QUESTION 1

During January Year 3, Doe Corp. agreed to sell the assets and product line of its Hart division. The decision represents a major strategic shift for Doe and will have a significant effect on its operations and financial results. The sale was completed on January 15, Year 4, and resulted in a gain on disposal of $900,000. Hart's operating losses were $600,000 for Year 3 and $50,000 for the period January 1 through January 15, Year 4. Disregarding income taxes, what amount of net gain (loss) should be reported in Doe's comparative Year 4 and Year 3 income statements?

	Year 3	*Year 4*
A.	$0	$250,000
B.	$(600,000)	$850,000
C.	$250,000	$0
D.	$(650,000)	$900,000

Explanation

Choice "B" is correct. The Year 3 operating losses would be reported in the Year 3 income statement. The Year 4 operating losses and the gain on disposal would be netted and reported in the Year 4 income statement. Each amount would be reported in the period it occurred.

Choice "A" is incorrect. It reports the total projected gains and losses in Year 4 and nothing in Year 3. Each amount should be reported in the period it occurred.

Choice "C" is incorrect. It reports the total projected gains and losses in Year 3 and nothing in Year 4. Each amount should be reported in the period it occurred.

Choice "D" is incorrect. It reports the total projected losses in Year 3 and the gain in Year 4. Each amount should be reported in the period it occurred.

QUESTION 2

Which of the following items should be shown as a component of comprehensive income?

A. Deferred revenue.

B. Foreign-currency translation adjustment.

C. Additional capital contribution.

D. Dividend paid to a shareholder.

Explanation

Choice "B" is correct. Comprehensive income includes all components of net income and "other comprehensive income." A foreign currency translation adjustment will be included in other comprehensive income, and therefore comprehensive income.

Choice "A" is incorrect. Deferred revenue represents cash received prior to revenue being "earned." Because it represents a liability until it qualifies as earned, deferred revenue will have no effect on comprehensive income.

Choice "C" is incorrect. Additional capital contributions represent investments by owners and are therefore excluded from the calculation of comprehensive income.

Choice "D" is incorrect. Comprehensive income includes all changes in equity except those resulting from investments by owners and distributions to owners. A dividend paid to a shareholder is an owner transaction.

QUESTION 3

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 decreased by $57,000.

C. It decreased by $32,000.

D. It increased by $105,000.

Explanation

Choice "B" is correct. Assets = Liabilities + Stockholders' equity. If cash increased by $40,000 and other assets decreased by $65,000, the net change in assets is a decline of $25,000. Liabilities increased $32,000.
Setting up the equation to reflect the changes in each category, −$25,000 = $32,000 + SE.
SE = −$57,000.

Choice "A" is incorrect. Stockholders' equity could not have increased if assets decreased and liabilities increased.

Choice "C" is incorrect. Equity could only decrease by $32,000 if assets remained constant.

Choice "D" is incorrect. This answer choice assumes that other assets increased (instead of decreased) by $65,000 and that liabilities were unchanged.

QUESTION 4

The following costs were incurred by Griff Co., a manufacturer:

Accounting and legal fees	$25,000
Freight-in	175,000
Freight-out	160,000
Officers salaries	150,000
Insurance	85,000
Sales representatives salaries	215,000

What amount of these costs should be reported as general and administrative expenses?

A. $550,000

B. $260,000

C. $635,000

D. $810,000

Explanation

Choice "B" is correct. $260,000. The following costs should be reported as general and administrative expenses:

Accounting and legal fees	$ 25,000
Officers salaries	150,000
Insurance	85,000
Total "general and admin" expenses	**$260,000**

"Freight-in" is a part of "cost of goods sold."

"Freight-out" is a "selling" expense.

Sales representative salaries is a selling expense.

QUESTION 5

Envoy Co. manufactures and sells household products. Envoy experienced losses associated with its small appliance group. Operations and cash flows for this group can be clearly distinguished from the rest of Envoy's operations. Envoy plans to sell the small appliance group with its operations. What is the earliest point at which Envoy should report the small appliance group as a discontinued operation?

