### Accounting for Bonds Payable

On January 1, 2015, Crabb & Co. issued 10-year bonds with a total face value of $500,000. The bond requires annual interest payments on December 31 at a stated rate of 6%. Bonds with similar features are discounted in the market at 8%.

**Were the bonds issued at a discount or a premium?** Discount

**How much cash will Crabb & Co. receive from issuing the bond?** $432,897

*$30,000 = ($500,000 x .06 x 1)…$30,000 x 6.71008 = $201.302...$500,000 x 0.46319 = $231,595…*

*$201.302 + 231,595 = $432,897*

**How does this transaction affect Crabb & Co.’s balance sheet on the date of the issuance?**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Cash |  | Bonds Payable |  | Discount on Bonds Payable |
| **432,897** |  |  |  | **500,000** |  | **67,103** |  |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **DATE** | **ACCOUNT NAME** | **DEBIT** | **CREDIT** | **BALANCE SHEET** | **INCOME STMT** |
| **A** | **=** | **L** | **+** | **E** | **R** |  **-** | **E** |
| **01/01/15** | **Cash** | **432,897** |  |  |  |  |  |  |
|  | **Discount on Bonds Payable** | **67,103** |  |  |  |  |  |  |
|  | **Bonds Payable** |  | **500,000** |  |  |  |  |  |

**What is the amount of cash interest paid by Crabb & Co. in 2015?**  **$30,000**

**What is the amount of interest expense on the income statement in 2015? $34,361.80**

*$432,897 x $.08 = $34,361.80*

**What is the carrying value of the bond on December 31, 2015? $437,529**

**Prepare the entry at 12/31/15 to record interest expense, cash paid, and discount amortization.**

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| **DATE** | **ACCOUNT NAME** | **DEBIT** | **CREDIT** | **BALANCE SHEET** | **INCOME STMT** |
| **A** | **=** | **L** | **+** | **E** | **R** |  **-** | **E** |
| **12/31/15** | **Interest Expense** | **34,631.80** |  |  |  |  |  |  |
|  | **Discount on Bonds Payable** |  | **4,631.80** |  |  |  |  |  |
|  | **Cash** |  | **30,000** |  |  |  |  |  |

*Discount on Bonds Payable….$34,631.80 - $30,000 = $4,631.80*

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| **Statement of Cash Flows** |  |  | **2015** |  | **2016** |
| Issuance of bond (F) |  |  | **437,529** |  | **442,531** |
| Paid interest (O) |  |  | **30,000** |  | **30,000** |

|  |  |  |
| --- | --- | --- |
| **Income Statement** |  |  |
| Interest expense |  |  | **34,631.80** |  | **35,002.30** |

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| **Balance Sheet** |  |  |  |
| Cash |  |  | **407,529** |  | **412,531** |
| **Change in Total Assets** |  |  | **(30,000)** |  | **(30,000)** |
| Bonds payable, net of discount |  |  | **437,529** |  |  **442,531** |
| Retained earnings  |  |  |  **407,529** |  | **412,531** |
| **Change in Total Liabilities & Equity** |  |  | **(30,000)** |  | **(30,000)** |