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CHAPTER 2

REPORTING INTERCORPORATE INVESTMENTS AND CONSOLIDATION OF WHOLLY OWNED SUBSIDIARIES WITH NO DIFFERENTIAL

ANSWERS TO QUESTIONS

Q2-1 (a) An investment in the voting common stock of another company is reported on an equity-method basis when the investor is able to significantly influence the operating and financial policies of the investee.

(b) An investment in the voting common stock of another company is carried at fair value when the investor is NOT able to significantly influence the operating and financial policies of the investee.

Q2-2 Under normal circumstances, the balance in the intercorporate investment account is expected to be different if the investment is carried at fair value, or if the equity method of accounting is used.

Q2-3 At the time the investment qualifies for use of the equity method, the investor shall add the cost of acquiring the additional interest in the investee (if any) to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting

Q2-4 A dividend is treated as a reduction of the investment account under equity-method reporting. A dividend received on investments carried at fair value is recorded as dividend income.

Q2-5 For securities carried at fair value, the change in the fair value of the shares held by the investor is recorded as an unrealized gain or loss at the end of the period. Under the equity method the investor's share of the earnings of the investee are recorded as investment income (and recorded as an increase to the investment account). Under the equity method any dividends received from the investee are treated as a reduction of the investment account and these dividends are not considered income to the investor.

Q2-6 A one-line consolidation implies that under equity-method reporting the investor's net income and stockholders' equity will be the same as if the investee were consolidated. Income from the investee is included in a single line in the investor's income statement and the investment is reported as a single line in the investor's balance sheet.

Q2-7 An adjusting entry is recorded on the company's books and causes the balances reported by the parent or subsidiary company to change. Consolidation entries, on the other hand, are not recorded on the books of the companies. Instead, they are entered in the consolidation worksheet so that when the amounts included in the consolidation entries are applied, - the appropriate balances for the consolidated entity are reported.

Q2-8 Each of the stockholders' equity accounts of the subsidiary is eliminated in the consolidation process. Thus, none of the balances is included in the stockholders' equity accounts of the consolidated entity. That portion of the stockholders' equity claim assigned to the noncontrolling shareholders is reported indirectly in the balance assigned to the noncontrolling shareholders.

Q2-9 Additional entries are needed to eliminate all income statement and retained earnings statement effects of intercorporate ownership and any transfers of goods and services between related companies.

Q2-10 Separate parts of the consolidation worksheet are used to develop the consolidated income statement, retained earnings statement, and balance sheet. All consolidation entries needed to complete the entire worksheet normally are entered before any of the three statements are prepared. The income statement portion of the worksheet is completed first so that net income can be carried forward to the retained earnings statement portion of the worksheet. When the retained earnings portion is completed, the ending balances are carried forward and entered in the consolidated balance sheet portion of the worksheet.

Q2-11 None of the dividends declared by the subsidiary are included in the consolidated retained earnings statement. Those which are paid to the parent have not gone outside the consolidated entity and therefore must be eliminated in preparing the consolidated statements.

Q2-12 Consolidated net income includes 100 percent of the revenues and expenses of the individual consolidating companies arising from transactions with unaffiliated companies.

Q2-13 Consolidated retained earnings is that portion of the undistributed earnings of the consolidated entity accruing to the parent company shareholders.

Q2-14 Consolidated retained earnings at the end of the period is equal to the beginning consolidated retained earnings balance plus consolidated net income attributable to the controlling interest, less consolidated dividends. Under the fully adjusted equity method, consolidated retained earnings should equal the parent company's retained earnings.

Q2-15 The retained earnings statement shows the increase or decrease in retained earnings during the period. Thus, income for the period is added to the beginning balance and dividends are deducted in deriving the ending balance in retained earnings. Because the consolidation worksheet includes the retained earnings statement, the beginning retained earnings balance must be entered in the worksheet.

Q2-16A The general rule established in ASC 323 is that in the absence of other evidence, common stock ownership of 20 percent or more is viewed as indicating that the investor is able to exercise significant influence over the investee. However, ASC 323-10-15-6 also states a number of factors that could constitute other evidence of the ability to exercise significant influence:

1. Representation on board of directors.
2. Participation in policy making.
3. Material intercompany transactions.
4. Interchange of managerial personnel.
5. Technological dependency.
6. Size of investment in relation to concentration of other shareholdings.

Q2-17A Equity-method reporting should not be used when (a) the investee has initiated litigation or complaints challenging the investor's ability to exercise significant influence, (b) the investor signs an agreement surrendering important shareholder rights, (c) majority ownership is concentrated in a small group that operates the company without regard to the investor's desires, (d) the investor is not able to acquire the information from the investee, or (e) the investor tries and fails to gain representation on the board of directors.

Q2-18A When the modified equity method is used, a proportionate share of subsidiary net income and dividends is recorded on the parent's books and an appropriate amount of any differential is amortized each period. In some situations, companies also choose not to make adjustments for intercompany profits and the amortization of the differential. Under the fully adjusted equity method, the parent's books also are adjusted for unrealized profits and any other items that are needed to bring the investor's net income into agreement with the income to the controlling interest that would be reported if consolidation were used.

Q2-19A The term modified equity method generally is used when the investor records its portion of the reported net income and dividends of the investee and amortizes an appropriate portion of any differential. Unlike the fully adjusted equity method, no adjustment for unrealized profit on intercompany transfers normally is made on the investor's books. (In some situations, companies also choose not to amortize the differential.) When an investee is consolidated for financial reporting purposes, the investor may not feel it is necessary to record fully adjusted equity method entries on its books since income from the investee and the balance in the investment account must be eliminated in preparing the consolidated statements.

SOLUTIONS TO CASES

C2-1 Choice of Accounting Method

a. The equity method is to be used when an investor has significant influence over an investee. Significant influence normally is assumed when more than 20 percent ownership is held. Factors to be considered in determining whether to apply equity-method reporting include the following:

1. Is the investee under the control of the courts or other parties as a result of filing for reorganization or entering into liquidation procedures?

2. Does the investor have representation on the board of directors, or has it attempted to gain representation and been unable to do so?

3. Has the investee initiated litigation or complaints challenging the investor's ability to exercise significant influence?

4. Has the investor signed an agreement surrendering its ability to exercise significant influence?

5. Is majority ownership concentrated in a small group that operates the company without regard of the wishes of the investor?

6. Is the investor able to acquire the information needed to use equity-method reporting?

b. The equity method will align the contribution to Slanted's earnings with the earnings reported by Flat. If the investment is carried at fair value, the contribution to Slanted's earnings will be aligned with the change in market value of Flat's shares, thus market expectations play a key role in the contribution to earnings if the investment is carried at fair value.

c. The key reason that the equity method is more appropriate as the percentage of ownership increases is that GAAP requires the use of the equity method at the point when the investor gains significant influence over an investee. Therefore Slanted is likely to be required to use the equity method to account for its investment in Flat. Some of the reasons for this include that as the investor uses more of its resources to acquire ownership of the investee, and as the investor has a greater share of the investee's profits and losses, the success of the investee's operations may have more of an impact on the overall financial well-being of the investor. In many cases, the investor will want to participate in key decisions of the investee once the investor's ownership share reaches a certain level. Also, use of the equity method eliminates the possibility of the investor manipulating its own income by influencing investee dividend distributions, as might occur if the investor carries the investment at fair value.

C2-2 Intercorporate Ownership

MEMO

To: Chief Accountant
Most Company

From: ______ ______, CPA

Re: Equity Method Reporting for Investment in Adams Company

The equity method should be used in reporting investments in which the reporting company has a significant influence over the operating and financing decisions of another company. In this case, Most Company holds 15 percent of the voting common stock of Adams Company and Port Company holds an additional 10 percent. During the course of the year, both Most and Port are likely to carry their respective investments in Adams at fair value. However, when consolidated statements are prepared for Most, the combined ownership must be used in determining whether significant influence exists. Both direct and indirect ownership must be taken into consideration. [ASC 323]

A total of 15 percent of the voting common stock of Adams is held directly by Most Company and an additional 10 percent is controlled indirectly through Most's ownership of Port Company. Equity-method reporting for the investment in Adams Company therefore appears to be required in the consolidated financial statements.

If Most and Port have carried their investments in Adams at fair value during the year, then at the time consolidated statements are prepared, adjustments must be made to (a) increase the balance in the investment account for a proportionate share of the investee's reported net income (25 percent) and reduce the balance in the investment account for a proportionate share of the dividend paid by the investee, (b) include a proportionate share of the investee's net income in the consolidated income statement, (c) delete any dividend income recorded by Most and Port, and (d) reverse any impact of entries that Most and Port have made related to changes in fair value of Adams stock during the year.

Primary citation
ASC 323

C2-3 Application of the Equity Method

MEMO

To: Controller
Forth Company

From: ______ ______, CPA

Re: Equity Method Reporting for Investment in Brown Company

This memo is prepared in response to your request to evaluate whether Forth should use the equity method in accounting for its investment in Brown Company, or if the investment should be carried at fair value.