A. When Envoy receives an offer for the segment.

B. When Envoy classifies it as held for sale.

C. When Envoy first sells any of the assets of the segment.

D. When Envoy sells the majority of the assets of the segment.

Explanation

Choice "B" is correct. The earliest period that a component of an entity can be reported in discontinued operations is when the component meets the following "held for sale" criteria:

1. Management commits to a plan to sell the component.
2. The component is available for immediate sale in its present condition.
3. An active program to locate a buyer has been initiated.
4. The sale of the component is probable and the sale is expected to be completed within one year.
5. The sale of the component is being actively marketed.
6. It is unlikely that significant change to the plan to sell will be made or that the plan will be withdrawn.

Choices "A", "C", and "D" are incorrect, per the explanation above.

QUESTION 6

Reclassification adjustments must be shown in the financial statement that discloses comprehensive income:

A. To avoid including transactions with shareholders in items of comprehensive income.

B. To show what portion of comprehensive income is from the realization of current assets.

C. To avoid double counting in comprehensive income items, which are currently displayed in net income.

D. To show the tax effect of items of comprehensive income.

Explanation

Choice "C" is correct. Reclassification entries may be necessary to avoid double counting an item previously reported as comprehensive income (i.e., unrealized gain), which are now reported as part of net income (i.e., realized gain).

Choice "A" is incorrect. Transactions with shareholders such as paying dividends and issuing capital stock are not included in comprehensive income, thus, reclassification adjustments are not necessary to exclude them.

Choice "B" is incorrect. The classification of assets as current or non-current has no bearing on reporting comprehensive income.

Choice "D" is incorrect. All items of comprehensive income must be shown net of the related tax effects, but it is not done with reclassification adjustments.

QUESTION 7

Which of the following is *not* used in the calculation of comprehensive income?

- **A.** Unrealized gain on available-for-sale debt securities held at year-end.
- **B.** Realized losses on trading debt securities sold during the year.
- **C.** Gain on reissuance of treasury stock under the cost method.
- **D.** Losses from foreign currency translations.

Explanation

Choice "C" is correct. Comprehensive income includes all changes in equity during a period except those resulting from investments by owners or distributions to owners. Treasury stock transactions are owner transactions and are not part of comprehensive income.

Choice "A" is incorrect. Unrealized gains and losses on available-for debt sale securities are an item of other comprehensive income.

Choice "B" is incorrect. Realized gains and losses on any type of security are recognized in the income statement. Comprehensive income is net income plus other comprehensive income "PUFI" items.

Choice "D" is incorrect. Losses from foreign currency translations are an item of other comprehensive income.

QUESTION 8

Under U.S. GAAP, the effect of a material transaction that is infrequent in occurrence but not unusual in nature should be presented separately as a component of income from continuing operations when the transaction results in a:

	Gain	*Loss*
A.	Yes	No
B.	Yes	Yes
C.	No	No
D.	No	Yes

Explanation

Choice "B" is correct, Yes - Yes. Under U.S. GAAP, a material transaction that is "infrequent in occurrence" and/or "unusual in nature" should be presented separately as a component of "income from continuing operations" when the transaction results in a gain or loss.

QUESTION 9

Which of the following items would *not* be found in comprehensive income?

A. Nonmonetary exchanges of common stock for productive assets.

B. Recognition of prior service cost due to pension plan amendment.

C. Unrealized losses from changes in the value of available-for-sale debt securities.

D. Income from continuing operations.

Explanation

Choice "A" is correct. Comprehensive income includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. The exchange of common stock for productive assets represents a transaction with owners specifically excluded from comprehensive income.

Choice "B" is incorrect. The changes in the funded status of a pension plan due to the recognition of prior service cost from a plan amendment is included in other comprehensive income.

Choice "C" is incorrect. Unrealized gains and losses on available-for-sale debt securities are specifically included in other comprehensive income.

Choice "D" is incorrect. Income from continuing operations is included in comprehensive income. Generally comprehensive income is the sum of income from operations and other comprehensive income.

QUESTION 10

Which of the following items is *not* classified as "other comprehensive income?"

A. Minimum pension liability equity adjustment for a defined-benefit pension plan.

B. Gains from extinguishment of debt.

C. Unrealized gains for the year on available-for-sale debt securities.

D. Foreign currency translation adjustments.

Explanation

Choice "B" is correct. Gains from extinguishment of debt are a component of net income, not a component of other comprehensive income. Comprehensive income is the sum of net income plus other comprehensive income. Other comprehensive income include changes in the funded status of a pension plan, unrealized gains and losses on available-for-sale debt securities and derivative instruments designated as cash flow hedges, foreign currency items, and instrument-specific credit risk.

