I. Please answer the following statements as either True or False.

_1. The legal contract between the issuing corporation and the bondholders is called the bond indenture._

_2. Callable bonds reduce the bondholders' risk by requiring the issuer to create a sinking fund of assets set aside at specified amounts and dates to repay the bonds at maturity._

_3. Both interest on bonds and dividends on stock are tax deductible._

_4. Premium on Bonds Payable is an adjunct account._

_5. Equity securities reflect a creditor relationship such as an investment in notes and bonds._

_6. A company holds $40,000 of 7% bonds as a held-to-maturity security. This bondholder's journal entry to record receipt of the semiannual interest payment includes a debit to Cash for $2,800 and a credit to Interest Revenue for $2,800._

_7. When an investor company owns more than 25% of the voting stock of an investee company, it has controlling influence._

_8. Unrealized gains and losses on trading securities are reported as part of net income._

_9. The statement of cash flows explains the difference between the beginning and ending balances of cash and cash equivalents._

_10. Accounting standards require companies to include a statement of cash flows in a complete set of financial statements._

_11. Companies have the option of using either the direct or indirect method to prepare the operating section of the statement of cash flows._

_12. A purchase of land in exchange for a long-term note payable is reported in the investing section of the statement of cash flows._

II. Complete the following statements with the proper word(s).

1. Describe the two payment patterns on an installment note.
2. The ___________________________ method of amortizing a bond discount allocates an equal portion of the total bond interest expense to each interest period.

3. What is an advantage to a corporation who issues bonds to raise capital instead of selling stock? ____________________________________________________________

4. Explain the primary difference between Trading Securities and Available-for-Sale Securities. ____________________________________________________________

5. What are the two major challenges in accounting for international operations? ____________________________________________________________

6. When is the equity method used when accounting for investments in equity securities? ____________________________________________________________

7. ___________________________ activities on the Statement of Cash Flows include the cash effects of transactions and events that determine net income.

8. List two examples of cash outflows under the investing section on a Statement of Cash Flows. ____________________________________________________________

9. Where on the Statement of Cash Flows is the payment of dividends by the corporation shown? ____________________________________________________________

10. Is depreciation a source of cash flow? Explain. ____________________________________________________________
III. Select the best answer to the following statements.

__ 1. A bond traded at 102 ½ means that:
   a. the bond pays 2.5% interest
   b. the bond traded at $1,025 per $1,000 bond
   c. the market rate of interest is 2.5%
   d. the bonds were retired at $1,025 each
   e. the market rate of interest is 2 ½% above the contract rate

__ 2. Secured bonds:
   a. are called debentures
   b. have specific assets of the issuing company pledged as collateral
   c. are backed by the issuer’s bond
   d. are subordinated to those of other unsecured liabilities
   e. are the same as sinking fund bonds

__ 3. A disadvantage of bonds is:
   a. bonds require periodic payments of interest
   b. bonds require payment of principal
   c. bonds can decrease return on equity
   d. bond payments can be burdensome when income and cash flow are low
   e. all of the above

__ 4. A company owns $100,000 of 9% bonds that pay interest on October 1 and April 1. The amount of interest accrued on December 31, the company’s year end, would be:
   a. $750
   b. $1,500
   c. $2,250
   d. $4,500
   e. $9,000

__ 5. Long-term investments can include:
   a. held-to-maturity debt securities
   b. available-for-sale debt securities
   c. available-for-sale equity securities
   d. equity securities giving an investor significant influence over an investee
   e. all of the above

__ 6. Foreign exchange rates fluctuate due to changes in:
   a. political conditions
   b. economic conditions
   c. supply and demand for currencies
   d. expectations of future events
   e. all of the above
7. Murphy Company purchased 2,000 shares of O'Leary Company's common stock for $143,000 as a long-term investment. This investment is considered available-for-sale. The par value of the stock was $1 per share. Murphy paid $375 in commissions on the transaction. The entry to record the transaction would include a:
   a. credit to Common Stock for $2,000
   b. credit to Common Stock for $143,000
   c. credit to Common Stock for $143,375
   d. debit to Long-Term Investments for $143,000
   e. debit to Long-Term Investments for 143,375