Forth Company held 85 percent of the common stock of Brown Company prior to January 1, 20X2, and was required to fully consolidate Brown Company in its financial statements prepared prior to that date [ASC 810]. Forth now holds only 15 percent of the common stock of Brown. Investments are normally carried at fair value when ownership is less than 20 percent of the stock that is directly or indirectly held by the investor.

Equity-method reporting should be used when the investor has “significant influence over operating and financing policies of the investee.” While 20 percent ownership is regarded as the level at which the investor is presumed to have significant influence, other factors must be considered as well. [ASC 323]

Although Forth currently holds only 15 percent of Brown’s common stock, the other factors associated with its ownership indicate that Forth does exercise significant influence over Brown. Forth has two members on Brown’s board of directors, it purchases a substantial portion of Brown’s output, and Forth appears to be the largest single shareholder by virtue of its sale of 10,000 shares to each of 7 other investors.

These factors provide strong evidence that Forth has significant influence over Brown and points to the need to use equity-method reporting for its investment in Brown. Your office should monitor the activities of the standard setting bodies with respect to consolidation standards [www.fasb.org]. Active consideration is being given to situations in which control may be exercised even though the investor does not hold majority ownership. It is conceivable that your situation might be one in which consolidation could be required.

Primary citations
APB 18, par. 17; ASC 323-10-15-6 through 15-8
ASC 810

C2-4 Need for Consolidation Process

After the financial statements of each of the individual companies are prepared in accordance with generally accepted accounting principles, consolidated financial statements must be prepared for the economic entity as a whole. The individual companies generally record transactions with other subsidiaries on the same basis as transactions with unrelated enterprises. In preparing consolidated financial statements, the effects of all transactions with related companies must be removed, just as all transactions within a single company must be removed in preparing financial statements for that individual company. It therefore is necessary to prepare a consolidation worksheet and to enter a number of special journal entries in the worksheet to remove the effects of the intercorporate transactions. The parent company also reports an investment in each of the subsidiary companies and investment income or loss in its financial statements. Each of these accounts must be eliminated as well as the stockholders' equity accounts of the subsidiaries. The latter must be eliminated so that only the parent's equity remains. This is because only the parent's ownership is held by parties outside the consolidated entity.

C2-5 Account Presentation

MEMO

To: Chief Accountant
Prime Company

From: ______ ______, Accounting Staff

Re: Combining Broadly Diversified Balance Sheet Accounts

Many manufacturing and merchandising enterprises excluded finance, insurance, real estate, leasing, and perhaps other types of subsidiaries from consolidation prior to 1987 on the basis of "nonhomogeneous" operations. Companies generally argued that the accounts of these companies were dissimilar in nature and combining them in the consolidated financial statements would mislead investors. ASC 810 specifically eliminated the exception for nonhomogeneous operations. ASC 810 affirms the requirement for consolidating entities in which a controlling financial interest is held.

Prime Company controls companies in very different industries and combining the accounts of its subsidiaries may lead to confusion by some investors; however, it may be equally confusing to provide detailed listings of assets and liabilities by industry or other breakdowns in the consolidated balance sheet. The actual number of assets and liabilities presented in the consolidated balance sheet must be carefully considered, but is the decision of Prime's management.

It is important to recognize that the notes to the consolidated financial statements are regarded as an integral part of the financial statements and Prime Company is required to include in its notes to the financial statements certain information on its reportable segments [ASC 280]. Because of the diversity of its ownership, Prime may wish to provide more than the minimum disclosures specified in the guidance. Segment information appears to be used quite broadly by investors and permits the company to provide sufficient detail to assist the financial statement user in gaining a better understanding of the various operating divisions of the company.

You have requested information on those situations in which it may not be appropriate to combine similar appearing accounts of two or more subsidiaries. The following is a partial listing of such situations: (a) the accounts of a subsidiary should not be included along with other subsidiaries if control of the assets and liabilities does not rest with Prime Company, as when a subsidiary is in receivership; (b) while the assets and liability accounts of the subsidiary should be combined with the parent, the equity account balances should not; (c) negative account balances in cash or accounts receivable should be reclassified as liabilities rather than being added to the positive balances of other affiliates if there is no right of offset in the underlying bank accounts, and (d) assets pledged for a specific purpose and not available for other use by the consolidated entity generally should be separately reported.

Primary citations:
ASC 810
ASC 280-10
ASC 810-10-65-1
Secondary sources:
ASC 810

C2-6 Consolidating an Unprofitable Subsidiary

MEMO

TO: Chief Accountant
Amazing Chemical Corporation

FROM: ___________ ___________, Accounting Staff

Re: Consolidation of Unprofitable Boatyard

This memo is intended to provide recommendations on the presentation of the boatyard in Amazing Chemical's consolidated financial statements. Amazing Chemical Corporation currently has full ownership of the boatyard and should fully consolidate the boatyard in its financial statements. Consolidated statements should be prepared when a company directly or indirectly has a controlling financial interest in one or more other companies. [ASC 810]. Amazing Chemical appears to be following generally accepted accounting procedures in fully consolidating the boatyard in its financial statements and should continue to do so.

The operations of the boatyard appear to be distinct from the other operations of the parent company and its losses appear to be sufficient to establish it as a reportable segment [ASC 280]. While the operating losses of the boatyard may not be evident in analyzing the consolidated income statement, a review of the notes to the consolidated statements should provide adequate disclosure of its operations as a reportable segment. The financial statements for the current period should contain these disclosures and if prior period statements have not included the boatyard as a reportable segment it may be necessary to restate those statements.

Failure of the president of Amazing Chemical to receive approval by the board of directors for the purchase of the boatyard and his subsequent actions to keep information about its operations from the board members appears to be a serious breach of ethics. These actions by the president should immediately be brought to the attention of the board of directors for appropriate action by the board.

Primary citations:
ASC 810-10-10-1
ASC 810
ASC 280-10-50
ASC 810-10-65-1

SOLUTIONS TO EXERCISES

E2-1 Multiple-Choice Questions on Accounting for Equity Investments [AICPA Adapted]

1. **a** – Cash dividends received will never cause an *increase* in the investment account under either method.

   (b) *Incorrect*. A cash dividend is recorded as dividend income and does not affect the investment account when the investment is carried at fair value. Under the equity method, dividends *reduce* the investment account.
   (c) *Incorrect.* A cash dividend is recorded as dividend income and does not affect the investment account when the investment is carried at fair value.
   (d) *Incorrect.* Under the equity method, dividends *reduce* the investment account.

2. **a** – Because the ownership in Amal Corporation is less than 20%, the investment should be carried at fair value. Accordingly, the $1,500 dividend received from Amal is recorded as dividend revenue.

   (b) *Incorrect*. Stock dividends are not recorded as income.
   (c) *Incorrect.* The cash dividend received from B&K is not recorded as dividend revenue because it is accounted for under the equity method.
   (d) *Incorrect.* The stock dividend and cash dividend from B&K are not recorded as dividend revenue.

3. **a** – Under the equity method, net income increases the investment account while dividends decrease it. Because net income was greater than the dividends declared, this results in a net increase in the investment account. The problem information indicated that fair value of the stock was unchanged during the year. Thus in this problem, the balance at year-end would be lower if the investment was carried at fair value than it would be under the equity method.

   (b) *Incorrect*. This would only be true if the dividends were less than the net income.
   (c) *Incorrect.* It doesn't matter when the dividends are paid; as soon as they are declared they act as a reduction to the investment under the equity method.
   (d) *Incorrect.* It doesn't matter when the dividends are paid; as soon as they are declared they act as a reduction to the investment under the equity method.

4. **b** – Under the equity method the company records a share of the affiliate net income as income for the company. This increases the net income of the company which increases earnings per share.

   (a) *Incorrect*. An increase in income affects long-term assets, not current assets or current liabilities, so it would have no effect on the current ratio.
   (c) *Incorrect.* The assets would be higher so asset turnover would decrease. No other turnover ratios would be affected.
   (d) *Incorrect.* The affiliate company's profitability would not decrease the book value per share of the company, it would increase it since retained earnings would increase with the recognition of income from the subsidiary.

E2-2 Multiple-Choice Questions on Intercorporate Investments

1. **b** – Equity method reporting is used when an investor gains significant influence over the operating and financing decisions of the investee. Typically, this is satisfied by maintaining 20% or more of the voting stock, but can also be obtained by other contractual obligations or circumstances.

   (a) *Incorrect.* Voting shares can be obtained without gaining significant influence (i.e. less than 20%) and thus the equity method is not typically used.
   (c) *Incorrect.* Purchasing goods and services would not constitute significant influence over the company, and thus does not result in the equity method being applied.
   (d) *Incorrect.* This would result in a write-down of the investment, and does not correlate to the use of the equity method.

2. **c** – Under the equity method, net income from the investee causes an increase to the investment, while dividends declared by the investee causes a reduction.

   (a) *Incorrect.* This simply represents the historical cost of the investment. It must be adjusted for the income and dividends declared by the investee.
   (b) *Incorrect.* Dividends declared by the investee cause a reduction to the investment, not an increase.
   (d) *Incorrect.* Net income reported by the investee causes an increase to the investment, not a decrease.