Choice "A" is incorrect. The minimum pension liability adjustment is no longer required under U.S. GAAP.

Choice "C" is incorrect. Unrealized gains (and losses) on available-for-sale debt securities are included in other comprehensive income.

Choice "D" is incorrect. Foreign currency translation adjustments are a component of other comprehensive income.

QUESTION 11

On October 1, 20X4, Host Co. approved a plan to dispose of one of the company's operating segments. The decision represents a major strategic shift for Host and will have a significant effect on its operations and financial results. Host expected that the sale would occur on April 1, 20X5 at an estimated gain of $350,000. The segment had actual and estimated operating losses as follows:

1/1/X4 to 9/30/X4	$(300,000)
10/1/X4 to 12/31/X4	(200,000)
1/1/X5 to 3/31/X5	(400,000)

In its 20X4 income statement, what should Host report as a loss from discontinued operations before income taxes?

A. $900,000

B. $550,000

C. $500,000

D. $200,000

Explanation

Choice "C" is correct. In its 20X4 income statement, Host would include in its loss from discontinued operations the 20X4 losses but not the projected 20X5 operating losses and not the projected gain on disposal. The 20X4 losses are $500,000 in total.

The projected 20X5 operating loss of $400,000 and the projected gain on disposal would be included in its 20X5 income statement.

Choice "A" is incorrect. It includes all of the projected operating losses in the 20X4 loss from discontinued operations. Each amount should be reported in the period it occurred.

Choice "B" is incorrect. It includes all of the projected operating losses and the projected gain in the 20X4 loss from discontinued operations. Each amount should be reported in the period it occurred.

Choice "D" is incorrect. It includes only a portion of the 20X4 operating losses in the 20X4 loss from discontinued operations. Each amount should be reported in the period it occurred, and the entire 20X4 operating loss, not just the portion that occurred after the decision date, would be included.

QUESTION 12

On November 1, Year 1, Smith Co. contracted to dispose of an industry segment. Throughout Year 1 the segment had operating losses. These losses were expected to continue until the segment's disposition. If a loss is projected on final disposition, how much of the operating losses should be included in the loss from discontinued operations reported in Smith's Year 1 income statement?

I. Operating losses for the period January 1 to October 31, Year 1.

II. Operating losses for the period November 1 to December 31, Year 1.

III. Estimated operating losses for the period January 1 to February 28, Year 2.

A. I and II only.

B. I and III only.

C. II and III only.

D. II only.

Explanation

Choice "A" is correct. The operating losses to be included in Smith's Year 1 income statement would be the total Year 1 operating losses, regardless of whether those losses occurred before or after the date the decision to dispose of the component was made, and not any Year 2 operating losses. Projected operating losses are not anticipated and accrued.

Choice "B" is incorrect. The operating losses to be included in Smith's Year 1 income statement would be the total Year 1 operating losses, regardless of whether those losses occurred before or after the date the decision to dispose of the component was made, and not any Year 2 operating losses.

Choice "C" is incorrect. The operating losses to be included in Smith's Year 1 income statement would be the total Year 1 operating losses, regardless of whether those losses occurred before or after the date the decision to dispose of the component was made, and not any Year 2 operating losses.

Choice "D" is incorrect. The operating losses to be included in Smith's Year 1 income statement would be the total Year 1 operating losses, regardless of whether those losses occurred before or after the date the decision to dispose of the component was made, and not any Year 2 operating losses.

QUESTION 13

For the fiscal year ended June 30, Year 1, Safety Toys Company reported after-tax income from continuing operations of $87,500,000 and income from discontinued operations of $5,650,000 (net of tax). There were no other items impacting the company's net earnings. Additionally, the company had a foreign currency translation gain of $1,100,000 (net of tax) and an $800,000 loss (net of tax) from a current amendment impacting Safety's prior service cost associated with its pension plan's funded status. Given the above and assuming that a $55,000 loss from a fair value hedge was included in reported income from continuing operations, what is the company's comprehensive income for the fiscal year ended June 30, Year 1?

