ACCT 101 – Chapter 10

I. Financing Corporations

When a corporation needs money, it can get from 2 primary sources.

A. Debt Financing – borrow the money –

1. Note Payable

2. Mortgage Payable

3. Bonds Payable

B. Equity Financing – selling additional shares of stock

1. Preferred Stock
2. Common Stock

Bonds are long-term debt where the interest is paid in intervals over the life of the bond and the principal is paid in one lump sum at the end of the bond's life. Unlike a loan or note payable which you will owe only one lender, bonds are usually owed to many lenders.

II. Characteristics of a Bond

A. Bond Indenture – contract or terms of the bond

B. Principal – amount borrowed, the face amount of the bond

C. Interest Rate – always stated in annual terms. Interest will be paid in intervals, either annually, semi-annually or quarterly. (Usually semi-annually)

D. Term Bonds – all of the bonds mature on the same date

E. Callable Bonds – issue reserves the right to redeem the bonds before their maturity date

F. Information Needed:
1. Principal
2. Term
3. Interest rate
4. Frequency of interest payments

III. Accounting for Bonds Payable

A. Bonds Issued at Face Value

Dan Druff Inc. issued $100,000, 12% 3-year bonds on January 1, 2022. Interest is paid annually on December 31.

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2022						1
2	Jan	1					2
3							3
4							4
5	Dec	31					5
6							6
7	2023						7
8	Dec	31					8
9							9
10	2024						10
11	Dec	31					11
12							12
13							13
14	Dec	31					14
15							15
16							16

Use the same information as above, but the interest is paid semi-annually on June 30 and Dec 31.

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2022						1
2	Jan	1					2
3							3
4							4
5	Jun	30					5
6							6
7							7
8	Dec	31					8
9							9
10	2023						10
11	Jun	30					11
12							12
13							13
14	Dec	31					14
15							15
16	2024						16
17	Jun	30					17
18							18
19							19
20	Dec	31					20
21							21
22							22
23	Dec	31					23
24							24
25							25
26							26

B. Bonds Issued at a Discount

Dan Druff Inc. issued $100,000, 12% 3-year bonds on January 1, 2022, for $96,406. The market rate of interest is 13%. Interest is paid annually. *Interest will always be paid on the face amount of the bonds and the Discount on Bonds Payable account must be $0 by the maturity date.*

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2022						1
2	Jan	1					2
3							3
4							4
5							5
6	Dec	31					6
7							7
8							8
9	Dec	31					9
10							10
11	2023						11
12	Dec	31					12
13							13
14							14
15	Dec	31					15
16							16
17	2024						17
18	Dec	31					18
19							19
20	Dec	31					20
21							21
22	Dec	31					22
23							23
24							24

Carrying Value of Bonds Payable –
On 12/31/22 above

C. Bonds Issued at a Premium

Dan Druff Inc. issued $100,000, 12% 3-year bonds on January 1, 2022, for $103,768. The market rate of interest is 11%. Interest paid annually. *The interest will always be paid on the face amount of the bonds and the Premium on Bonds Payable must be $0 by the maturity date.*

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2022						1
2	Jan	1					2
3							3
4							4
5							5
6	Dec	31					6
7							7
8							8
9	Dec	31					9
10							10
11	2023						11
12	Dec	31					12
13							13
14							14
15	Dec	31					15
16							16
17	2024						17
18	Dec	31					18
19							19
20	Dec	31					20
21							21
22	Dec	31					22
23							23
24							24

Carrying Value of Bonds Payable

On 12/31/22 above

IV. Bond Redemption

A. Gain on Redemption of Bonds

On December 31, 2023, Dan Druff Inc. called the bonds issued at a premium. The bonds were called at 98.

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2023						1
2	Dec	31					2
3							3
4							4

B. Loss on Redemption of Bonds

On December 31, 2023, Dan Druff Inc. calls the bonds issued at a premium. The bonds are called at 104.

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2023						1
2	Dec	31					2
3							3
4							4

V. Long-Term Loan Payable/Mortgage Payable

Long-Term loans and mortgages are repaid in periodic installments and each payment is applied part to interest expense and part toward the principal balance. The periodic payment is fixed, however, the amount of each payment that is applied to interest and principal changes with each payment. The amount of interest expense for each payment is calculated from the outstanding loan balance at the time the payment is made.

On January 1, 2020, Skip Stone issued a $250,000, 8%, 10-year loan to buy new equipment. The note is to be repaid in annual installments of $37,257.

Date	Payment	Interest Expense	Principal	Balance
01/01/20				$ 250,000
12/31/20	37,257			
12/31/21	37,257			
12/31/22	37,257			
12/31/23	37,257			
12/31/24	37,257			
12/31/25	37,257			
12/31/26	37,257			
12/31/27	37,257			
12/31/28	37,257			
12/31/29	37,257			

Record the entries for the first annual payment on December 31, 2020, and the second annual payment on December 31, 2021.

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2020						1
2	Dec	31					2
3							3
4							4
5	2021						5
6	Dec	31					6
7							7
8							8
9							9
10							10

Bond Practice Exercise

2022

Jan. 1 Issued $1,000,000 of 12-year, 8%, callable bonds for $1,034,560, with interest payable semiannually on June 30 and December 31 of each year.

Jun 30 Record the first semiannual interest payment and amortization

Dec. 31 Record the second semiannual interest payment and amortization.

2026

Apr 1 The company called the bonds at 99.
(Record the redemption of the bonds only).

	DATE		DESCRIPTION	P/R	DEBIT	CREDIT	
1	2022						1
2	Jan	1					2
3							3
4							4
5							5
6	Jun	30					6
7							7
8							8
9		30					9
10							10
11							11
12	Dec	31					12
13							13
14							14
15		31					15
16							16
17							17
18							18
19	2026						19
20	Apr	1					20
21							21
22							22
23							23
24							24
25							25

ACCT 101 - Chapter 10 Classwork

Use the data from the textbook to complete the problems.

Romero Company issues $3,400,000 of 8%, 10-year bonds dated January 1, 2021, that pay interest semiannually on June 30 and December 31. The bonds are issued at a price of $3,010,000

1. Record the journal entry to issue the bonds on January 1, 2021.
2. a. Record the journal entry to pay the semi-annual interest payment and amortize the discount on June 30, 2021.
   b. Record the journal entry to pay the semi-annual interest payment and amortize the discount on Dec. 31, 2021.
4. On September 1, 2025, Romero calls the bonds at 99. Record the journal entry to call the bonds.
5. What is the total interest expense for the bonds for:
   a. One full year?
   b. The entire 10-year life of the bond? (if the bond had been held until maturity)
6. What is the carrying value of the bonds on:
   a. December 31, 2021?
   b. December 31, 2022?

Ripken Company issues 9%, 5-year bonds dated January 1, 2021, with a $320,000 par value. The bonds pay interest on June 30 and December 31 and were issued at a price of $332,988.

1. Record the journal entry to issue the bonds on January 1, 2021.
2. a. Record the journal entry to pay the semi-annual interest payment and amortize the premium on June 30, 2021.
   b. Record the journal entry to pay the semi-annual interest payment and amortize the premium on Dec. 31, 2021.
3. On April 30, 2023, Ripkin calls the bonds at 102. Record the journal entry to call the bonds.
4. What is the total interest expense for the bonds for:
   a. One full year?
   b. The entire 5-year life of the bond? (if the bond had been held until maturity)
5. What is the carrying value of the bonds on:
   a. December 31, 2021?
   b. December 31, 2022?