E2-3 Multiple-Choice Questions on Applying Equity Method [AICPA Adapted]

1. **d** – $250,000 + ($100,000 x 0.30) – ($10,000 x 0.30) = $277,000

2. **d** – If the investment had been accounted for using the equity method, Investor would have recorded its share of Alimand's income by increasing the investment account and increasing earnings by $40,000 ($100,000 x 40%). Investor would also have decreased the investment account by $4,000 for its share of the dividends ($10,000 x 40%). However, since Investor incorrectly accounted for the investment as if were carried at fair value, the only entry Investor recorded was to increase income by $4,000 for the dividends. As a result, the investment account will be understated, earnings will be understated, and retained earnings will be understated.

3. **d** – Under the equity method, dividends by the investee are recorded with a credit to the investment account, not to dividend revenue. By wrongly classifying this entry, the investment is overstated, and retained earnings are also overstated.

   (a) *Incorrect.* Because the dividend entry was recorded incorrectly, the financial position will not be correctly stated.
   (b) *Incorrect.* Because the dividends were recorded as dividend revenue, retained earnings would be overstated.
   (c) *Incorrect.* Currently, the investment is overstated because the dividends declared should have resulted in a reduction to the investment account.

E2-4 Carrying an Investment at Fair Value versus Equity Method Reporting

a. Winston Corporation net income – carried at fair value:

20X2	$100,000	+	.40($30,000)	+	$20,000	$132,000
20X3	$ 60,000	+	.40($60,000)	+	$20,000	104,000
20X4	$250,000	+	.40($50,000[a])	+	$20,000	290,000

[a] A liquidating dividend can impact the entry made by the company declaring the dividend where it may need to debit a paid-in-capital account instead of a retained earnings account.

In the past, if the recipient of the dividend was accounting for the equity investment under the cost method, then the entry to record a liquidating dividend needed to be modified to exclude the liquidating amount from dividend income. The liquidating amount received was recorded as a reduction in the investment.

However, under current standards if the equity investment is being accounting for under the equity method, then all dividends are treated as a return of investment (as opposed to a return on investment). Therefore, all dividends are all dividends are effectively accounted for as liquidating the investment (hopefully the investment is increasing through investee earnings).

If the investment is carried at fair value, then dividends received are recorded as income. However, all changes in fair value are also recorded through income each period. If a company is truly in the process of liquidating paid in capital, the fair value of that company will be expected to be declining.

b. Winston Corporation net income – equity method:

20X2	$100,000	+	.40($70,000)	$128,000
20X3	$ 60,000	+	.40($40,000)	76,000
20X4	$250,000	+	.40($25,000)	260,000

E2-5 Acquisition Price

Balance at date of acquisition:

a. Carried at fair value: $54,000 − $6,000 = $48,000

The investment account would be increased by $2,000 each year reflecting the increase in the market value of Phillips' investment in Jones' stock.

b. Equity method $54,000 - $2,000 = $52,000

Year	Net Income	Dividends	Phillips's share of Investment
20X1	$ 8,000	$15,000	$(2,800)
20X2	12,000	10,000	800

20X3	20,000	10,000	4,000
Change in account balance			$ 2,000

E2-6 Investment Income

a. (1) Ravine Corporation net income when investment is carried at fair value:

20X6	$140,000	+	0.30($20,000)	+ $10,000	=	$156,000
20X7	$ 80,000	+	0.30($40,000)	+ $10,000	=	$102,000
20X8	$220,000	+	0.30($40,000)	+ $10,000	=	$242,000
20X9	$160,000	+	0.30($20,000)	+ $10,000	=	$176,000

A liquidating dividend can impact the entry made by the company declaring the dividend where it may need to debit a paid-in-capital account instead of a retained earnings account.

In the past, if the recipient of the dividend was accounting for the equity investment under the cost method, then the entry to record a liquidating dividend needed to be modified to exclude the liquidating amount from dividend income. The liquidating amount received was recorded as a reduction in the investment.

However, under current standards if the equity investment is being accounting for under the equity method, then all dividends are treated as a return of investment (as opposed to a return on investment). Therefore, all dividends are all dividends are effectively accounted for as liquidating the investment (hopefully the investment is increasing through investee earnings).

If the investment is carried at fair value, then dividends received are recorded as income. However, all changes in fair value are also recorded through income each period. If a company is truly in the process of liquidating paid in capital, the fair value of that company will be expected to be declining.

(2) Ravine Corporation net income under Equity Method:

20X6	$140,000	+	0.30($30,000)	=	$149,000
20X7	$ 80,000	+	0.30($50,000)	=	$ 95,000
20X8	$220,000	+	0.30($10,000)	=	$223,000
20X9	$160,000	+	0.30($40,000)	=	$172,000

b. Journal entries recorded by Ravine Corporation in 20X8:

(1) Carried at fair value:

Cash	12,000	
Dividend Income		12,000

Investment in Valley Stock	10,000	
Unrealized Gain on Valley Stock		10,000

(2) Equity method:

Cash	12,000	

Investment in Valley Stock		12,000

Investment in Valley Stock	3,000	
Income from Valley		3,000

E2-7 Investment Value

The following amounts would be reported as the carrying value of Port's investment in Sund:

20X2	$184,500	=	$180,000	+	($40,000 x 0.30)	-	($25,000 x 0.30)
20X3	$193,500	=	$184,500	+	($30,000 x 0.30)		
20X4	$195,000	=	$193,500	+	($5,000 x 0.30)		

E2-8 Carrying an Investment at Fair Value versus Equity Method Reporting

a. Fair value method:

Operating income reported by Mock	$90,000
Unrealized gain on increase in value of Small stock	16,000
Dividend income from Small ($15,000 x 0.20)	3,000
Net income reported by Mock	$ 109,000

b. Equity method:

Operating income reported by Mock	$90,000
Income from investee ($40,000 x 0.20)	8,000
Net income reported by Mock	$98,000

E2-9 Carrying an Investment at Fair Value versus Equity Method Reporting

a. Journal entries under the equity method:

(1)	Investment in Lomm Company Stock	140,000	
	Cash		140,000

Record purchase of Lomm Company stock.

(2)	Cash	7,000	
	Investment in Lomm Company Stock		7,000

Record dividends from Lomm Company: $20,000 x 0.35

(3)	Investment in Lomm Company Stock	28,000	
	Income from Lomm Company		28,000

Record equity-method income: $80,000 x 0.35

b. Journal entries for investment carried at fair value.

(1)	Investment in Lomm Company Stock	140,000	
	Cash		140,000
	Record purchase of Lomm Company stock.		
(2)	Cash	7,000	
	Dividend Income		7,000
	Record dividends from Lomm Company: $20,000 x 0.35		
(3)	Investment in Lomm Company Stock	34,000	
	Unrealized Gain on Increase in Value of Lomm Stock		34,000
	Record increase in value of Lomm stock: $174,000 - $140,000		

E2-10 Basic Consolidation Entry

Common Stock – Broadway Corporation	200,000	
Additional Paid-In Capital	300,000	
Retained Earnings	100,000	
Investment in Broadway Common Stock		600,000

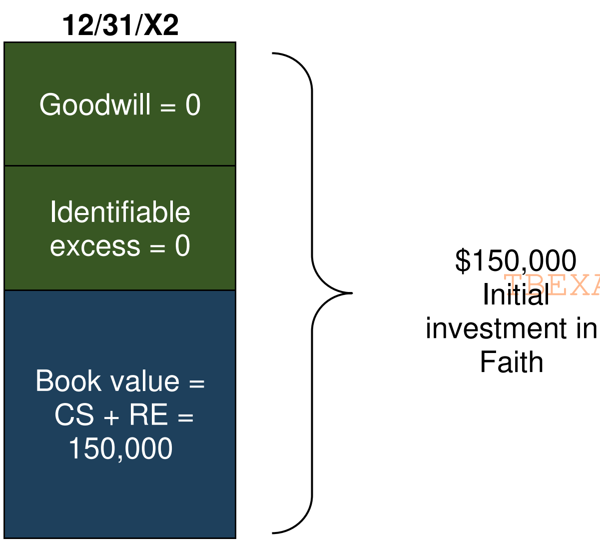
E2-11 Balance Sheet Worksheet

a.

Equity Method Entries on Blank's Books:

Investment in Faith	150,000	
Cash		150,000

Record the initial investment in Faith



Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Ending book value	150,000		60,000		90,000

Basic Consolidation Entry

Common stock	60,000	
Retained earnings	90,000	
Investment in Faith		150,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	30,000	
Buildings & equipment		30,000

E2-11 (continued)

(Since the buildings and equipment are reported net of accumulated depreciation on the balance sheet, this entry will not affect the worksheet. However, if sufficient information had been given, this entry would have made a difference in the worksheet balances for Buildings and Equipment and Accumulated Depreciation. Additionally, this entry would impact any footnote disclosure of the details of Buildings and Equipment.)

b.

			Consolidation Entries		
	Blank	Faith	DR	CR	Consolidated
Balance Sheet					
Cash	65,000	18,000			83,000
Accounts Receivable	87,000	37,000			124,000
Inventory	110,000	60,000			170,000
Buildings & Equipment (net)	220,000	150,000	30,000	30,000	370,000
Investment in Faith	150,000			150,000	0
Total Assets	**632,000**	**265,000**	**30,000**	**180,000**	**747,000**
Accounts Payable	92,000	35,000			127,000
Notes Payable	150,000	80,000			230,000
Common Stock	100,000	60,000	60,000		100,000
Retained Earnings	290,000	90,000	90,000		290,000
Total Liabilities & Equity	**632,000**	**265,000**	**150,000**	**0**	**747,000**

E2-12 Consolidation Entries for Wholly Owned Subsidiary

a.

