

Chapter 1—Financial accounting

Multiple choice

1. Which of the following statements is true regarding economic events?
- The signing of a service contract is an example of an external event that is recorded in the accounting records
 - Every event which affects an entity can be identified from a source document
 - All internal and external events must be measured with sufficient reliability.
 - External events involve exchanges between an entity and another entity outside the company

ANS: D PTS: 1 DIF: 2 OBJ: 1-1 NAT: | AACSB
Communication | APO-06-Recording Transactions

2. Which of the following underlying assumptions of the conceptual framework is the reason the dollar is used in the preparation of financial statements?
- Economic entity
 - Continuity
 - Time-period
 - Monetary unit

ANS: D PTS: 1 DIF: 1 OBJ: 1-1 NAT: | AACSB Communication |
APO-02-GAAP

3. Which of the following is an assumption made in the preparation of financial statements?
- Financial statements are prepared for a specific entity that is distinct from the entity's owners
 - The current market value is assumed to be less relevant than the original cost paid
 - The preparation of financial statements for a specific time period assumes that the balance sheet covers a designated period of time
 - Financial statements are prepared assuming that inflation has a distinct effect on the monetary unit

ANS: A PTS: 1 DIF: 2 OBJ: 1-1 NAT: | AACSB Communication |
APO-02-GAAP

4. The time period assumption is necessary because:
- inflation exists and causes confusing swings in financial statement amounts over time
 - business owners and interested parties want periodic measurements of the business' success or failure

- c. business owners and interested parties expect full disclosure of all economic events throughout the entire time period
- d. it is required by the federal government

ANS: B PTS: 1 DIF: 1 OBJ: 1-1 NAT: | AACSB Communication |
APO-02-GAAP

- 5.** The going concern assumption is concerned with:
- a. the company's ability to continue operations long enough to carry out its existing obligations
 - b. any information that is capable of influencing the decisions of anyone using the financial statements
 - c. measuring ongoing business activities at their exchange price at the time of the initial external transaction
 - d. offsetting management's natural optimism by providing a prudent approach to uncertainty in financial statement items

ANS: A PTS: 1 DIF: 2 OBJ: 1-1 NAT: | AACSB Communication |
APO-02-GAAP

- 6.** 'Revenues' are best described as:
- a. a decrease in resources resulting from the sale of goods or the provision of services
 - b. an increase in resources resulting from the sale of goods or the provision of services
 - c. assets used or consumed in the sale of products or services
 - d. an increase in the financing activities

ANS: B PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-02-GAAP

- 7.** 'Expenses' are best described as:
- a. an increase in resources resulting from the sale of goods or the provision of services
 - b. the amount of interest or claim that the owners have in the business
 - c. the future economic resources of a business entity
 - d. a decrease in resources resulting from the sale of goods or provision of services

ANS: D PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB Communication |
APO-02-GAAP

- 8.** Which statement demonstrates the financial success or failure of the company over that specific period of time?
- a. The statement of cash flows
 - b. The statement of changes in equity

- c. The balance sheet
- d. The income statement

ANS: D PTS: 1 DIF: 1 OBJ: 1-2 N NAT: |
AACSB Communication | APO-09-Financial statements

- 9.** The resources used to generate revenues during a period are called:
- a. Profit
 - b. Expenses
 - c. Revenues
 - d. Dividends

ANS: B PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB
Communication | APO-09-Financial statements

- 10.** Which of the following is the correct date format for the financial statement heading?
- a. Balance sheet for the Year Ended 30 June 2016
 - b. Income statement at 30 June 2016
 - c. Income statement for the Year Ended 30 June 2016
 - d. Statement of changes in equity at 30 June 2016

ANS: C PTS: 1 DIF: 3 OBJ: 1-2 NAT: | AACSB
Communication | APO-09-Financial statements

- 11.** Which of the following terms best describes a distribution of the profit of a company to its owners?
- a. Retained earnings
 - b. Dividends
 - c. Liquidation of assets
 - d. Monetary unit

ANS: B PTS: 1 DIF: 1 OBJ: 1-3 NAT: | AACSB
Communication | APO-09-Financial statements

- 12.** IPOD Corporations' end of year balance sheet consisted of the following amounts.

Cash	\$ 150 000	Accounts receivable	\$500 000
Property, plant and equipment	700 000	Long-term debt	400 000
Ordinary share	1 000 000	Accounts payable	200 000
Retained earnings	?	Inventory	350 000

What amount should IPOD report on its balance sheet for total assets?

