1: (217) External Financial Statements

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1: (217) External Financial Statements

1: (10) Concepts of Financial Accounting

Study Unit 1: External Financial Statements | Subunit 1: Concepts of Financial Accounting

1) A primary objective of external financial reporting is

A. Direct measurement of the value of a business enterprise.

B. Provision of information that is useful to present and potential investors, creditors, and others in making rational financial decisions regarding the enterprise.

C. Establishment of rules for accruing liabilities.

D. Direct measurement of the enterprise's stock price.

2) The accounting measurement that is **not** consistent with the going concern concept is

A. Historical cost.

B. Realization.

C. The transaction approach.

D. Liquidation value.

3) An objective of financial reporting is

A. Providing information useful to investors, creditors, donors, and other users for decision making.

B. Assessing the adequacy of internal control.

C. Evaluating management results compared with standards.

D. Providing information on compliance with established procedures.

4) The financial statements included in the annual report to the shareholders are **least** useful to which one of the following?

A. Stockbrokers.

B. Bankers preparing to lend money.

C. Competing businesses.

D. Managers in charge of operating activities.

5) Which of the following is a **true** statement about the objective of general-purpose financial reporting?

A. Financial reporting is ordinarily focused on industries rather than individual entities.

B. The objective applies only to information that is useful for investment professionals.

C. Financial reporting directly measures management performance.

D. The information provided relates to the entity's economic resources and claims.

6) Which basis of accounting is most likely to provide the **best** assessment of an entity's past and future ability to generate net cash inflows?

A. Cash basis of accounting.

B. Modified cash basis of accounting.

C. Accrual basis of accounting.

D. Tax basis of accounting.

7) All of the following support the objective of financial reporting **except** providing information that

A. Is useful for making investment and credit decisions.

B. Helps management evaluate alternative projects.

C. Concerns enterprise resources and claims to those resources.

D. Helps investors and creditors predict future cash flows.

8) General purpose external financial reporting of a corporation focuses primarily on the needs of which of the following users?

A. Regulatory and taxing authorities.

B. Investors and creditors and their advisors.

C. The board of directors of the corporation.

D. The management of the corporation.

9) For financial reporting to be useful, it must

A. Be in accordance with generally accepted accounting principles.

B. Provide information useful for making business and investment decisions.

C. Be understandable to those who have a limited knowledge of business activities.

D. Directly measure the value of the entity being reported on.

10) What is the primary objective of financial reporting?

A. To provide economic information that is comprehensible to all users.

B. To provide management with an accurate evaluation of their financial performance.

C. To provide forecasts for future cash flows and financial performance.

D. To provide information that is useful for economic decision making.

1: (217) External Financial Statements

2: (29) Statement of Financial Position (Balance Sheet)

Study Unit 1: External Financial Statements | Subunit 2: Statement of Financial Position (Balance Sheet)

1) When classifying assets as current and noncurrent for reporting purposes,

A. The amounts at which current assets are carried and reported must reflect realizable cash values.

B. Prepayments for items such as insurance or rent are included in an “other assets” group rather than as current assets as they will ultimately be expensed.

C. The time period by which current assets are distinguished from noncurrent assets is determined by the seasonal nature of the business.

D. Assets are classified as current if they are reasonably expected to be realized in cash or consumed during the normal operating cycle.

2) A statement of financial position provides a basis for all of the following except

A. Computing rates of return.

B. Evaluating capital structure.

C. Assessing liquidity and financial flexibility.

D. Determining profitability and assessing past performance.

3) A statement of financial position is intended to help investors and creditors

A. Assess the amount, timing, and uncertainty of prospective net cash inflows of a firm.

B. Evaluate economic resources and obligations of a firm.

C. Evaluate economic performance of a firm.

D. Evaluate changes in the ownership equity of a firm.

4) A corporation uses a calendar year for financial and tax reporting purposes and has $100 million of mortgage bonds due on January 15, Year 2. By January 10, Year 2, the corporation intends to refinance this debt with new long-term mortgage bonds and has entered into a financing agreement that clearly demonstrates its ability to consummate the refinancing. This debt is to be

A. Classified as a current liability on the statement of financial position at December 31, Year 1.

B. Classified as a long-term liability on the statement of financial position at December 31, Year 1.

C. Retired as of December 31, Year 1.

D. Considered off-balance-sheet debt.

5) The primary purpose of the statement of financial position is to reflect

A. The fair value of the firm's assets at some moment in time.

B. The status of the firm's assets in case of forced liquidation of the firm.

C. The success of a company's operations for a given amount of time.

D. Items of value, debt, and net worth.

6) A statement of financial position allows investors to assess all of the following except the