Equity Method Entries on Trim Corp.'s Books:

Investment in Round Corp.	400,000	
Cash		400,000

Record the initial investment in Round Corp.

Investment in Round Corp.	80,000	
Income from Round Corp.		80,000

Record Trim Corp.'s 100% share of Round Corp.'s 20X2 income

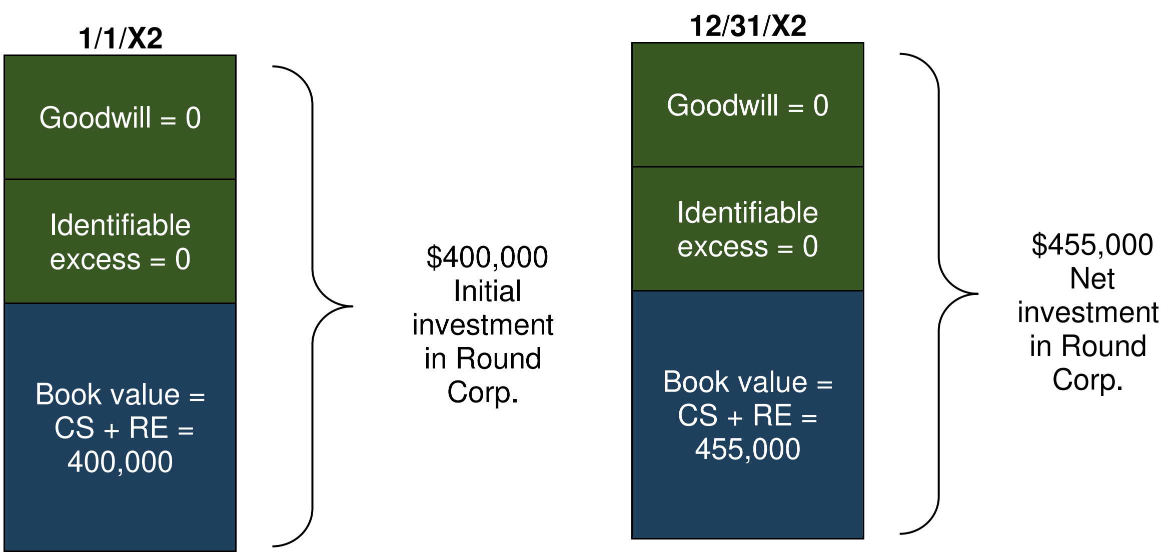
Cash	25,000	
Investment in Round Corp.		25,000

Record Trim Corp.'s 100% share of Round Corp.'s 20X2 dividend

b.

Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Beginning book value	**400,000**		**120,000**		**280,000**
+ Net Income	**80,000**				**80,000**
- Dividends	**(25,000)**				**(25,000)**
Ending book value	**455,000**		**120,000**		**335,000**



E2-12 (continued)

Basic Consolidation Entry

Common stock	**120,000**	
Retained earnings	**280,000**	
Income from Round Corp.	**80,000**	
Dividends declared		**25,000**
Investment in Round Corp.		**455,000**

E2-13 Basic Consolidation Entries for Fully Owned Subsidiary

a.

Equity Method Entries on Purple Co.'s Books:

Investment in Amber Corp.	500,000	
Cash		500,000

Record the initial investment in Amber Corp.

Investment in Amber Corp.	50,000	
Income from Amber Corp.		50,000

Record Purple Co.'s 100% share of Amber Corp.'s 20X7 income

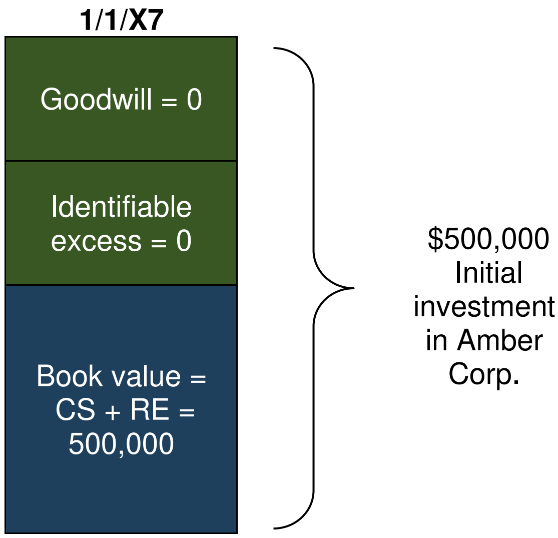
Cash	20,000	
Investment in Amber Corp.		20,000

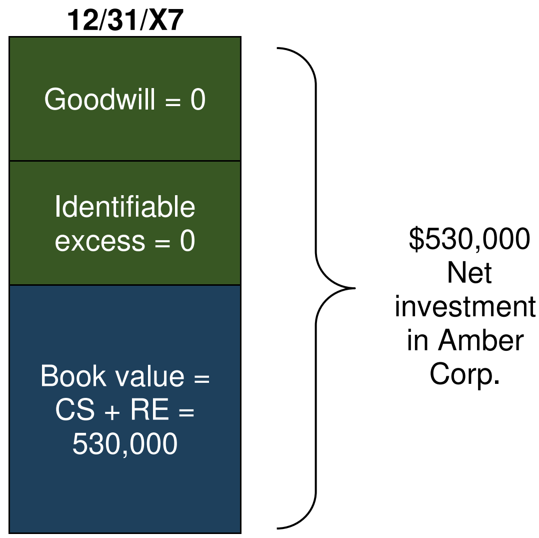
Record Purple Co.'s 100% share of Amber Corp.'s 20X7 dividend

b.

Book Value Calculations:

	Total Book Value	**=**	**Common Stock**	**+**	**Retained Earnings**
Original book value	**500,000**		**300,000**		**200,000**
+ Net Income	**50,000**				**50,000**
- Dividends	**(20,000)**				**(20,000)**
Ending book value	**530,000**		**300,000**		**230,000**


1/1/X7
Goodwill = 0
Identifiable excess = 0
Book value = CS + RE = 500,000
$500,000 Initial investment in Amber Corp.


12/31/X7
Goodwill = 0
Identifiable excess = 0
Book value = CS + RE = 530,000
$530,000 Net investment in Amber Corp.

E2-13 (continued)

Basic Consolidation Entry

Common stock	300,000	
Retained earnings	200,000	
Income from Amber Corp.	50,000	
Dividends declared		20,000
Investment in Amber Corp.		530,000

	Investment in Amber Corp.			Income from Amber Corp.		
Acquisition Price	500,000					
Net Income	50,000				50,000	Net Income
		20,000	Dividends			
Ending Balance	530,000				50,000	Ending Balance
		530,000	Basic	50,000		
	0				0	

E2-14A Income Reporting

Journal entry recorded by Grandview Company:

Investment in Spinet Corporation Stock	36,000	
Income from Spinet Corporation		24,000
Discontinued Operations (from Spinet Corporation)		12,000

E2-15A Investee with Preferred Stock Outstanding

Journal entries recorded by Reden Corporation:

(1)

Investment in Montgomery Co. Stock	288,000	
Cash		288,000

Record purchase of Montgomery Co. stock.

(2)

Cash	6,750	
Investment in Montgomery Co. Stock		6,750

Record dividend from Montgomery Co.: [$40,000 - ($250,000 x .10)] x 0.45

(3)

Investment in Montgomery Co. Stock	31,500	
Income from Montgomery Co.		31,500

Record equity-method income: [$95,000 - ($250,000 x .10)] x 0.45

E2-16A Other Comprehensive Income Reported by Investee

Journal entries recorded by Callas Corp. during 20X9:

(1)	Investment in Thinbill Co. Stock	380,000	
	Cash		380,000
	Record purchase of Thinbill Company		
(2)	Cash	3,600	
	Investment in Thinbill Co. Stock		3,600
	Record dividend from Thinbill: $9,000 x 0.40		
(3)	Investment in Thinbill Co. Stock	18,000	
	Income from Thinbill Co.		18,000
	Record equity-method income: $18,000 = $45,000 x 0.40		
(4)	Investment in Thinbill Co. Stock	8,000	
	Unrealized Gain on Investments of Investee (OCI)		8,000
	Record share of OCI reported by Thinbill: $8,000 = $20,000 x 0.40		

Closing entries recorded at December 31, 20X9:

(5)	Income from Thinbill Co.	18,000	
	Retained Earnings		18,000
(6)	Unrealized Gain on Investments of Investee (OCI)	8,000	
	Accumulated Other Comprehensive Income from Investee-Unrealized Gain on Investments		8,000

E2-17A Other Comprehensive Income Reported by Investee

Investment account balance reported by Baldwin Corp.		$67,000
Add decrease in account recorded in 20X8:		
Equity-method loss ($20,000 x .25)	$ (5,000)	
Dividend received ($10,000 x .25)	(2,500)	7,500
Deduct increase in account recorded in 20X9:		
Equity-method income ($68,000 x .25)	$17,000	
Dividend received ($16,000 x .25)	(4,000)	
Other comprehensive income reported by Gwin Company ($12,000 x .25)	3,000	(16,000)
Purchase price		$58,500

SOLUTIONS TO PROBLEMS
P2-18 Changes in the Number of Shares Held

Journal entries recorded by Idle Corporation:

(1)	Investment in Fast Track Enterprises Stock	34,000	
	Cash		34,000
	Record purchase of Fast Track stock.		