- a. \$1 100 000
- b. \$1 550 000
- c. \$1 700 000

d. \$1 900 000

ANS: C PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB
Analytic | APO-09-Financial statements

13. IPOD Corporations' end of year balance sheet consisted of the following amounts.

Cash	\$150 000	Accounts receivable	\$500 000
Property, plant and equipment	700 000	Long-term debt	400 000
Ordinary share	1 000 000	Accounts payable	200 000
Retained earnings	?	Inventory	350 000

What is IPOD's retained earnings balance at the end of the current year?

- a. \$100 000
- b. \$1 100 000
- c. \$1 600 000
- d. \$1 700 000

ANS: A PTS: 1 DIF: 3 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

14. The Peck Company reported the following items on its financial statements for the year ending 30 June 2016.

Sales	\$1 560 000	Cost of sales	\$1 400 000
Selling, general and administrative expense	40 000	Other expense	30 000
Dividends	10 000	Income tax expense	25 000

The income statement for Peck will report profit for the current year in the amount of:

- a. \$ 45 000
- b. \$ 65 000
- c. \$ 85 000
- d. \$465 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB
Analytic | APO-09-Financial statements

15. The Peck Company reported the following items on its financial statements for the year ending 30 June 2016.

Sales	\$1 560 000	Cost of sales	\$1 400 000
Selling, general and administrative expense	40 000	Other expense	30 000
Dividends	10 000	Income tax expense	25 000

How much will be reported as retained earnings on its balance sheet at 30 June 2016, if this is the first year of operations?

- a. \$45 000
- b. \$55 000
- c. \$85 000
- d. Not enough information is provided.

ANS: B PTS: 1 DIF: 3 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

16. Ponzi Corporation reported the following information for the year ended 30 June 2016.

Profit	\$100 000
Dividends	6 000
Retained earnings at 30 June 2016	\$120 000

What was the balance of retained earnings at 1 July 2015?

- a. \$ 21 000
- b. \$ 26 000
- c. \$106 000
- d. \$214 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

17. Ponzi Corporation reported the following information for the year ended 30 June 2016.

Profit	\$100 000
Dividends	6 000
Retained earnings at 30 June 2016	\$120 000

What was the economic effect of the payment of Ponzi's dividends?

- a. The dividend reduced profit for 2016
- b. The dividend should be added to profit if the company's accounting equation is in balance
- c. The dividend reduced total retained earnings
- d. The dividends must be paid whenever Ponzi Corp. reports profit

ANS: C PTS: 1 DIF: 1 OBJ: 1-4 NAT: | AACSB
Communication | APO-09-Financial statements

- 18.** You are a potential creditor and are concerned that a particular company you are ready to give a loan to might have too much debt. Which financial statement would provide you with the information needed to evaluate your concern?
- a. The balance sheet
 - b. The income statement
 - c. The statement of changes in equity
 - d. The statement of public accounting

ANS: A PTS: 1 DIF: 2 OBJ: 1-3 NAT: |AACSB
Analytic | APO-09-Financial statements

- 19.** Which financial statement would you refer to in order to determine how many resources (assets) the company owned?
- a. The balance sheet
 - b. The statement of changes in equity
 - c. The income statement
 - d. The statement of public accounting

ANS: A PTS: 1 DIF: 2 OBJ: 1-3 NAT: |AACSB
Communication | APO-09-Financial statements

- 20.** Businesses engage in which of the following three main activity categories?
- a. Financing, investing, operating
 - b. Cash, credit, non-cash
 - c. Financing, credit, operating
 - d. Financing, management, operating

ANS: A PTS: 1 DIF: 1 OBJ: 1-5 NAT: |AACSB Communication |
APO-01-Purpose

- 21.** Which one of the following is not one of the three business activities?
- a. Financing
 - b. Operating
 - c. Investing
 - d. Measuring

ANS: D PTS: 1 DIF: 1 OBJ: 1-5 NAT: |AACSB Communication |
APO-01-Purpose

- 22.** Which financial statement would you analyse to determine its operating performance for the past year?
- a. The balance sheet
 - b. The statement of changes in equity
 - c. The income statement
 - d. The statement of public accounting

ANS: C PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Communication |
APO-09-Financial statements

23. Which one of the following financial statements shows the end of the year cash balance for a business entity?

- a. The income statement and the statement of changes in equity
- b. The balance sheet and the statement of cash flows
- c. The statement of changes in equity and the statement of cash flows
- d. The balance sheet and the statement of changes in equity

ANS: B PTS: 1 DIF: 3 OBJ: 1-3 | 1-5 NAT: | AACSB Analytic |
APO-09-Financial statements

