

# PRINCIPLES OF FINANCIAL AND MANAGERIAL ACCOUNTING II

## Long-Term Liabilities

### Objectives:

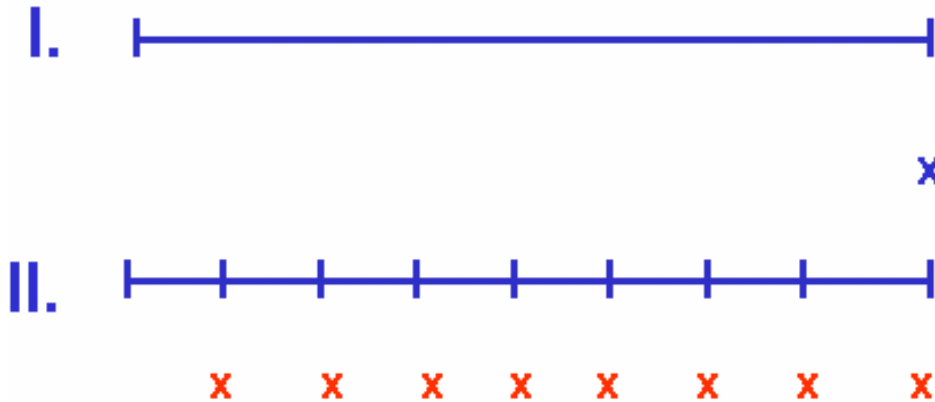
1. Determine and record the selling price of bonds payable.
2. Determine and record amortization of premium and discount on bonds payable using the straight-line method and the interest method.

## Bonds Payable

### Obligations incurred when issuing bonds:

- I. "I promise I will pay you \_\_\_\_\_ at maturity."
- II. "I promise that, between now and then, I will pay you periodic \_\_\_\_\_ at the \_\_\_\_\_ rate on the \_\_\_\_\_ amount."

These two obligations can be envisioned on "time lines" as follows:



The rate is sometimes called:

\_\_\_\_\_ (specified)

\_\_\_\_\_ (reflected in sales price of the bond)

When \_\_\_\_\_ is GREATER than \_\_\_\_\_, the bonds are *unattractive* and will sell at a \_\_\_\_\_.

When \_\_\_\_\_ is LESS than \_\_\_\_\_, the bonds are *attractive* and will sell at a \_\_\_\_\_.



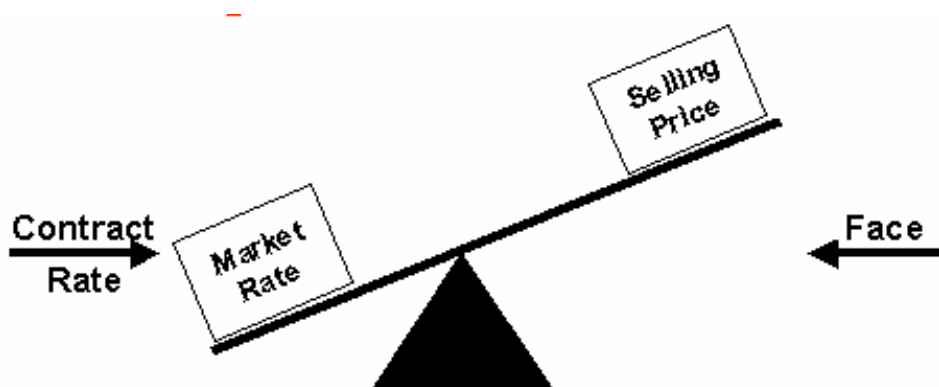
**Issuing Bonds at Face**



The journal entry necessary to record the sale of the bonds at face would be:

	face	
		face

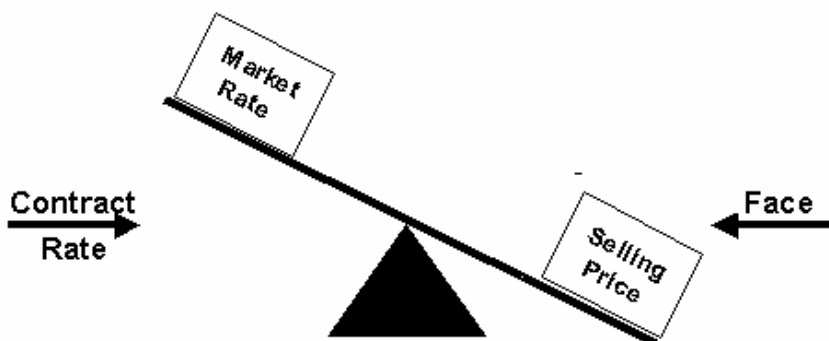
**Issuing Bonds at More Than Face**



The journal entry necessary to record the sale of the bonds for more than face would be:

