CMA

MCQ TEST BANK

PART 1

Financial Planning, Performance, & Analytics

VOLUME 1

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1: (217) External Financial Statements

- 1: (10) Concepts of Financial Accounting
- 2: (29) Statement of Financial Position (Balance Sheet)
- 3: (33) Income Statement and Statement of Comprehensive Income
- 4: (46) Statement of Changes in Equity and Equity Transactions
- 5: (69) Statement of Cash Flows
- 6: (30) Consolidation Accounting

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.

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

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

Answer (B) is **correct.**
According to the FASB's Conceptual Framework, the objectives of external financial reporting are to provide information that (1) is useful to present and potential investors, creditors, and others in making rational financial decisions regarding the enterprise; (2) helps those parties in assessing the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from sale, redemption, or maturity of securities or loans; and (3) concerns the economic resources of an enterprise, the claims thereto, and the effects of transactions, events, and circumstances that change its resources and claims thereto.

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.

Answer (D) is **correct.**
Financial accounting principles assume that a business entity is a going concern in the absence of evidence to the contrary. The concept justifies the use of depreciation and amortization schedules, and the recording of assets and liabilities using attributes other than liquidation value.

3) An objective of financial reporting is

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

Answer (A) is **correct.**
The objective is to report financial information that is useful in making decisions about providing resources to the reporting entity. Primary users of financial information are current or prospective investors and creditors who cannot obtain it directly. Their decisions depend on expected returns.

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.

Answer (D) is **correct.**
Accrual-basis amounts used in financial reporting are not useful to managers making day-to-day operating decisions. The practice of management accounting fulfills the needs of these users.

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.

Answer (D) is **correct.**
The information reported relates to the entity's economic resources and claims to them (financial position) and to changes in those 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.

Answer (C) is **correct.**
Accrual accounting reports the effects of transactions and other events and circumstances even if the resulting cash flows occur in a different period. The advantage of accrual accounting is that information about an entity's economic resources and claims and changes in them during a period

provides a better basis for assessing past and future performance than information solely about cash flows.

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.

Answer (B) is **correct.**
The role of general purpose external financial reporting is to provide information that is useful to current and potential investors and creditors, not merely to management.

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.

Answer (B) is **correct.**
The objective is to report financial information that is useful in making decisions about providing resources to the reporting entity. Primary users of financial information are current and potential investors and creditors who cannot obtain it directly.

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.

Answer (B) is **correct.**
The objective of general-purpose financial reporting is to report financial information that is useful in making decisions about providing resources to the reporting entity. This information must have the fundamental qualitative characteristics of relevance and faithful representation.

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.

Answer (D) is **correct.**
The overall objective is to report financial information that is useful to current and potential investors and creditors in making decisions about providing resources to an individual reporting entity.

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.

Answer (D) is **correct.**
For financial reporting purposes, current assets consist of cash and other assets or resources expected to be realized in cash, sold, or consumed during the longer of 1 year or the normal operating cycle of the business.

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

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.

Answer (D) is **correct.**
The statement of financial position, also known as the balance sheet, reports an entity's financial position at a moment in time. It is therefore not useful for assessing past performance for a period of time. A balance sheet can be used to help users assess liquidity, financial flexibility, and risk.

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.

Answer (B) is **correct.**
The statement of financial position, or balance sheet, provides

information about an entity's resource structure (assets) and financing structure (liabilities and equity) at a moment in time. According to the FASB's Conceptual Framework, the statement of financial position does not purport to show the value of a business, but it enables investors, creditors, and other users to make their own estimates of value. It helps users assess liquidity, financial flexibility, profitability, and risk.

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.

Answer (B) is **correct.**
Short-term obligations expected to be refinanced should be reported as current liabilities unless the firm both plans to refinance and has the ability to refinance the debt on a long-term basis. The ability to refinance on a long-term basis is evidenced by a post-balance-sheet date issuance of long-term debt or a financing arrangement that will clearly permit long-term refinancing.

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.

Answer (D) is **correct.**
The balance sheet presents three major financial accounting

elements: assets (items of value), liabilities (debts), and equity (net worth). According to the FASB's Conceptual Framework, assets are probable future economic benefits resulting from past transactions or events. Liabilities are probable future sacrifices of economic benefits arising from present obligations as a result of past transactions or events. Equity is the residual interest in the assets after deduction of liabilities.

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.