24. Which one of the following involves a liability for a business?

- a. An obligation to pay for goods purchased on credit from a supplier
- b. Inventories purchased for cash
- c. Amounts invested by the owners
- d. Shares sold to the general public

ANS: A PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB Analytic |
APO-02-GAAP

25. Which one of the following is a correct fundamental accounting equation?

- a. $\text{Assets} + \text{Liabilities} = \text{Equity}$
- b. $\text{Assets} + \text{Retained Earnings} = \text{Equity}$
- c. $\text{Assets} + \text{Equity} = \text{Liabilities}$
- d. $\text{Assets} = \text{Liabilities} + \text{Equity}$

ANS: D PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB
Communication | APO-09-Financial statements

26. How is the balance sheet linked to the other financial statements?

- a. The amount of retained earnings is reported on the balance sheet as a liability
- b. Retained earnings are added to total assets and reported on the balance sheet
- c. Retained earnings are reported on the balance sheet
- d. There is no link between the balance sheet and other statements, as each contains different accounts and provides different information

ANS: C PTS: 1 DIF: 3 OBJ: 1-4 NAT: | AACSB
Communication | APO-09-Financial statements

27. On 1 July 2015, Blackstone Company reported assets of \$1 000 000 and liabilities of \$600 000. During 2016 assets decreased by \$200 000 and equity decreased \$250 000. What is the amount of equity at 30 June 2016?

- a. \$650 000
- b. \$150 000
- c. \$400 000
- d. \$800 000

	<u>Assets</u>		<u>Liabilities</u>		<u>Equity</u>
1 Jan. 2016	\$1 000 000	=	\$600 000	+	\$400 000
During 2016	200 000	=	50 000	+	-250 000
31 Jan. 2016	800 000	=	650 000	+	150 000

ANS: B PTS: 1 DIF: 3 OBJ: 1-3 NAT: | AACSB Analytic |
APO-09-Financial statements

- 28.** Which of the following best describes the term 'retained earnings'?
- a. The amount of total profits earned by a company since it began operations
 - b. The amount of claim that the owners have on the assets of the company
 - c. The future economic resources of a company
 - d. The accumulated profit of a company that has not been distributed to owners in the form of dividends

ANS: D PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB
Communication | APO-09-Financial statements

- 29.** Which one of the following items appears on a balance sheet?
- a. Retained earnings
 - b. Sales revenue
 - c. Electricity expense
 - d. Dividends

ANS: A PTS: 1 DIF: 1 OBJ: 1-3 NAT: | AACSB
Communication | APO-09-Financial statements

- 30.** Which of the following is an organisation that lends funds to a business entity and expects repayment of the funds?
- a. A partner
 - b. A shareholder
 - c. An owner
 - d. A creditor

ANS: D PTS: 1 DIF: 1 OBJ: 1-3 NAT: | AACSB
Communication | APO-01-Purpose

- 31.** Which of the following invests funds into a business and is considered an owner?
- a. Shareholders
 - b. Creditors
 - c. Bankers

d. Lenders

ANS: A PTS: 1 DIF: 1 OBJ: 1-3 NAT: | AACSB
Communication | APO-01-Purpose

32. Which one of the following financial statements reports an entity's financial position at a specific date?

- a. The balance sheet
- b. The statement of changes in equity
- c. The income statement
- d. Both the income statement and the balance sheet

ANS: A PTS: 1 DIF: 1 OBJ: 1-3 NAT: | AACSB
Communication | APO-09-Financial statements

33. Bailout Corp. reported the following information for the year ended 30 June 2016.

Revenues	\$2 500 000
Expenses	2 000 000
Retained earnings at 30 June 2015	100 000
Retained earnings at 30 June 2016	450 000

How much was paid out in dividends in 2016?

- a. \$500 000
- b. \$150 000
- c. \$350 000
- d. \$250 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

34. Jetson Corp. reported the following information for the year ended 30 June 2016.

Revenue	\$14 000 000
Expenses	11 500 000
Dividends	1 000 000
Retained earnings at 30 June 2016	1 750 000

What was the retained earnings balance at 30 June, 2015?

- a. \$ 250 000
- b. \$2 500 000
- c. \$1 500 000
- d. \$ 350 000

ANS: A PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

35. On 1 July 2015, Money Company's balance in retained earnings was \$10 000 000. At the end of the year, 30 June 2016, the balance in retained earnings was \$9 400 000. During 2016, the company earned profit of \$440 000. How much were dividends?

- a. \$1 040 000
- b. \$1 000 000
- c. \$ 600 000
- d. \$ 440 000

ANS: A PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

36. Refer to the following information for Tarp Corporation.

Beginning retained earnings	\$550 000
Ending retained earnings	700 000
Dividends paid	100 000
Revenue	525 000

What is the profit for Tarp Corp.?