A. Efficiency with which enterprise assets are used.

B. Liquidity and financial flexibility of the enterprise.

C. Capital structure of the enterprise.

D. Net realizable value of enterprise assets.

7) The accounting equation (Assets – Liabilities = Equity) reflects the

A. Entity point of view.

B. Fund theory.

C. Proprietary point of view.

D. Enterprise theory.

8) Long-term obligations that are or will become callable by the creditor because of the debtor's violation of a provision of the debt agreement at the balance sheet date should be classified as

A. Long-term liabilities.

B. Current liabilities unless the debtor goes bankrupt.

C. Current liabilities unless the creditor has waived the right to demand repayment for more than 1 year from the balance sheet date.

D. Contingent liabilities until the violation is corrected.

9) A manufacturer receives an advance payment for special-order goods that are to be manufactured and delivered within the next year. The advance payment should be reported in the manufacturer's current-year statement of financial position as a(n)

A. Current liability.

B. Noncurrent liability.

C. Contra asset amount.

D. Accrued revenue.

10) A company has outstanding accounts payable of $30,000 and a short-term construction loan in the amount of $100,000 at year end. The loan was refinanced through issuance of long-term bonds after year end but before issuance of financial statements. How should these liabilities be recorded in the balance sheet?

A. Noncurrent liabilities of $130,000.

B. Current liabilities of $130,000.

C. Current liabilities of $30,000, noncurrent liabilities of $100,000.

D. Current liabilities of $130,000, with required footnote disclosure of the refinancing of the loan.

11) Noncurrent debt should be included in the current section of the statement of financial position if

A. It is to be converted into common stock before maturity.

B. It matures within the year and will be retired through the use of current assets.

C. Management plans to refinance it within the year.

D. A bond retirement fund has been set up for use in its scheduled retirement during the next year.

12) A company has the following items recorded on its financial records:

Available-for-sale debt securities	$200,000
Prepaid expenses	400,000
Treasury stock	100,000

The total amount of the above items to be shown as assets on the statement of financial position is

A. $400,000

B. $500,000

C. $600,000

D. $700,000

13) A receivable classified as current on the statement of financial position is expected to be collected within

A. The current operating cycle.

B. 1 year.

C. The current operating cycle or 1 year, whichever is longer.

D. The current operating cycle or 1 year, whichever is shorter.

14) Current assets are reasonably expected to be realized in cash or sold or consumed during the normal operating cycle of the business. Current assets most likely include

A. Intangible assets.

B. Purchased goodwill.

C. Organizational costs.

D. Trading securities.

15) A corporation was incorporated on January 1, Year 6, with $500,000 from the issuance of stock and borrowed funds of $75,000. During the first year of operations, net income was $25,000. On December 15, the corporation paid a $2,000 cash dividend. No additional activities affected equity in Year 6. At December 31, Year 6, the corporation's liabilities had increased to $94,000. In the corporation's December 31, Year 6 balance sheet, total assets should be reported at

A. $598,000

B. $600,000

C. $617,000

D. $692,000

16) An entity had the following account balances at year end.

Sales	$452,000
Cash	23,400
Accounts payable	14,300
Rent expense	3,700
Accounts receivable	9,400
Cost of goods sold	214,000
Land	104,000
Unearned revenue	6,800
Gain on sale	17,500
Equipment	28,800
Inventories	2,200
Notes payable	67,000

What is the amount of total current assets reported on the balance sheet?

A. $35,000

B. $39,900

C. $59,300

D. $63,800

17) All of the following are limitations of the balance sheet except that

A. The balance sheet is prepared using management judgments and estimates.

B. Assets and liabilities are usually recorded at historical cost, which might differ significantly from current market value.

C. The balance sheet provides information on the liquidity and solvency of the company.

D. The balance sheet omits many items that cannot be recorded objectively but which have financial value to the company.

18) Which one of the following would not be classified as a current liability?

A. Security deposits received from renters for a one-year lease.

B. Rent for the current year received on January 2 of the current year.

C. Undistributed stock dividends.

D. Ten-year bonds sold 110 months ago.

19) A company received an invoice in January for the electricity used by its warehouse in December, and it recorded the expense in January. The company uses the accrual basis of accounting. What is the impact to the company's December financial statements?