Answer (D) is **correct.**
Assets are usually measured at original historical cost in a statement of financial position, although some exceptions exist. For example, some short-term receivables are reported at their net realizable value. Thus, the statement of financial position cannot be relied upon to assess NRV.

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

A. Entity point of view.

B. Fund theory.

C. Proprietary point of view.

Answer (C) is **correct.**
The equation is based on the proprietary theory. Equity in an enterprise is what remains after the economic obligations of the enterprise are deducted from its economic resources.

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.

Answer (C) is **correct.**
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 normally are classified as current liabilities. However, the debt need not be reclassified if the violation will be cured within a specified grace period or if the creditor formally waives or subsequently loses the right to demand repayment for a period of more than a year from the balance sheet date (also, reclassification is not required if the debtor expects and has the ability to refinance the obligation on a long-term basis).

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.

Answer (A) is **correct.**
The entity has not substantially completed what it must do to be entitled to the benefits of the advance payment, and the

receipt of future economic benefits is not sufficiently certain to justify income recognition. Accordingly, the receipt of cash in anticipation of goods to be delivered or services to be performed must be recognized as a liability, usually called deferred (or unearned) revenue or deferred (or unearned) income. Because the manufacturer must deliver the goods within the next year, this liability is current.

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.

Answer (C) is **correct.**
Accounts payable are properly classified as current liabilities because they are for items entering into the operating cycle. Short-term debt that is refinanced by a post-balance-sheet-date issuance of long-term debt should be classified as noncurrent. (The ability to refinance on a long-term basis has been demonstrated.) Thus, the short-term construction loan is classified as noncurrent. Accordingly, the entity records current liabilities of $30,000 and 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.

Answer (B) is **correct.**
Current liabilities include those obligations that are expected to be satisfied by the (1) payment of cash, (2) use of current

assets other than cash, or (3) creation of new current liabilities within 1 year from the balance sheet date (or operating cycle, if longer).

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

Answer (C) is **correct.**
Available-for-sale debt securities (an investment) and prepaid expenses are assets, but treasury stock is an equity item. The

total of the assets reported is therefore $600,000 ($200,000 + $400,000).

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.

Answer (C) is **correct.**
Current assets are reasonably expected to be realized in cash, sold, or consumed during the normal operating cycle of the business or within 1 year, whichever is longer. The operating cycle is the time between the acquisition of materials or services and the final cash realization from the earning process.

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.

Answer (D) is **correct.**
Current assets include, in descending order of liquidity, cash and cash equivalents; certain individual trading, available-for-sale, and held-to-maturity debt securities; receivables; inventories; and prepaid expenses. Trading securities are expected to be sold in the near term, so they are likely to be classified as current.

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

Answer (C) is **correct.**
Total assets equal the sum of total liabilities and equity. Total liabilities were $94,000 at year end, and equity amounted to $523,000 ($500,000 from issuance of stock + $25,000 net income – $2,000 cash dividend). Total assets are therefore $617,000 ($523,000 + $94,000).

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

Answer (A) is **correct.**
The major categories of current assets are cash and cash equivalents, certain investments, receivables, inventories, and prepaid expenses. The entity's total current assets are $35,000 ($23,400 cash + $9,400 accounts receivable + $2,200 inventories).

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.

Answer (C) is **correct.**
The balance sheet provides information about economic resources and claims, which helps to evaluate liquidity, solvency, financing needs, and the probability of obtaining financing. This is an advantage of the balance sheet.

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.

Answer (C) is **correct.**
Current liabilities are those debts that must be paid during the upcoming year or current operating cycle, whichever period is longer. Examples include accounts payable, wages payable, prepaid rents received from tenants, security deposits from

tenants, and the current portion of long-term debt. Undistributed stock dividends are not liabilities because they are not to be paid in cash but are distributed as shares of stock. Undistributed stock dividends are merely reclassifications of different equity accounts and are not liabilities.

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.

Answer (A) is **correct.**
Failure to record an expense in December will result in current liabilities being understated. Also, retained earnings will be overstated due to the failure to record the expense.

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.

Answer (B) is **correct.**
Long-term liabilities are liabilities that are due in more than 12 months. After refinancing, the debt is due more than 12 months from December Year 2. Thus, the debt is 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

Answer (C) is **correct.**
According to the proprietary theory, assets equal liabilities plus stockholders' equity. Based on the given information, Company A's total assets are $349,500 ($20,000 + $45,000 + $10,250 + $300,000 – $25,750). Additionally, total liabilities