- a. \$150 000
- b. \$250 000
- c. \$300 000
- d. \$350 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

37. Refer to the following information for Tarp Corporation.

Beginning retained earnings	\$550 000
Ending retained earnings	700 000
Dividends paid	100 000
Revenue	525 000

The company's expenses are:

- a. \$100 000
- b. \$150 000
- c. \$450 000
- d. \$275 000

ANS: D PTS: 1 DIF: 2 OBJ: 1-2 | 1-4 NAT: |
AACSB Analytic | APO-09-Financial statements

- 38.** If a company has \$10 500 000 of revenues, declares and pays \$550 000 in dividends, and has profit of \$1 600 000, how much were expenses for the year?
- a. \$9 950 000
 - b. \$1 050 000
 - c. \$2 150 000
 - d. \$8 900 000

ANS: D PTS: 1 DIF: 2 OBJ: 1-5 | 1-6 NAT: |
AACSB Analytic | APO-09-Financial statements

- 39.** Ranger Company has assets of \$5 000 000, liabilities of \$3 000 000, and retained earnings of \$1 200 000. How much is total equity?
- a. \$ 800 000
 - b. \$2 000 000
 - c. \$3 800 000
 - d. \$1 800 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB
Analytic | APO-09-Financial statements

- 40.** Doughty's Pet Shop reported a net loss of \$1 500 000 and total expenses of \$2 900 000. How much are total sales?
- a. \$4 400 000
 - b. \$1 400 000
 - c. \$2 400 000
 - d. \$1 600 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB
Analytic | APO-09-Financial statements

- 41.** 'Economic resources' are known as:
- a. Assets
 - b. Liabilities and shareholders' equity
 - c. Owners' equity and shareholders' equity
 - d. Retained earnings and revenues

ANS: A PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB
Communication | APO-09-Financial statements

- 42.** The income statement shows:
- a. how much profit the company has earned since it began operations
 - b. profit equal to the amount of cash on the balance sheet
 - c. a summary of the results of operations for a period of time
 - d. the liquidity of the company on an annual basis

ANS: C PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB

Communication | APO-09-Financial statements

43. Which one of the following equations represents the statement of changes in equity activity?

- a. Beginning retained earnings + profit + dividends = ending retained earnings
- b. Beginning retained earnings + cash inflows – cash outflows = ending retained earnings
- c. Beginning retained earnings + dividends – profit = ending retained earnings
- d. Beginning retained earnings + profit – dividends = ending retained earnings

ANS: D PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB

Communication | APO-09-Financial statements

44. Davis Construction began operation on 1 July 2015, with an initial investment of \$100 000 from each of its three shareholders. During the year ending 30 June 2016 Davis Construction had profit of \$125 000 and paid dividends of \$50 000.

Calculate its retained earnings balance at 30 June 2016.

- a. \$175 000
- b. \$ 75 000
- c. \$250 000
- d. \$375 000

ANS: B PTS: 1 DIF: 2 OBJ: 1-4 NAT: | AACSB

Analytic | APO-09-Financial statements

45. Davis Construction began operation on 1 July 2015, with an initial investment of \$100 000 from each of its three shareholders. During the year ending 30 June 2016 Davis Construction had profit of \$125 000 and paid dividends of \$50 000.

The dividends for the year:

- a. increase the amount of ordinary share reported by the company
- b. are part of Davis Construction's operating expense
- c. are reported on the statement of changes in equity
- d. are reported on the income statement.

ANS: C PTS: 1 DIF: 1 OBJ: 1-4 NAT: | AACSB

Communication | APO-09-Financial statements

46. Davis Construction began operation on 1 July 2015, with an initial investment of \$100 000 from each of its three shareholders. During the year ending 30 June 2016 Davis Construction had profit of \$125 000 and paid dividends of \$50 000.

If Davis Construction's revenues were \$500 000 for the year ended 30 June 2016, how much were total expenses?