(3)	Dividends Receivable	5,000	
	Investment in Fast Track Enterprises Stock		5,000
	Record dividend from Fast Track Enterprises: $20,000 x .25		

(4)	Investment in Fast Track Enterprises Stock	12,500	
	Income from Fast Track Enterprises		12,500
	Record equity-method income: $50,000 x .25		

P2-19 Investments Carried at Fair Value and Equity Method

a. Fair value method:

	20X6	20X7	20X8
Investment income:			
Dividends received	$ 3,000	$ 6,000	$ 4,000
Gain (loss) on fair value	19,000	(3,000)	11,000
Total income reported	$22,000	$ 3,000	$15,000
Balance in investment account	$89,000	$86,000	$97,000

b. Equity method:

	20X6	20X7	20X8
Investment income:			
$40,000 x .20	$ 8,000		
$35,000 x .20		$ 7,000	
$60,000 x .20			$12,000
Balance in investment account:			
Balance at January 1	$70,000	$75,000	$76,000
Investment income	8,000	7,000	12,000
Dividends received	(3,000)	(6,000)	(4,000)
Balance at December 31	$75,000	$76,000	$84,000

P2-20 Carried at Fair Value Journal Entries

Journal entries investment carried at fair value for 20X8:

(1)	Investment in Brown Company Stock	85,000	
	Cash		85,000
	Record purchase of Brown Company stock.		

(2)	Cash	4,000	

	Dividend Income		4,000

Record dividends from Brown Company: $10,000 x .40

(3)	Investment in Brown Company Stock	12,000	
	Unrealized Gain on Increase in Value of Brown Company Stock		12,000

Record increase in value of Brown stock: $97,000 - $85,000

Journal entries investment carried at fair value for 20X9:

(1)	Cash	6,000	
	Dividend Income		6,000

Record dividends from Brown Company: $15,000 x .40

(2)	Unrealized Loss on Decrease in Value of Brown Company Stock	5,000	
	Investment in Brown Company Stock		5,000

Record decrease in value of Brown stock: $97,000 - $92,000

P2-21 Consolidated Worksheet at End of the First Year of Ownership (Equity Method)

a.

Equity Method Entries on Peanut Co.'s Books:

Investment in Snoopy Co.	300,000	
Cash		300,000

Record the initial investment in Snoopy Co.

Investment in Snoopy Co.	75,000	
Income from Snoopy Co.		75,000

Record Peanut Co.'s 100% share of Snoopy Co.'s 20X8 income

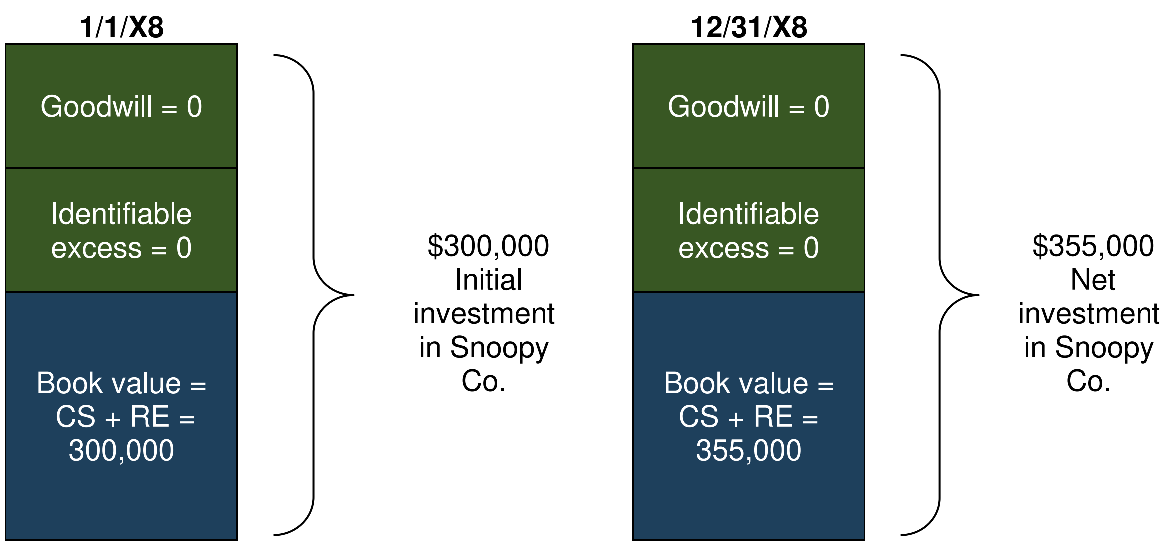
Cash	20,000	
Investment in Snoopy Co.		20,000

Record Peanut Co.'s 100% share of Snoopy Co.'s 20X8 dividend

b.

Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Beginning book value	**300,000**		**200,000**		**100,000**
+ Net Income	**75,000**				**75,000**
- Dividends	**(20,000)**				**(20,000)**
Ending book value	**355,000**		**200,000**		**155,000**



P2-21 (continued)

Basic Consolidation Entry

Common stock	200,000	
Retained earnings	100,000	
Income from Snoopy Co.	75,000	
Dividends declared		20,000
Investment in Snoopy Co.		355,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	10,000	
Buildings & equipment		10,000

The amount of this entry is found by looking at the depreciation expense ($10,000) for the year and the accumulated depreciation at the end of the year ($20,000). The difference must be what was in accumulated depreciation at the date of the acquisition. Note that this assumes there were no sales or other disposals of Buildings and equipment during the year.

Investment in Snoopy Co.

Acquisition Price	300,000		
Net Income	75,000		
		20,000	Dividends
Ending Balance	355,000		
		355,000	Basic
	0		

Income from Snoopy Co.

		75,000	Net Income
		75,000	Ending Balance
Basic	75,000		
		0	

P2-21 (continued)

	Peanut Co.	Snoopy Co.	Consolidation Entries DR	Consolidation Entries CR	Consolidated
Income Statement					
Sales	800,000	250,000			1,050,000
Less: COGS	(200,000)	(125,000)			(325,000)
Less: Depreciation Expense	(50,000)	(10,000)			(60,000)
Less: Other Expenses	(225,000)	(40,000)			(265,000)
Income from Snoopy Co.	75,000		75,000		0
Net Income	**400,000**	**75,000**	**75,000**	**0**	**400,000**
Statement of Retained Earnings					
Beginning Balance	225,000	100,000	100,000		225,000
Net Income	**400,000**	**75,000**	**75,000**	**0**	400,000
Less: Dividends Declared	(100,000)	(20,000)		20,000	(100,000)
Ending Balance	**525,000**	**155,000**	**175,000**	**20,000**	**525,000**
Balance Sheet					
Cash	130,000	80,000			210,000
Accounts Receivable	165,000	65,000			230,000
Inventory	200,000	75,000			275,000
Investment in Snoopy Co.	355,000			355,000	0
Land	200,000	100,000			300,000
Buildings & Equipment	700,000	200,000		10,000	890,000
Less: Accumulated Depreciation	(450,000)	(20,000)	10,000		(460,000)
Total Assets	**1,300,000**	**500,000**	**10,000**	**365,000**	**1,445,000**
Accounts Payable	75,000	60,000			135,000
Bonds Payable	200,000	85,000			285,000
Common Stock	500,000	200,000	200,000		500,000
Retained Earnings	**525,000**	**155,000**	**175,000**	**20,000**	525,000
Total Liabilities & Equity	**1,300,000**	**500,000**	**375,000**	**20,000**	**1,445,000**

P2-22 Consolidated Worksheet at End of the Second Year of Ownership (Equity Method)

a.