A. Current liabilities were understated, and retained earnings were overstated.

B. Operating expenses were overstated, and retained earnings were overstated.

C. Cash and cash equivalents were overstated, and retained earnings were understated.

D. Accrued expenses were overstated, and retained earnings were understated.

20) A company has $100 million of debt that is due in March Year 3. In December Year 2, the company entered into a non-cancelable agreement with its lender to refinance the debt with the same interest rate, and the full principal is due in December Year 5. How should the debt be classified on the December Year 2 balance sheet of the company?

A. Classified as a current liability.

B. Classified as a long-term liability.

C. Considered as an off-balance-sheet liability.

D. Classified as a contingent liability.

21) Company A had the following financial items listed on its statement of financial position as of December 31, Year 1:

Cash	$ 20,000
Accounts receivable	45,000
Prepaid assets	10,250
Gross property, plant, and equipment (PPE)	300,000
Accumulated depreciation on PPE	25,750
Accounts payable	22,500
Notes payable	125,000
Unearned revenue	30,000

Assuming the only remaining accounts are equity accounts, what is Company A's total stockholders' equity on December 31, Year 1?

A. $197,750

B. $202,000

C. $172,000

D. $223,500

22) Which of the following defines equity as it relates to a business entity?

A. Net revenues.

B. Total revenues less total expenses.

C. Total assets and liabilities.

D. Total assets less total liabilities.

23) A company's year-end comparative statement of financial position reflects the following changes from the prior year: cash increased by $40,000, total liabilities increased by $32,000, and all other assets decreased by $65,000. Which of the following statements is correct regarding the current-year change in the company's stockholders' equity?

A. It increased by $25,000.

B. It increased by $105,000.

C. It decreased by $32,000.

D. It decreased by $57,000.

24) How would the proceeds received from the advance sale of nonrefundable tickets for a theatrical performance be reported in the seller's financial statements before the performance?

A. Revenue for the entire proceeds.

B. Revenue to the extent of related costs expended.

C. Unearned revenue to the extent of related costs expended.

D. Unearned revenue for the entire proceeds.

25) Which of the following statements is correct regarding deferred revenues recorded by a company that provides services to customers?

A. Deferred revenue is a liability until the service has been performed.

B. Deferred revenues represent revenues recognized but not yet received in cash.

C. Deferred revenues result from services that have been performed but have not been billed.

D. A deferred revenue on the books of one company is an accrued expense on the books of another company.

26) On Geo's April 30, Year 3, balance sheet, a note receivable was reported as a noncurrent asset, and its accrued interest for 10 months was reported as a current asset. Which of the following terms would fit Geo's note receivable?

A. Both principal and interest amounts are payable on June 30, Year 3 and Year 4.

B. Principal and interest are due December 31, Year 3.

C. Both principal and interest amounts are payable on December 31, Year 3 and Year 4.

D. Principal is due June 30, Year 4, and interest is due June 30, Year 3 and Year 4.

27) Clear Co. has the following selected account balances:

Cash (includes $10,000 in bond-sinking fund for long-term bond payable)	$50,000
Accounts receivable	20,000
Allowance for credit losses	5,000
Deposits received from customers	3,000
Merchandise inventory	7,000
Unearned rent	1,000
Investment in trading debt securities	2,000

What amount should Clear report as total current assets in its balance sheet?

A. $64,000

B. $67,000

C. $72,000

D. $74,000

28) Which of the following is a false statement about balance sheet disclosure of accounts receivable?

A. Accounts receivable should be identified on the balance sheet as pledged if they are used as security for a loan even though the loan is shown on the same balance sheet as a liability.

B. That portion of installment accounts receivable from customers which falls due more than 12 months from the balance sheet date usually would be excluded from current assets.

C. Allowances may be deducted from the gross amount of accounts receivable for credit losses and adjustments to be made in the future on accounts shown in the current balance sheet.

D. Trade receivables are best shown separately from nontrade receivables where amounts of each are material.

29) Current liabilities are best defined as those obligations

A. The liquidation of which will require the use of resources properly classifiable as current assets within the next operating cycle or 1 year, whichever is longer.

B. The liquidation of which will require the use of cash or increase current liabilities within the next operating cycle or 1 year, whichever is longer.