8. On July 31, Shamrock Co. purchased 2,000 shares of Irish Tech stock for $16,000. This investment is considered to be an available-for-sale investment. On October 31, which is Shamrock's year-end, the stock had a market value of $20,000. Shamrock should record a:
   a. credit to Unrealized Gain-Equity for $4,000
   b. credit to Market Adjustment – Available-for-Sale for $4,000
   c. credit to Investment Revenue for $4,000
   d. debit to Investment Revenue for $4,000
   e. debit to Unrealized Gain-Equity for $4,000

9. A cash equivalent is an investment that:
   a. is readily convertible to a known amount of cash
   b. is sufficiently close to its maturity date so its market value is unaffected by interest rate changes
   c. generally is within 3 months of its maturity date
   d. is highly liquid
   e. all of the above

10. If a company borrows money from a bank, the interest paid on this loan should be reported on the Statement of Cash Flows as a(n):
    a. operating activity
    b. investing activity
    c. financing activity
    d. noncash investing and financing activity
    e. none of these. This is not reported in the Statement of Cash Flows.

11. The direct method of reporting operating cash flows:
    a. is recommended but not required by the FASB
    b. must be used by all companies
    c. is used by most companies
    d. is considered supplementary disclosure
    e. is not recommended by the FASB, but is commonly used
12. The Statement of Cash Flows helps analysts evaluate the:
   a. source of cash for debt repayment
   b. source of cash for plant expansion
   c. differences between net income and net operating cash flow
   d. means used to finance investing activities
   e. all of the above

IV. Essay
1. Define and explain significant noncash investing and financing activities and the method of reporting them on the statement of cash flows.

2. What is a bond? Identify and discuss three different types of bonds.
V. Montana Memories, Inc. sells Montana products to companies in Germany on a regular basis. Prepare the journal entries for the following transactions.

Oct. 31, 2008 Sold Montana products to Weimar Company for 13,000 euros, with payment due in 90 days. The exchange rate was $1.16 per euro.

December 31, 2008 The exchange rate was $1.19 per euro.

January 29, 2009 Received payment from Weimar Company when the exchange rate was $1.14.

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<th>Date</th>
<th>Account Titles and Explanation</th>
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VI. Equity Method (Significant Influence)
Prepare journal entries to reflect the long-term investment transactions incurred by Paddy’s Productions, Inc.

March 17, 2009 Purchased 15,000 shares of Cowboy Cinema, Inc. for $29 per share plus $4,500 in fees and commissions. These shares represent a 25% ownership of Cowboy Cinema, Inc.

October 17, 2009 Received a cash dividend of $.90 per share from Cowboy Cinema

December 31, 2009 Cowboy Cinema, Inc. reported net income of $169,500 for the year.
VII. Legacy, Inc. issued $345,000 of 5%, four-year bonds dated January 1, 2009, that pay interest semiannually on June 30 and December 31. They are issued at $332,888 and their market rate is 6% on the issue date. Prepare the journal entries to record the sale of the bonds and to record the first semiannual interest payment on June 30, 2009.

VIII. At December 31, 2008, Sullivan Sports, Inc. owned 450 shares of March Madness, Inc. common stock with a book value (cost) of $47,250 and a year-end market value of $43,700. Sullivan also held bonds issued by Sunshine Adventures, Inc. with a book value of $157,300 and a year-end market value of $168,800. These investments are classified as available-for-sale securities.

Prepare the journal entries to record the market value of the investments as of the company’s December 31, 2008 year-end. (Mark to the Market!)
IX. Statement of Cash Flows

Use the following information to prepare Mikoshika Company’s Statement of Cash Flows (direct method) for the year ended December 31, 2008.

Cash and cash equivalents, beginning year balance $18,000
Cash and cash equivalents, ending year balance 78,750
Cash paid for store equipment 15,750
Cash borrowed on three-month note payable 22,500
Cash payments for merchandise inventory 75,750
Cash paid for salaries 39,000
Cash dividends paid 12,000
Cash payments for other operating expenses 48,000
Building purchased and financed by long-term note payable 78,000
Cash received from customers 220,500
Cash interest received 8,250

Statement of Cash Flows
For Year Ended December 31, 2009

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