Cash	received	
		difference
Bonds Payable		face

### Issuing Bonds at Less Than Face



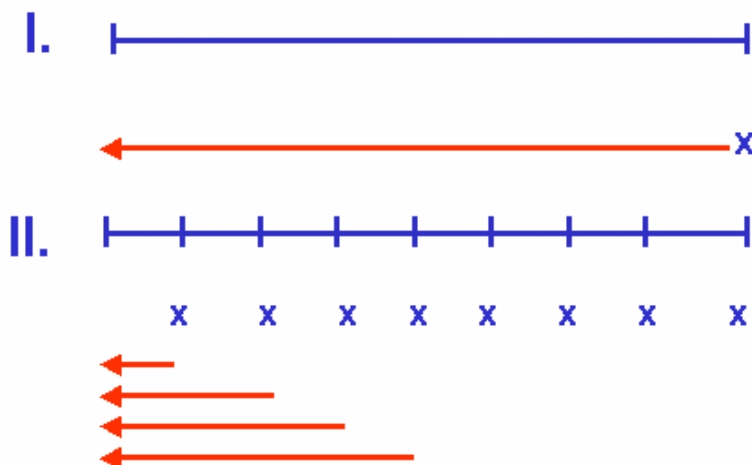
The journal entry necessary to record the sale of the bonds for less than face would be:

Cash	received	
	difference	
Bonds Payable		face

Referring to the advertisement from *The Wall Street Journal*, at 10 3/8% interest, the bonds must have been \_\_\_\_\_ because the 99.82% advertised price meant the bonds were selling at a \_\_\_\_\_. The market rate of interest must have been \_\_\_\_\_ than 10 3/8%.

### Determining the Selling Price of Bonds

The selling price of the bonds is the sum of the “present values” of the two future “promises” made at the time the bonds are sold (refer to page 1):



- I. Present Value of Face (using factor from table)
- II. + Present Value of Interest Payments (using factor from annuity table)
- = Proceeds from Sale of Bonds



Related Definition:

**Review:**

Equipment  
- Accumulated Depreciation  
= Book Value

**New:**

Bonds Payable  
+ (unamortized) Premium  
- (unamortized) Discount  
= Bond Carrying Amount

**Journal Entries to Record Amortization**

Amortization of Premium

	amount	
		amount

Amortization of Discount

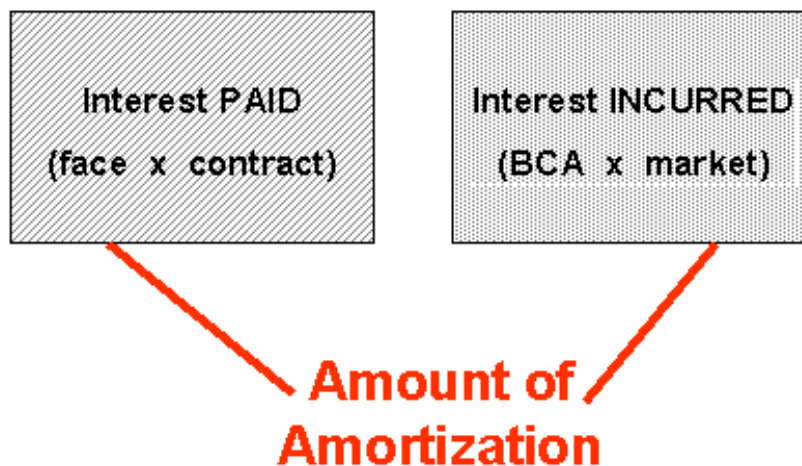
	amount	
		amount

**Determining Amount of Amortization**

Straight-Line Method (presented in chapter)

Premium or Discount = same amount each period  
periods

(Effective) Interest Method (presented in Appendix at end of chapter)



**Exercise**

(continued from page 4)

(b) (1) Record the journal entry for the payment of the first semiannual interest on July 1 (amortization is to be recorded in a separate entry).


(b) (2) Record the journal entry for the amortization of the discount (using the effective interest method) at the time of the first semiannual interest payment on July 1.

	*	
		*

(c) (1) Record the journal entry for the accrual of interest at December 31.


(c) (2) Record the journal entry for the amortization of the discount (using the effective interest method) at the time of the accrual of interest on December 31.

	*	
		*

\* Determine the amount of amortization (effective interest method) following the textbook examples on pages 658 and 659 and the chart below:

	<b><u>A</u></b> <b>Interest Paid</b> <small>(face x contract)</small>	<b><u>B</u></b> <b>Interest Expense</b> <small>(E x mkt)</small>	<b><u>C</u></b> <b>Discount Amort.</b> <small>(B - A)</small>	<b><u>D</u></b> <b>Unamort. Discount</b> <small>(D - C)</small>	<b><u>E</u></b> <b>B.C.A.</b> <small>(face - D) (E + C)</small>
Pmt				16,201	243,799
1			490		
2					
3	11,700	12,240	540	14,657	245,343
4	11,700	12,267	567	14,090	245,910
5	11,700	12,296	596	13,494	246,506