C. The liquidation of which is reasonably expected to require the use of current assets or the creation of other current liabilities within the next operating cycle or 1 year, whichever is longer.

D. Involving commitments made within the next operating cycle or 1 year, whichever is longer.

1: (217) External Financial Statements

3: (33) Income Statement and Statement of Comprehensive Income

Study Unit 1: External Financial Statements | Subunit 3: Income Statement and Statement of Comprehensive Income

1) The profit and loss statement of an entity includes the following information for the current fiscal year:

Sales	$160,000
Gross profit	48,000
Year-end finished goods inventory	58,300
Opening finished goods inventory	60,190

The cost of goods manufactured by the entity for the current fiscal year is

A. $46,110

B. $49,890

C. $110,110

D. $113,890

2) Which one of the following would be shown on a multiple-step income statement but **not** on a single-step income statement?

A. Loss from discontinued operations.

B. Gross profit.

C. Cost of goods sold.

D. Net income from continuing operations.

3) Given the following data for a company, what is the cost of goods sold?

Beginning inventory of finished goods	$100,000
Cost of goods manufactured	700,000
Ending inventory of finished goods	200,000
Beginning work-in-process inventory	300,000
Ending work-in-process inventory	50,000

A. $500,000

B. $600,000

C. $800,000

D. $950,000

4) The financial statement that provides a summary of the firm's operations for a period of time is the

A. Income statement.

B. Statement of financial position.

C. Statement of shareholders' equity.

D. Statement of retained earnings.

5) Comprehensive income is **best** defined as

A. Net income excluding extraordinary gains and losses.

B. The change in net assets for the period including contributions by owners and distributions to owners.

C. Total revenues minus total expenses.

D. The change in net assets for the period excluding owner transactions.

6) Because of inexact estimates of the service life and the residual value of a plant asset, a fully depreciated asset was sold in the current year at a material gain. This gain **most** likely should be reported

A. In the other revenues and gains section of the current income statement.

B. As part of sales revenue on the current income statement.

C. In the extraordinary item section of the current income statement.

D. As an adjustment to prior periods' depreciation on the statement of changes in equity.

7) Assume that employees confessed to a $500,000 inventory theft but are not able to make restitution. How should this material fraud be shown in the company's financial statements?

A. Classified as a loss and shown as a separate line item in the income statement.

B. Initially classified as an accounts receivable because the employees are responsible for the goods. Because they cannot pay, the loss would be recognized as a write-off of accounts receivable.

C. Included in cost of goods sold because the goods are not on hand, losses on inventory shrinkage are ordinary, and it would cause the least amount of attention.

D. Recorded directly to retained earnings because it is not an income-producing item.

8) An entity had the following opening and closing inventory balances during the current year:

	1/1	12/31
Finished goods	$ 90,000	$260,000
Raw materials	105,000	130,000
Work-in-progress	220,000	175,000

The following transactions and events occurred during the current year:

- $300,000 of raw materials were purchased, of which $20,000 were returned because of defects.
- $600,000 of direct labor costs were incurred.
- $750,000 of production overhead costs were incurred.

The cost of goods sold for the current year ended December 31 would be

A. $1,480,000

B. $1,500,000

C. $1,610,000

D. $1,650,000

9) If the beginning balance for May of the materials inventory account was $27,500, the ending balance for May is $28,750, and $128,900 of materials were used during the month, the materials purchased during the month cost

A. $101,400

B. $127,650

C. $130,150

D. $157,650

10) The following information was taken from last year's accounting records of a manufacturing company.

Inventory	January 1	December 31
Raw materials	$38,000	$ 45,000
Work-in-process	21,000	10,000
Finished goods	78,000	107,000
Other information		
Direct labor		$236,000
Shipping costs on outgoing orders		6,500
Factory rent		59,000
Factory depreciation		18,700
Advertising expense		24,900
Net purchases of raw materials		115,000
Corporate administrative salaries		178,000
Material handling costs		35,800

On the basis of this information, the company's cost of goods manufactured and cost of goods sold are

A. $460,500 and $489,500, respectively.

B. $468,500 and $439,500, respectively.

C. $468,500 and $470,900, respectively.

D. $646,500 and $617,500, respectively.

11) The following information pertains to a corporation's income statement for the 12 months just ended. The company has an effective income tax rate of 40%.