Equity Method Entries on Peanut Co.'s Books:

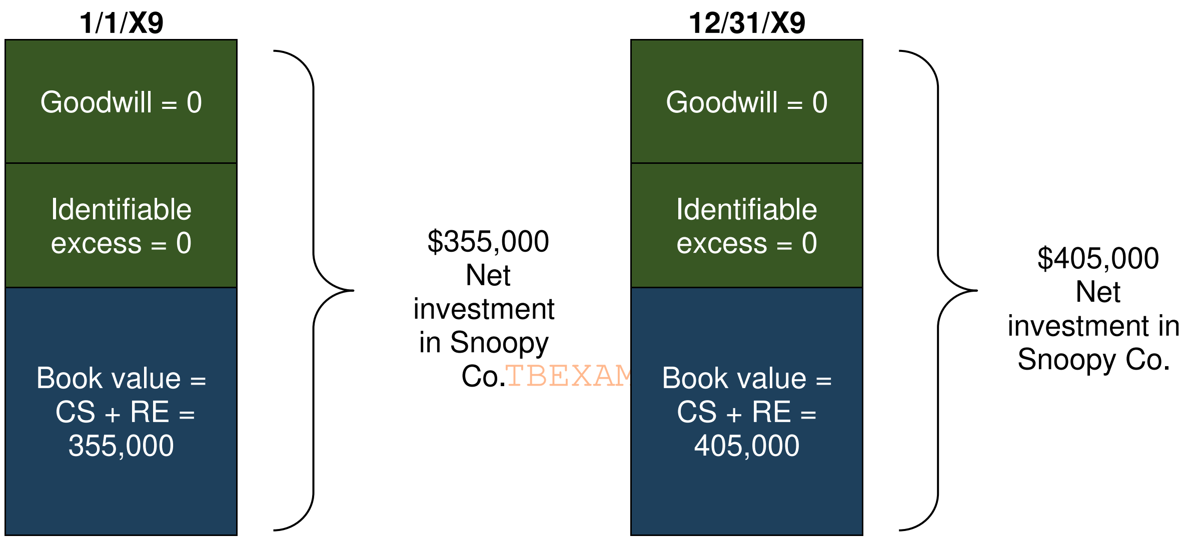
Investment in Snoopy Co.	80,000	
Income from Snoopy Co.		80,000

Record Peanut Co.'s 100% share of Snoopy Co.'s 20X9 income

Cash	30,000	
Investment in Snoopy Co.		30,000

Record Peanut Co.'s 100% share of Snoopy Co.'s 20X9 dividend

b.



Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Beg. book value	**355,000**		**200,000**		**155,000**
+ Net Income	**80,000**				**80,000**
- Dividends	**(30,000)**				**(30,000)**
Ending book value	**405,000**		**200,000**		**205,000**

P2-22 (continued)

Basic Consolidation Entry

Common stock	200,000	
Retained earnings	155,000	
Income from Snoopy Co.	80,000	
Dividends declared		30,000
Investment in Snoopy Co.		405,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	10,000	
Buildings & equipment		10,000

Note that this entry is carried forward from the previous year (see solution to P2-21) again assuming that no sales or other disposals of Buildings and equipment took place during the year.

Investment in Snoopy Co.

Beginning Balance	355,000		
Net Income	80,000		
		30,000	Dividends
Ending Balance	405,000		
		405,000	Basic
	0		

Income from Snoopy Co.

		80,000	Net Income
		80,000	Ending Balance
Basic	80,000		
		0	

P2-22 (continued)

	Peanut Co.	Snoopy Co.	Consolidation Entries DR	Consolidation Entries CR	Consolidated
Income Statement					
Sales	850,000	300,000			1,150,000
Less: COGS	(270,000)	(150,000)			(420,000)
Less: Depreciation Expense	(50,000)	(10,000)			(60,000)
Less: Other Expenses	(230,000)	(60,000)			(290,000)
Income from Snoopy Co.	80,000		80,000		0
Net Income	**380,000**	**80,000**	**80,000**	**0**	**380,000**
Statement of Retained Earnings					
Beginning Balance	525,000	155,000	155,000		525,000
Net Income	**380,000**	**80,000**	**80,000**	**0**	380,000
Less: Dividends Declared	(225,000)	(30,000)		30,000	(225,000)
Ending Balance	**680,000**	**205,000**	**235,000**	**30,000**	**680,000**
Balance Sheet					
Cash	230,000	75,000			305,000
Accounts Receivable	190,000	80,000			270,000
Inventory	180,000	100,000			280,000
Investment in Snoopy Co.	405,000			405,000	0
Land	200,000	100,000			300,000
Buildings & Equipment	700,000	200,000		**10,000**	890,000
Less: Accumulated Depreciation	(500,000)	(30,000)	**10,000**		(520,000)
Total Assets	**1,405,000**	**525,000**	**10,000**	**415,000**	**1,525,000**
Accounts Payable	75,000	35,000			110,000
Bonds Payable	150,000	85,000			235,000
Common Stock	500,000	200,000	200,000		500,000
Retained Earnings	**680,000**	**205,000**	**235,000**	**30,000**	680,000
Total Liabilities & Equity	**1,405,000**	**525,000**	**435,000**	**30,000**	**1,525,000**

P2-23 Consolidated Worksheet at End of the First Year of Ownership (Equity Method)

a.

Equity Method Entries on Paper Co.'s Books:

Investment in Scissor Co.	370,000	
Cash		370,000

Record the initial investment in Scissor Co.

Investment in Scissor Co.	93,000	
Income from Scissor Co.		93,000

Record Paper Co.'s 100% share of Scissor Co.'s 20X8 income

Cash	25,000	
Investment in Scissor Co.		25,000

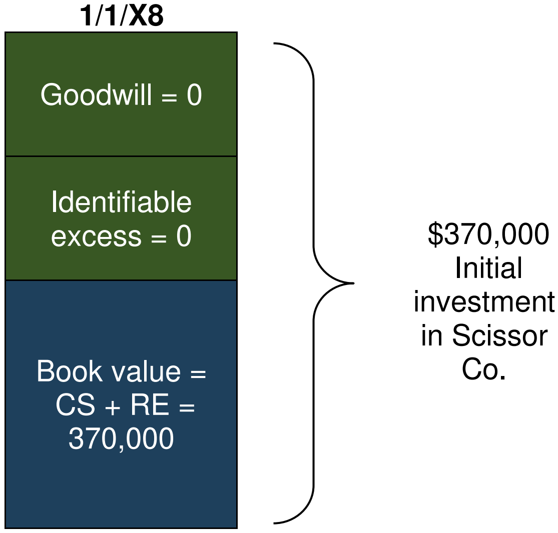
Record Paper Co.'s 100% share of Scissor Co.'s 20X8 dividend

b.

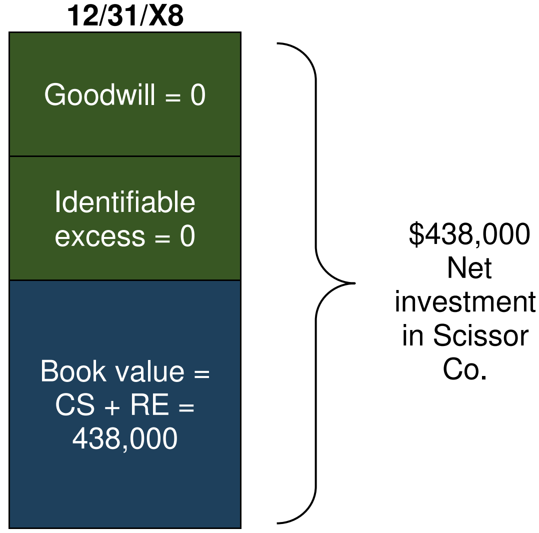
Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Beginning book value	**370,000**		**250,000**		**120,000**
+ Net Income	**93,000**				**93,000**
- Dividends	**(25,000)**				**(25,000)**
Ending book value	**438,000**		**250,000**		**188,000**

1/1/X8



12/31/X8



P2-23 (continued)

Basic Consolidation Entry

Common stock	250,000	
Retained earnings	120,000	
Income from Scissor Co.	93,000	
Dividends declared		25,000
Investment in Scissor Co.		438,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	24,000	
Buildings & equipment		24,000

The amount of this entry is found by looking at the depreciation expense ($12,000) for the year and the accumulated depreciation at the end of the year ($36,000). The difference must be what was in accumulated depreciation at the date of the acquisition. Note that this assumes there were no sales or other disposals of Buildings and equipment during the year.

	Investment in Scissor Co. (Dr)	Investment in Scissor Co. (Cr)		Income from Scissor Co. (Dr)	Income from Scissor Co. (Cr)	
Acquisition Price	370,000					
Net Income	93,000				93,000	Net Income
		25,000	Dividends			
Ending Balance	438,000				93,000	Ending Balance
		438,000	Basic	93,000		
	0				0	

P2-23 (continued)

	Paper Co.	Scissor Co.	Consolidation Entries DR	Consolidation Entries CR	Consolidated
Income Statement					
Sales	800,000	310,000			1,110,000
Less: COGS	(250,000)	(155,000)			(405,000)
Less: Depreciation Expense	(65,000)	(12,000)			(77,000)
Less: Other Expenses	(280,000)	(50,000)			(330,000)
Income from Scissor Co.	93,000		93,000		0
Net Income	**298,000**	**93,000**	**93,000**	**0**	**298,000**
Statement of Retained Earnings					
Beginning Balance	280,000	120,000	120,000		280,000
Net Income	**298,000**	**93,000**	**93,000**	**0**	298,000
Less: Dividends Declared	(80,000)	(25,000)		25,000	(80,000)
Ending Balance	**498,000**	**188,000**	**213,000**	**25,000**	**498,000**
Balance Sheet					
Cash	122,000	46,000			168,000
Accounts Receivable	140,000	60,000			200,000
Inventory	190,000	120,000			310,000
Investment in Scissor Co.	438,000			438,000	0
Land	250,000	125,000			375,000
Buildings & Equipment	875,000	250,000		**24,000**	1,101,000
Less: Accumulated Depreciation	(565,000)	(36,000)	**24,000**		(577,000)
Total Assets	**1,450,000**	**565,000**	**24,000**	**462,000**	**1,577,000**
Accounts Payable	77,000	27,000			104,000
Bonds Payable	250,000	100,000			350,000
Common Stock	625,000	250,000	250,000		625,000
Retained Earnings	**498,000**	**188,000**	**213,000**	**25,000**	498,000
Total Liabilities & Equity	**1,450,000**	**565,000**	**463,000**	**25,000**	**1,577,000**

P2-24 Consolidated Worksheet at End of the Second Year of Ownership (Equity Method)

a.