- **A.** $91,300,000
- **B.** $87,800,000
- **C.** $93,450,000
- **D.** $94,195,000

Explanation

Choice "C" is correct. Comprehensive income is derived as follows:

Income from continuing operations	$ 87,500,000
Add:	
Income from discontinued operations	5,650,000
Net income	$ 93,150,000
Add other comprehensive income:	
Translation gain	1,100,000
Prior service cost loss	(800,000)
Total other comprehensive income	$300,000
Comprehensive income	$**93,450,000**

Choice "A" is incorrect. This answer choice incorrectly excludes income from discontinued operations when calculating comprehensive income.

Choice "B" is incorrect. While the other comprehensive income components were correctly determined, the calculation erroneously adds income from continuing operations to other comprehensive income to derive comprehensive income.

Choice "D" is incorrect. This answer choice does not include the prior service cost loss as a component of other comprehensive income and improperly includes the fair value hedge loss as a component of other comprehensive income even though this is also appropriately included in net income.

QUESTION 14

Which of the following statements is correct regarding the reporting of comprehensive income?

A. All companies must present a statement of comprehensive income.

B. The statement of comprehensive income can be shown as part of the footnotes only or as a separate financial statement.

C. Comprehensive income may be presented in a single financial statement that presents both net income and comprehensive income.

D. Other comprehensive income per share is presented in a statement of comprehensive income.

Explanation

Choice "C" is correct. Comprehensive income can be shown in one statement of comprehensive income which displays other comprehensive income items individually, and in total, below the net income amount, and totals them for comprehensive income. At the company's discretion, comprehensive income can also be shown as a separate statement that follows the income statement.

Choice "A" is incorrect. The requirement to present a statement of comprehensive income does not apply to a company that has no items of other comprehensive income.

Choice "B" is incorrect. Comprehensive income and its components are presented with the same prominence as the other financial statements that constitute a full set of financial statements. Comprehensive income cannot be shown as in the footnotes only.

Choice "D" is incorrect. Comprehensive income is not reported on a per share basis.

QUESTION 15

What is the purpose of reporting comprehensive income?

A. To summarize all changes in equity from nonowner sources.

B. To reconcile the difference between net income and cash flows provided from operating activities.

C. To provide a consolidation of the income of the firm's segments.

D. To provide information for each segment of the business.

Explanation

Choice "A" is correct. Comprehensive income represents all changes in stockholders' equity that come from nonowner sources. Therefore, comprehensive income includes all net income plus any and all components of other comprehensive income, the "PUFI" items. Comprehensive income would not include investments by stockholders (owners) nor would it include distributions or dividends to stockholders (owners).

Choices "B", "C", and "D" are incorrect per the explanation above.

QUESTION 15

A European company has made a purchase, which it intends to pay for in Japanese yen. Which of the following exchange rate movements will give rise to a loss for the company?

I.	The euro depreciating versus the yen
II.	The yen appreciating versus the euro
III.	When more euros are needed to purchase one yen
IV.	When more yen are needed to purchase one euro

A. III only.

B. I, II, and III.

C. IV only.

D. I, II, and IV

Explanation

Choice "B" is correct. Any situation in which the euro depreciates versus the yen will cause the European company to book a loss. The yen appreciating versus the euro and a situation in which more euros are needed to purchase one yen describe the euro depreciating versus the yen.

Choice "A" is incorrect. The euro depreciating versus the yen (and by the same token, the yen appreciating versus the euro) will cause a loss for the European company.

Choice "C" is incorrect. This is the only situation in which the European company will have a gain.

Choice "D" is incorrect. When more yen are needed to purchase one euro, this represents a situation in which the euro has appreciated versus the yen and the European company will book a gain rather than a loss.

QUESTION 16

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. $200,000

B. $30,000

C. $110,000

D. $140,000

Explanation

Choice "D" is correct. Comprehensive income is equal to current period net income plus current period other comprehensive income. Sales revenue, cost of goods sold and operating expense can be used to calculate net income:

Net income = Sales revenue - Cost of goods sold - Operating expenses

Net income = $800,000 - $600,000 - $90,000 = $110,000

The unrealized holding gain on available-for-sale debt securities is not a component of net income, but is included in other comprehensive income.

Total comprehensive income is calculated as follows:

Comprehensive income = Net income + Other comprehensive income

Comprehensive income = $110,000 + $30,000 = $140,000

Choice "A" is incorrect. Comprehensive income is not equal to the gross profit of $200,000 ($800,000 sales revenue - $600,000 cost of goods sold).