Appendix 1 Ex. 15–23

a. 2010
Jan. 2

Investments—Government Bonds	83,200*	
Cash		83,200

*1.04 × $80,000

b. 2010
Dec. 31

Interest Revenue	320*	
Investments—Government Bonds		320
To amortize premium on bond investment.		

Purchase price of bonds (1.04 × $80,000)	$83,200
Face amount of bonds	80,000
Premium on bond investment	$ 3,200

*Premium amortization: $3,200/10 years = $320

c. The market rate of interest was less than the coupon rate of the bond, thus making the bond attractive to the buyer. This causes the bond price to increase, causing a premium. The amortization of the premium reduces the interest revenue earned on the bond through the adjusting journal entry shown in part (b). Ultimately, the buyer earns the market rate of interest, regardless of the coupon rate.

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