Equity Method Entries on Paper Co.'s Books:

Investment in Scissor Co.	107,000	
Income from Scissor Co.		107,000

Record Paper Co.'s 100% share of Scissor Co.'s 20X9 income

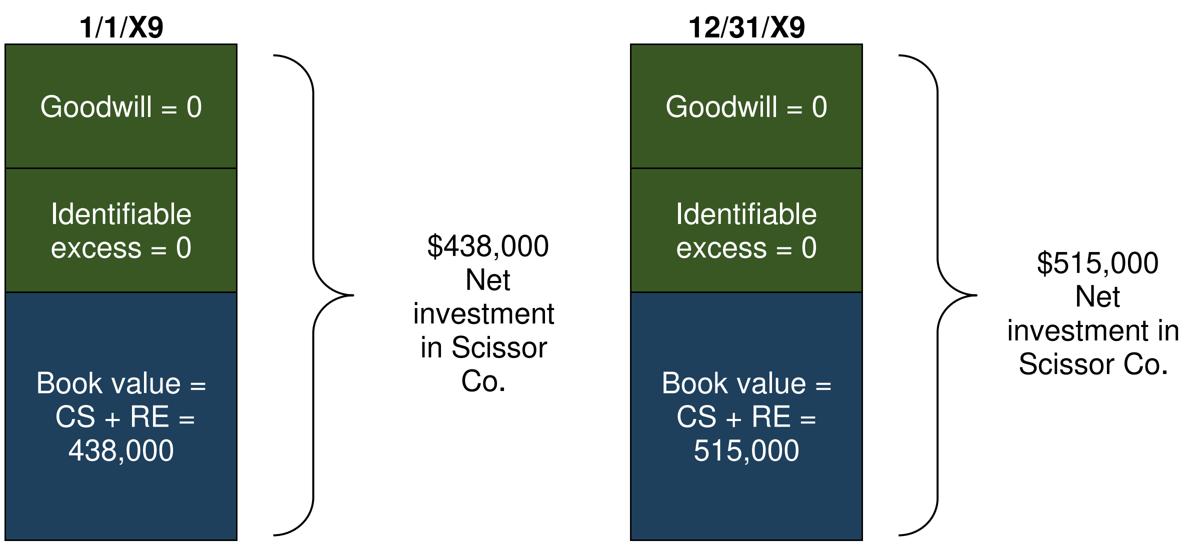
Cash	30,000	
Investment in Scissor Co.		30,000

Record Paper Co.'s 100% share of Scissor Co.'s 20X9 dividend

b.

Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Beg. book value	**438,000**		**250,000**		**188,000**
+ Net Income	**107,000**				**107,000**
- Dividends	**(30,000)**				**(30,000)**
Ending book value	**515,000**		**250,000**		**265,000**



P2-24 (continued)

Basic Consolidation Entry

Common stock	250,000	
Retained earnings	188,000	
Income from Scissor Co.	107,000	
Dividends declared		30,000
Investment in Scissor Co.		515,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	24,000	
Buildings & equipment		24,000

Note that this entry is carried forward from the previous year (see solution to P2-23) again assuming that no sales or other disposals of Buildings and equipment took place during the year.

	Investment in Scissor Co.			Income from Scissor Co.		
Beginning Balance	438,000					
Net Income	107,000				107,000	Net Income
		30,000	Dividends			
Ending Balance	515,000				107,000	Ending Balance
		515,000	Basic	107,000		
	0				0	

P2-24 (continued)

	Paper Co.	Scissor Co.	Consolidation Entries DR	Consolidation Entries CR	Consolidated
Income Statement					
Sales	880,000	355,000			1,235,000
Less: COGS	(278,000)	(178,000)			(456,000)
Less: Depreciation Expense	(65,000)	(12,000)			(77,000)
Less: Other Expenses	(312,000)	(58,000)			(370,000)
Income from Scissor Co.	107,000		107,000		0
Net Income	**332,000**	**107,000**	**107,000**	**0**	**332,000**
Statement of Retained Earnings					
Beginning Balance	498,000	188,000	188,000		498,000
Net Income	**332,000**	**107,000**	**107,000**	**0**	332,000
Less: Dividends Declared	(90,000)	(30,000)		30,000	(90,000)
Ending Balance	**740,000**	**265,000**	**295,000**	**30,000**	**740,000**
Balance Sheet					
Cash	232,000	116,000			348,000
Accounts Receivable	165,000	97,000			262,000
Inventory	193,000	115,000			308,000
Investment in Scissor Co.	515,000			515,000	0
Land	250,000	125,000			375,000
Buildings & Equipment	875,000	250,000		24,000	1,101,000
Less: Accumulated Depreciation	(630,000)	(48,000)	24,000		(654,000)
Total Assets	**1,600,000**	**655,000**	**24,000**	**539,000**	**1,740,000**
Accounts Payable	85,000	40,000			125,000
Bonds Payable	150,000	100,000			250,000
Common Stock	625,000	250,000	250,000		625,000
Retained Earnings	**740,000**	**265,000**	**295,000**	**30,000**	740,000
Total Liabilities & Equity	**1,600,000**	**655,000**	**545,000**	**30,000**	**1,740,000**

P2-25A Other Comprehensive Income Reported by Investee

a. Equity-method income reported by Dewey Corporation in 20X5:

Amounts reported by Jimm Co. for 20X5:	
Operating income	$70,000
Dividend income	7,000
Gain on investment in trading securities	18,000
Net income	$95,000
Ownership held by Dewey	x .30
Investment income reported by Dewey	$28,500

b. Computation of other comprehensive income reported by Jimm Co.:

Amount added to investment account in 20X5	$ 37,800
Investment income reported by Dewey in 20X5	(28,500)
Increase due to other comprehensive income reported by Jimm Co.	$ 9,300
Proportion of ownership held by Dewey	÷ 0.30
Other comprehensive income reported by Jimm Co.	$ 31,000

P2-26A Equity-Method Income Statement

a.

Diversified Products Corporation
Income Statement
Year Ended December 31, 20X8

Net Sales		$400,000
Cost of Goods Sold		(320,000)
Gross Profit		$ 80,000
Other Expenses	$(25,000)	
Gain on Sale of Truck	10,000	(15,000)
Income from Continuing Operations		$ 65,000
Discontinued Operations:		
Operating Loss from Discontinued Division	$(15,000)	
Gain on Sale of Division	44,000	29,000
Net Income		$ 94,000

P2-26A (continued)

Diversified Products Corporation
Retained Earnings Statement
Year Ended December 31, 20X8

Retained Earnings, January 1, 20X8	$260,000
20X8 Net Income	94,000
	$354,000
Dividends Declared, 20X8	(10,000)
Retained Earnings, December 31, 20X8	$344,000

b.

Wealthy Manufacturing Company
Income Statement
Year Ended December 31, 20X8

Net Sales		$850,000
Cost of Goods Sold		(670,000)
Gross Profit		$180,000
Other Expenses	$(90,000)	
Income from Continuing Operations of Diversified Products Corporation	26,000	(64,000)
Income from Continuing Operations		$116,000
Discontinued Operations:		
Share of Operating Loss Reported by Diversified Products on Discontinued Division	$ (6,000)	
Share of Gain on Sale of Division Reported by Diversified Products	17,600	11,600
Net Income		$127,600

Wealthy Manufacturing Company
Retained Earnings Statement
Year Ended December 31, 20X8

Retained Earnings, January 1, 20X8	$420,000
20X8 Net Income	127,600
	$547,600
Dividends Declared, 20X8	(30,000)
Retained Earnings, December 31, 20X8	$517,600

P2-27B Consolidated Worksheet at End of the First Year of Ownership (Investment Carried at Cost)

a.

Investment Carried at Cost Entries on Peanut Co.'s Books:

Investment in Snoopy Co.	300,000	
Cash		300,000

Record the initial investment in Snoopy Co.