- a. \$300 000

- b. \$375 000
- c. \$325 000
- d. \$625 000

ANS: B PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB
Analytic | APO-09-Financial statements

47. Which one of the following is not one of the activities on the statement of cash flows?

- a. Operating activities
- b. Investing activities
- c. Business activities
- d. Financing activities

ANS: C PTS: 1 DIF: 1 OBJ: 1-5 NAT: | AACSB
Communication | APO-09-Financial statements

48. Which of the following best describes a company's operating activities?

- a. Operating activities are cash flows directly related to earning income
- b. Operating activities are necessary to provide the money to start a business
- c. Operating activities are needed to provide the valuable assets required to run a business
- d. Operating activities represent the right to receive a benefit in the future

ANS: A PTS: 1 DIF: 1 OBJ: 1-5 NAT: | AACSB
Communication | APO-24-Statement of Cash Flows

49. In order for accounting information to be useful in making informed decisions, it must be

- a. internal
- b. relevant
- c. reliable
- d. both relevant and reliable

ANS: D PTS: 1 DIF: 1 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

50. Which of the following is a constraint to the qualitative characteristics of useful accounting information?

- a. Conservatism
- b. Materiality
- c. Relevance
- d. Comparability

ANS: B PTS: 1 DIF: 2 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

- 51.** The principle of conservatism is concerned with the:
- a. avoidance of overstating assets or income in the preparation of financial statements
 - b. minimisation of costs associated with providing financial information
 - c. company's ability to carry out its existing commitments
 - d. company's procedures for recording activities at their initial exchange price

ANS: A PTS: 1 DIF: 1 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

- 52.** Mullins manufactures furniture. Mullins has given you its most recent annual report in an effort to obtain a sizeable loan. The company is very profitable and appears to have a strong financial position. However, based on a news report you saw on television last night, you are aware that Mullins is a defendant in a class action lawsuit related to defective products. Serious injuries were allegedly caused by Mullins' infant high chairs overturning. The television news report is an example of financial information that is:
- a. predictable
 - b. conservative
 - c. relevant
 - d. comparable

ANS: C PTS: 1 DIF: 3 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

- 53.** If an investor can use accounting information for two different companies to evaluate the types and amounts of expenses, the information is said to have the quality of:
- a. comparability
 - b. consistency
 - c. neutrality
 - d. materiality

ANS: A PTS: 1 DIF: 2 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

- 54.** PTG Enterprises purchases many small pieces of office furniture, such as rubbish bins, that cost less than \$100 each. PTG accounts for these items as expenses when acquired rather than reporting them as property, plant and equipment on its balance sheet. The company's accountant states that no accounting principle has been violated. Justification for PTG's policy of expensing these furniture items is based on cost vs. benefit considerations as well as the accounting constraint of:
- a. conservatism
 - b. materiality
 - c. neutrality

d. verifiability

ANS: B PTS: 1 DIF: 2 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

55. Scott Brothers follow the qualitative characteristic of consistency. This means that:

- a. for expenses, Scott Brothers use the same account names as used by its competitors
- b. Scott Brothers have elected certain accounting principles that can never be changed
- c. Scott Brothers apply the same accounting principles each period
- d. Scott Brothers apply the same accounting principles as its competitors

ANS: C PTS: 1 DIF: 1 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

56. Information that is material means that an error in recording the dollar amount of a transaction would:

- a. likely affect the judgement of someone relying on the financial statements
- b. not affect the decisions of financial statement users
- c. not impact a business decision of a creditor
- d. result in the overstatement of assets or income

ANS: A PTS: 1 DIF: 2 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

57. An accountant is uncertain about the best estimate of an amount for a business transaction. If there are two possible amounts that could be recorded, the amount least likely to overstate assets and earnings is selected. Which of the following qualities is characterised by this action?

- a. Comparability
- b. Conservatism
- c. Materiality
- d. Neutrality

ANS: B PTS: 1 DIF: 2 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

58. The qualitative characteristics of accounting information include:

- a. reliability
- b. cash flow information
- c. all accounting information
- d. assets reported on the balance sheet

ANS: A PTS: 1 DIF: 1 OBJ: 1-6 | 1-7 NAT: | AACSB
Communication | APO-02-GAAP

59. If shareholders want to know how money flowed into and out of the company, what financial statement would they use?

- a. The income statement
- b. The statement of cash flows
- c. The balance sheet
- d. None of the options given

ANS: B PTS: 1 DIF: 1 OBJ: 1-5 NAT: AACSB Analytic |
APO-09-Financial statements

60. The assets and liabilities of the company are \$175 000 and \$40 000, respectively. Equity should equal:

- a. \$215 000
- b. \$135 000
- c. \$175 000
- d. \$40 000

ANS: B PTS: 1 DIF: 1 OBJ: 1-3 NAT: AACSB
Analytic | APO-15-Current Assets

61. Four financial statements are usually prepared for a business. The statement of cash flows is usually prepared last. The retained earnings statement (RE), the balance sheet (B), and the income statement (I) are prepared in a certain order to obtain information needed for the next statement. In what order are these three statements prepared?