Discontinued operations	$(70,000)
Income from continuing operations (net of tax)	72,000
Cumulative effect of change in accounting principle	60,000

Net income for the year is

A. $36,000

B. $12,000

C. $8,000

D. $30,000

12) Which of the following are acceptable formats for reporting comprehensive income?

I. In one continuous financial statement

II. In a statement of changes in equity
III. In a separate statement of net income
IV. In two separate but consecutive financial statements

A. I and II only.

B. I, II, and III only.

V.

C. III and IV only.

D. I and IV only.

13) A company reports the following information as of December 31:

Sales revenue	$800,000
Cost of goods sold	600,000
Operating expenses	90,000
Unrealized holding gain on available-for-sale debt securities, net of tax	30,000

What amount should the company report as comprehensive income as of December 31?

A. $30,000

B. $110,000

C. $140,000

D. $200,000

14) All of the following are defined as elements of an income statement **except**

A. Expenses.

B. Shareholders' equity.

C. Gains and losses.

D. Revenues.

15) According to U.S. GAAP, where on the income statement should a multinational company report the loss from the disposal sale of a major operating unit?

A. Report the loss, pretax, in a separate section between income from continuing operations and net income.

B. Report the loss, net of tax, in a separate section between income from continuing operations and net income.

C. Report the loss, pretax, in a separate section between income from operations and income before income tax.

D. Report the loss, net of tax, in a separate section between income before tax and net income.

16) A company reported first quarter revenues of $10,000,000, gross profit margin of 25%, and operating income of 15%. To reduce overhead expenses, a consultant recommends that the company outsource some of its operating activities beginning with the second quarter. This recommendation is anticipated to reduce operating expenses by 20% without affecting sales volume. The company has an income tax rate of 35%. Assuming cost of sales remains at 75%, what is the impact on the income statement if the company implements the recommendation?

A. Gross profit will increase by 8.0%.

B. Operating income will increase by 8.7%.

C. Operating income will increase by $200,000.

D. Operating expenses will be reduced by $300,000.

17) A company incurred $200,000 of manufacturing cost during the month, with a beginning finished goods inventory of $20,000 and an ending finished goods inventory of $15,000. Assuming no work-in-process inventories, the company's cost of goods sold was

A. $220,000

B. $205,000

C. $200,000

D. $105,000

18) To comply with the matching principle, the cost of labor services of an employee who participates in the manufacturing of a product normally should be charged to the income statement in the period in which the

A. Work is performed.

B. Employee is paid.

C. Product is completed.

D. Product is sold.

19) An income statement could be used by an external investor for all of the following purposes **except** to

A. Analyze the company's performance compared to the budget.

B. Compare the company's results to those of its competitors.

C. Assess the risk of the company achieving future profitability.

D. Predict the company's future revenues.

20) During the month of October, a company purchased 1,000 units of inventory for $500 per unit and sold 900 of these units, which represented 10% of the company's annual sales budget in units. The company also incurred administrative costs of $300,000 during October. By applying the matching principle, the total amount of the company's expenses on its October income statement is

A. $750,000

B. $800,000

C. $810,000

D. $860,000

21) A company is preparing its financial statements in accordance with U.S. GAAP. Listed below are select financial data for the company.

Net income	$950,000
Depreciation	40,000
Investment by owners	60,000
Unrealized gain on available-for-sale securities	90,000
Foreign currency translation loss	20,000

What is the amount that would be reported as comprehensive income?

A. $970,000

B. $1,020,000

C. $1,060,000

D. $1,120,000

22) A company used $200,000 of direct materials during June. At June 30, direct materials inventory was $30,000 more than it was at June 1. What were direct materials purchases during June?

A. $30,000

B. $170,000

C. $200,000

D. $230,000

23) In a multiple-step income statement for a retail company, all of the following are included in the operating section **except**

A. Sales.

B. Cost of goods sold.

C. Dividend revenue.

D. Administrative and selling expenses.

24) The major distinction made between the multiple-step and single-step income statement formats is the separation of

A. Operating and nonoperating data.

B. Income tax expense and administrative expenses.

C. Cost of goods sold expense and administrative expenses.

D. The effect on income taxes due to extraordinary items and the effect on income taxes due to income before extraordinary items.

25) A partial listing of a company's accounts is presented below:

Revenues	$80,000
Operating expenses	50,000
Foreign currency translation adjustment gain, net of tax	4,000
Income tax expense	10,000

What amount should the company report as net income?

A. $20,000

B. $24,000

C. $30,000

D. $34,000