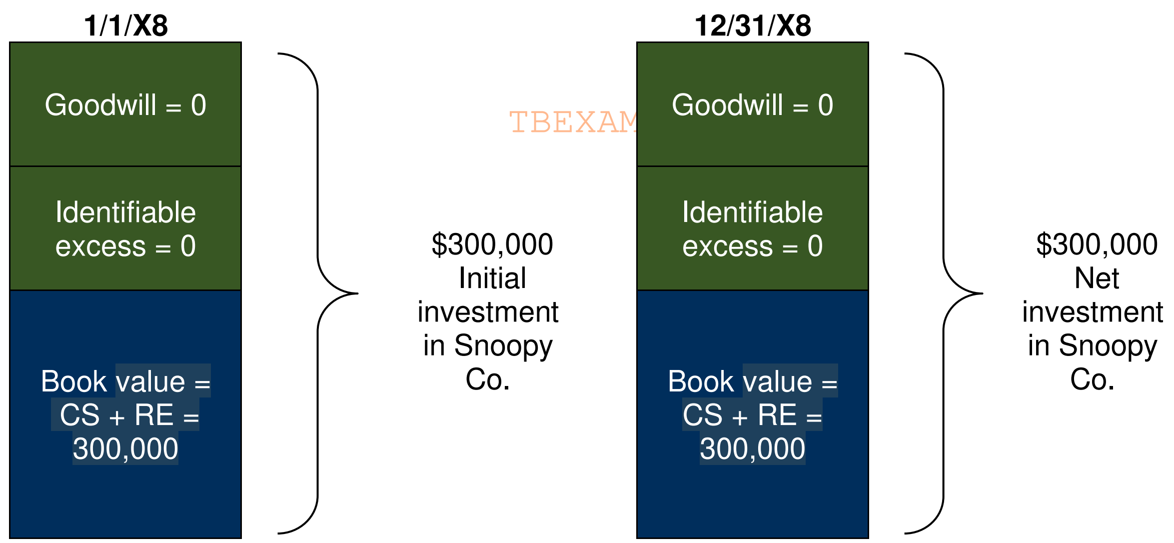
Cash	20,000	
Dividend Income		20,000

Record Peanut Co.'s 100% share of Snoopy Co.'s 20X8 dividend

b.

Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Original book value	300,000		200,000		100,000



P2-27B (continued)

Investment consolidation entry

Common stock	200,000	
Retained earnings	100,000	
Investment in Snoopy Co.		300,000

Dividend consolidation entry

Dividend income	20,000	
Dividends declared		20,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	10,000	
Buildings & equipment		10,000

The amount of this entry is found by looking at the depreciation expense ($10,000) for the year and the accumulated depreciation at the end of the year ($20,000). The difference must be what was in accumulated depreciation at the date of the acquisition. Note that this assumes there were no sales or other disposals of Buildings and equipment during the year.

	Investment in Snoopy Co. (Dr)	Investment in Snoopy Co. (Cr)		Dividend Income (Dr)	Dividend Income (Cr)	
Acquisition Price	300,000					
					20,000	Dividends
Ending Balance	300,000				20,000	Ending Balance
		300,000	Basic	20,000		
	0				0	

P2-27B (continued)

	Peanut Co.	Snoopy Co.	Consolidation Entries DR	Consolidation Entries CR	Consolidated
Income Statement					
Sales	800,000	250,000			1,050,000
Less: COGS	(200,000)	(125,000)			(325,000)
Less: Depreciation Expense	(50,000)	(10,000)			(60,000)
Less: Other Expenses	(225,000)	(40,000)			(265,000)
Dividend Income	20,000		20,000		0
Net Income	**345,000**	**75,000**	**20,000**	**0**	**400,000**
Statement of Retained Earnings					
Beginning Balance	225,000	100,000	100,000		225,000
Net Income	**345,000**	**75,000**	**20,000**	**0**	400,000
Less: Dividends Declared	(100,000)	(20,000)		20,000	(100,000)
Ending Balance	**470,000**	**155,000**	**120,000**	**20,000**	**525,000**
Balance Sheet					
Cash	130,000	80,000			210,000
Accounts Receivable	165,000	65,000			230,000
Inventory	200,000	75,000			275,000
Investment in Snoopy Co.	300,000			300,000	0
Land	200,000	100,000			300,000
Buildings & Equipment	700,000	200,000		10,000	890,000
Less: Accumulated Depreciation	(450,000)	(20,000)	10,000		(460,000)
Total Assets	**1,245,000**	**500,000**	**10,000**	**310,000**	**1,445,000**
Accounts Payable	75,000	60,000			135,000
Bonds Payable	200,000	85,000			285,000
Common Stock	500,000	200,000	200,000		500,000
Retained Earnings	**470,000**	**155,000**	**120,000**	**20,000**	525,000
Total Liabilities & Equity	**1,245,000**	**500,000**	**320,000**	**20,000**	**1,445,000**

P2-28B Consolidated Worksheet at End of the Second Year of Ownership (Investment Carried at Cost)

a.

Investment Carried at Cost Entries on Peanut Co.'s Books:

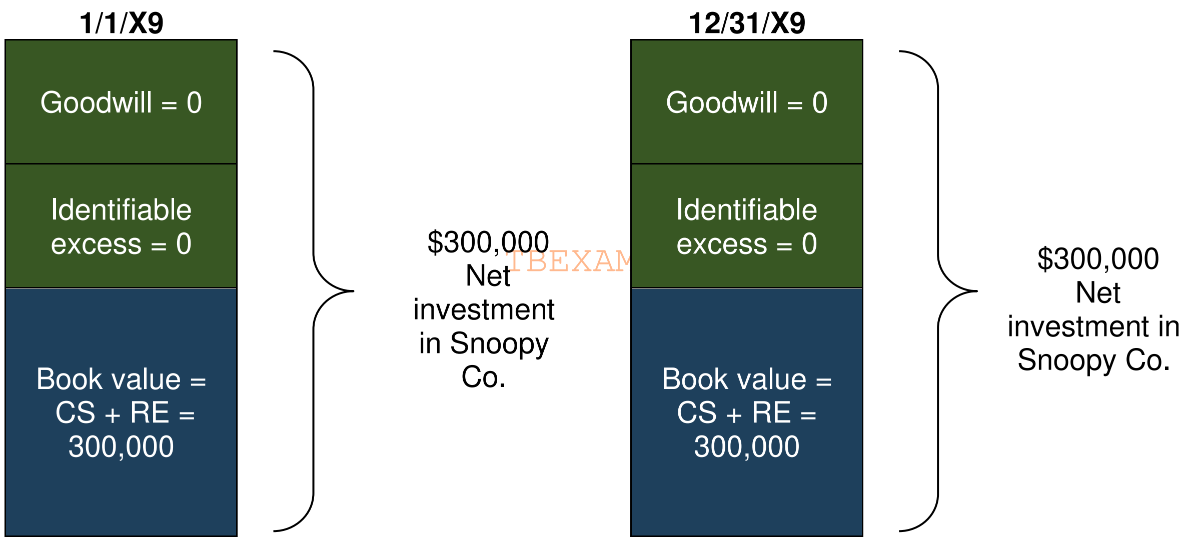
Cash	30,000	
Dividend Income		30,000

Record Peanut Co.'s 100% share of Snoopy Co.'s 20X9 dividend

b.

Book Value Calculations:

	Total Book Value	=	Common Stock	+	Retained Earnings
Original book value	300,000		200,000		100,000



P2-28B (continued)

Investment consolidation entry

Common stock	200,000	
Retained earnings	100,000	
Investment in Snoopy Co.		300,000

Dividend consolidation entry

Dividend income	30,000	
Dividends declared		30,000

Accumulated Depreciation Consolidation Entry

Accumulated depreciation	10,000	
Buildings & equipment		10,000

Note that this entry is carried forward from the previous year (see solution to P2-27B) again assuming that no sales or other disposals of Buildings and equipment took place during the year.

	Investment in Snoopy Co. (Dr)	Investment in Snoopy Co. (Cr)		Dividend Income (Dr)	Dividend Income (Cr)	
Acquisition Price	300,000					
					20,000	Dividends
Ending Balance	300,000				20,000	Ending Balance
		300,000	Basic	20,000		
	0				0	

P2-28B (continued)

	Peanut Co.	Snoopy Co.	Consolidation Entries DR	Consolidation Entries CR	Consolidated
Income Statement					
Sales	850,000	300,000			1,150,000
Less: COGS	(270,000)	(150,000)			(420,000)
Less: Depreciation Expense	(50,000)	(10,000)			(60,000)
Less: Other Expenses	(230,000)	(60,000)			(290,000)
Dividend Income	30,000		30,000		0
Net Income	**330,000**	**80,000**	**30,000**	**0**	**380,000**
Statement of Retained Earnings					
Beginning Balance	470,000	155,000	100,000		525,000
Net Income	**330,000**	**80,000**	**30,000**	**0**	380,000
Less: Dividends Declared	(225,000)	(30,000)		30,000	(225,000)
Ending Balance	**575,000**	**205,000**	**130,000**	**30,000**	**680,000**
Balance Sheet					
Cash	230,000	75,000			305,000
Accounts Receivable	190,000	80,000			270,000
Inventory	180,000	100,000			280,000
Investment in Snoopy Co.	300,000			300,000	0
Land	200,000	100,000			300,000
Buildings & Equipment	700,000	200,000		**10,000**	890,000
Less: Accumulated Depreciation	(500,000)	(30,000)	**10,000**		(520,000)
Total Assets	**1,300,000**	**525,000**	**10,000**	**310,000**	**1,525,000**
Accounts Payable	75,000	35,000			110,000
Bonds Payable	150,000	85,000			235,000
Common Stock	500,000	200,000	200,000		500,000
Retained Earnings	**575,000**	**205,000**	**130,000**	**30,000**	680,000
Total Liabilities & Equity	**1,300,000**	**525,000**	**330,000**	**30,000**	**1,525,000**