- a. I, RE, B
- b. B, I, RE
- c. RE, I, B
- d. B, RE, I

ANS: A PTS: 1 DIF: 1 OBJ: 1-4 NAT: AACSB
Analytic | APO-09-Financial statements

62. Liabilities are reported on the:

- a. income statement
- b. retained earnings statement
- c. statement of cash flows
- d. balance sheet

ANS: D PTS: 1 DIF: 1 OBJ: 1-3 NAT: AACSB
Analytic | APO-16-Current Liabilities

63. Expenses can be matched against revenue:

- a. if the earnings process is not complete
- b. when cash is collected from the sale of products

- c. in the same period as the revenue that it helped to generate
- d. when payment is made for costs related to revenue

ANS: C PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB
Communication | APO-09-Financial statements

64. What does the phrase, 'revenue is recognised when earned' mean?

- a. Revenue is recorded in the accounting records when the goods are received from a supplier, and reported on the income statement when sold to the customer
- b. Revenue is recorded in the accounting records and reported on the income statement when the cash is received from the customer
- c. Revenue is recorded in the accounting records when the goods are sold to a customer, and reported on the income statement when the cash payment is received from the customer
- d. Revenue is recorded in the accounting records and reported on the income statement when goods are sold and delivered to a customer

ANS: D PTS: 1 DIF: 3 OBJ: 1-2 NAT: | AACSB
Communication | APO-09-Financial statements

65. Which of the following concepts relates to separating the reporting of business and personal economic transactions?

- a. Cost principle
- b. Monetary unit assumption
- c. Economic entity assumption
- d. Objectivity assumption

ANS: C PTS: 1 DIF: 1 OBJ: 1-1 NAT: AACSB
Analytic | APO-02-GAAP

66. Which of the following is not an asset?

- a. Investments
- b. Cash
- c. Inventory
- d. Equity

ANS: D PTS: 1 DIF: 1 OBJ: 1-3 NAT: AACSB
Analytic | APO-15-Current Assets

67. Cash investments made by shareholders in exchange for ordinary shares in a business are reported on the statement of cash flows in the:

- a. financing activities section
- b. investing activities section
- c. operating activities section
- d. supplemental statement

ANS: A PTS: 1 DIF: 1 OBJ: 1-5 NAT: AACSB Analytic |
APO-24-Statement of Cash Flows

68. A 'Matching principle' is best described as:

- a. The principle that revenue should be recorded when a resource has been earned.
- b. An increase in resources resulting from the sale of goods or the provision of services
- c. The principle that expenses should be recorded in the period resources are used to generate revenues.
- d. An increase in financing activities

ANS: C PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-02-GAAP

69. Which one of the following is a correct basic structure of the cash flow statement?

- a. Cash Flows Provided (Used) by Operating Activities + / - Cash Flows Provided (Used) by Business Activities + / - Cash Flows Provided (Used) by Financing Activities = Net Increase (Decrease) in Cash
- b. Cash Flows Provided (Used) by Operating Activities + / - Cash Flows Provided (Used) by Investing Activities + / - Cash Flows Provided (Used) by Business Activities = Net Increase (Decrease) in Cash
- c. Cash Flows Provided (Used) by Operating Activities + / - Cash Flows Provided (Used) by Financing Activities + / - Net Change in Working Capital = Net Increase (Decrease) in Cash
- d. Cash Flows Provided (Used) by Operating Activities + / - Cash Flows Provided (Used) by Investing Activities + / - Cash Flows Provided (Used) by Financing Activities = Net Increase (Decrease) in Cash

ANS: D PTS: 1 DIF: 1 OBJ: 1-5 NAT: | AACSB Communication |
APO-09-Financial statements

70. Monaco Lawn Service Co. used \$250 of fuel to mow customer lawns in June. The fuel was purchased on account and due in July. Fuel expense should be recorded in:

- a. July
- b. June
- c. May
- d. None of the options given

ANS: B PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-02-GAAP

71. Monaco Lawn Service Co. creates a revenue each time a lawn is:

- a. scheduled for service

- b. paid in full
- c. mowed
- d. prepaid in advance

ANS: C PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-02-GAAP

72. Monaco Lawn Service Co. reports cash received from customers for mowing their lawns on the statement of cash flows in the:

- a. financing activities section
- b. investing activities section
- c. operating activities section
- d. supplemental statement

ANS: C PTS: 1 DIF: 1 OBJ: 1-5 NAT: AACSB Analytic |
APO-24-Statement of Cash Flows

73. Cash used to purchase a truck to transport lawn mowers and other tools to customer locations is reported on the statement of cash flows in the:

- a. financing activities section
- b. investing activities section
- c. operating activities section
- d. supplemental statement

ANS: B PTS: 1 DIF: 1 OBJ: 1-5 NAT: AACSB Analytic |
APO-24-Statement of Cash Flows

Completion

1. The type of business activity that relates to obtaining funds from either issuing shares or borrowing money is called _____.

