 12% compounded and paid semiannually. Make the Journal Entry to record the sale of the bonds and the first interest payment using a Straight Line amortization and an Effective Interest amortization.

Value of Interest	**Value of Bond**

Amount Received = $24,585 + $70,490 = $95,075.

Dec. 31	DR.	CR.

AMORTIZING BOND DISCOUNTS AND PAYING INTEREST

STRAIGHT LINE METHOD = $820.83

June 30	DR.	CR.

EFFECTIVE INTEREST METHOD (Round)

Period	(a) Carrying Amount BOP	(b) Interest Expense Recorded (.06)(a)	(c) Interest Paid	(d) Discount Amortized (b-c)	(e) Unamortized Discount (e-d)	Carrying Amount EOP (a+d)
0						
1	$95,075					
2	95,780					
3	96,527					
4	97,319					
5	98,158				953	
6	99,047	5,953	5,000	953	0	100,000

June 30	DR.	CR.

Note: Period 5's Unamortized Discount balance determines final adjustment period 6.

III. ISSUING BONDS AT A PREMIUM

Had The Computer Warehouse been more fortunate, interest rates would have fallen, and the bonds would have sold at a premium to yield 8% semiannually. Make the Journal Entry to record the sale of Bonds sold to yield 8% and the first interest payment using both a Straight Line amortization and an Effective Interest amortization.

Value of Interest	Value of Principal

Amount received equals $26,210 + $79,030 = $105,240.

	DR.	CR.
Dec. 31		

AMORTIZING BOND PREMIUMS AND PAYING INTEREST

STRAIGHT LINE METHOD

= $873.33

	DR.	CR.
June 30		

EFFECTIVE INTEREST METHOD (Round)

Period	(a) Carrying Amount BOP	(b) Interest Expense Recorded (.04)(a)	(c) Interest Paid	(d) Premium Amortized (c-b)	(e) Unamortized Premium (e-d)	Carrying Amount EOP (a-d)
0						
1	$105,240					
2	104,450					
3	103,628					
4	102,773					
5	101,884				959	
6	100,959	4,041	5,000	959	0	100,000

	DR.	CR.
June 30		

Note: Period 5's Unamortized Premium balance determines final adjustment period 6.

IV. BOND SINKING FUND

On Dec. 31, 2006, it was decided to start a sinking fund to pay off the discounted bonds issued that day. The first of 6 semiannual payments into the fund, which was expected to earn 12% semiannually, was made in 6 months. Calculate the equal payments. Make the entry to start the fund, the entry to record 6 month's interest, and the entry to pay the bondholders $100,000 three years hence.

	DR.	CR.

Hint: Six months interest equaled $860.22.