ANS: financing

PTS: 1 DIF: 1 OBJ: 1-5 NAT: | AACSB Communication | APO-01-Purpose

2. The names of the four basic financial statements are the income statement, statement of _____, statement of changes in equity and statement of cash _____.

ANS: financial, position, flows

PTS: 1 DIF: 1 OBJ: 1-2 | 1-3 | 1-4 | 1-5 NAT: | AACSB Communication |
APO-09-Financial statements

3. The fundamental accounting equation is _____ = _____ + _____.

ANS: assets, liabilities, equity

PTS: 1 DIF: 1 OBJ: 1-3 NAT: | AACSB Communication | APO-09-Financial statements

4. The financial statement in which you list revenues, starting with sales revenue (service revenue), is called the _____.

ANS: income statement

PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB Communication | APO-02-GAAP

5. Both profit and dividends can be found on the statement of _____.

ANS: changes in equity

PTS: 1 DIF: 1 OBJ: 1-4 NAT: | AACSB Communication | APO-02-GAAP

6. Profit from the income statement increases _____.

ANS: retained earnings

PTS: 1 DIF: 1 OBJ: 1-4 NAT: | AACSB Communication | APO-02-GAAP

7. The statement of cash flows classifies cash flow into these three categories: _____, _____ and _____.

ANS: operating, investing, financing

PTS: 1 DIF: 1 OBJ: 1-5 NAT: | AACSB Communication | APO-09-Financial statements

8. The three financial statements in which profit can be found are the _____ statement, statement of _____ and the statement of _____ using the indirect method.

ANS: income; changes in equity; cash flows

PTS: 1 DIF: 1 OBJ: 1-2 | 1-4 | 1-5 NAT: | AACSB Communication |
APO-09-Financial statements

Problem

1. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Determine the total assets at the end of the 2016 financial year.

ANS:\$1 247 000 PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB Analytic |
APO-09-Financial statements

2. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Determine the total liabilities at the end of 2016 financial year.

ANS:\$540 000 PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB Analytic |
APO-09-Financial statements

3. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000

Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Determine the total equity at the end of 2016 financial year

ANS:\$707 000 PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB Analytic |
APO-09-Financial statements

4. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Determine the total revenues for 2016 financial year.

ANS:\$1 005 000 PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-09-Financial statements

5. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Determine the total expenses for 2016 financial year.

ANS:\$905 000 PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-09-Financial statements

6. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Determine the profit for the financial year ended 30 June 2016.

ANS:\$100 000 PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-09-Financial statements

7. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Using good form, prepare an income statement for Times Corporation.

ANS:

Times Corporation
Income Statement
For the year ended 30 June 2016

Revenues:			
Sales revenue	\$955 000		
Interest income	<u>50 000</u>	\$1 005 000	
Expenses:			
Cost of sales	\$700 000		
Salary expense	140 000		
Selling expense	45 000		
Income tax expense	<u>20 000</u>	<u>905 000</u>	
Profit		<u>\$100 000</u>	

PTS: 1 DIF: 2 OBJ: 1-2 NAT: | AACSB Analytic |
APO-09-Financial statements

8. The accountant for the Times Corporation prepared the following list from the company's accounting records for the year ended 30 June 2016.

Retained earnings	?	Prepaid expenses	\$ 50 000
Cash	\$ 77 000	Ordinary share	400 000
Accounts payable	50 000	Accounts receivable	170 000
Sales revenue	955 000	Interest income	50 000
Cost of sales	700 000	Salary expense	140 000
Land	750 000	Income tax expense	20 000
Notes payable	450 000	Selling expense	45 000
Inventory	200 000	Salaries payable	40 000

Using good form, prepare a balance sheet for the Times Corporation.

ANS:

Times Corporation Balance Sheet As of 30 June 2016			
<u>Assets</u>		<u>Liabilities and equity</u>	
Cash	\$ 77 000	Accounts payable	\$ 50 000
Accounts receivable	170 000	Salaries payable	40 000
Inventory	200 000	Notes payable	450 000
Prepaid expenses	50 000	Ordinary share	400 000
Land	750 000	Retained earnings	307 000
Total assets	<u>\$1 247 000</u>	Total liabilities and equity	<u>\$1 247 000</u>

PTS: 1 DIF: 2 OBJ: 1-3 NAT: | AACSB Analytic |
APO-09-Financial statements

9. President Company started business at the beginning of the year, with assets of \$1 000 000 and equity of \$565 000. By the end of the year, assets increased by \$100 000 and liabilities decreased by \$150 000. Other than profit or loss, the only change in equity was dividends of \$50 000.

What was the amount of President Company equity at the end of the year?

ANS:

<u>Assets</u>			<u>Liabilities</u>	<u>Shareholders' equity</u>
Beginning of year	\$1 000 000		\$435 000	\$565 000
Change during year	+100 000		-150 000	+250 000
End of year	\$1 100 000	=	285 000	\$815 000

PTS: 1 DIF: 3 OBJ: 1-4 NAT: | AACSB Analytic |

APO-09-Financial statements

- 10.** President Company started business at the beginning of the year, with assets of \$1 000 000 and equity of \$565 000. By the end of the year, assets increased by \$100 000 and liabilities decreased by \$150 000. Other than profit or loss, the only change in equity was dividends of \$50 000.

What was the amount of President Company profit or net loss for the year?

ANS:

Change in equity	\$ 250 000
Add: dividends	<u>50 000</u>
Profit	<u>\$ 300 000</u>

PTS: 1 DIF: 3 OBJ: 1-4 NAT: | AACSB Analytic |
APO-09-Financial statements

- 11.** The following information comes from the records of America Corporation:

	<u>Assets</u>	<u>Liabilities</u>	<u>Equity</u>
1 July 2016	\$1 500 000	\$540 000	\$ <u> </u>
30 June 2017	1 810 000	<u> </u>	1 400 000

What is the amount of Equity at 1 July 2016?

ANS:\$960 000 PTS: 1 DIF: 2 OBJ: 1-2 | 1-3|1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

- 12.** The following information comes from the records of America Corporation:

	<u>Assets</u>	<u>Liabilities</u>	<u>Equity</u>
1 July 2016	\$1 500 000	\$540 000	\$ <u> </u>
30 June 2017	1 810 000	<u> </u>	1 400 000

What is the amount of Liabilities at 30 June 2017?

ANS:\$410 000 PTS: 1 DIF: 2 OBJ: 1-2 | 1-3|1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

- 13.** The following information comes from the records of America Corporation:

	<u>Assets</u>	<u>Liabilities</u>	<u>Equity</u>
1 July 2016	\$1 500 000	\$540 000	\$ <u> </u>
30 June 2017	1 810 000	<u> </u>	1 400 000

Assume that the company paid dividends of \$620 000 during the year. How much profit did it earn during the year?

ANS:\$1 060 000 PTS: 1 DIF: 2 OBJ: 1-2 | 1-3|1-4 NAT: | AACSB Analytic | APO-09-Financial statements

14. The following information comes from the records of America Corporation:

	Assets	Liabilities	Equity
1 July 2016	\$1 500 000	\$540 000	\$
30 June 2017	1 810 000		1 400 000

Assume that the company paid no dividends during the year. Without looking at the income statement, how can you tell if the company is profitable or not?

ANS: Assuming that the increase in Equity would come from profit, the company would have to be considered profitable. Profit will increase Retained Earnings which is a part of Equity. PTS: 1 DIF: 2 OBJ: 1-2 | 1-3|1-4 NAT: | AACSB Analytic | APO-09-Financial statements

15. The beginning balance of retained earnings was \$800 000, and the ending balance was \$500 000. The company paid dividends of \$50 000.

Determine the amount of profit (loss) for the year.

ANS:

(250,000) loss

[\$500,000 Ending Retained Earnings – \$800,000 Beginning Retained Earnings = (\$300,000)]

[((\$300,000) decrease + \$50,000 Dividends Paid = (\$250,000) loss]

PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB Analytic | APO-09-Financial statements

16. The beginning balance of retained earnings was \$800 000, and the ending balance was \$500 000. The company paid dividends of \$50 000.

What information would one find on the income statement in addition to profit?

ANS: The income statement will show the sources of amounts earned (revenues) as well as the amount and type of costs incurred by the company (expenses) during the period. PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB Analytic | APO-09-Financial statements

17. Several amounts from Chan Company at 31 Dec 2016 are listed below.

Service revenue	\$545 000	Salaries expense	\$229 000
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Dividends paid	50 000	Rent expense	86 000
Buildings	110 000	Land	100 000
Accounts payable	40 000	Accounts receivable	28 000
Ordinary share	60 000	Retained earnings, 1 Jan. 2016	400 000
Electricity expense	19 000	Notes payable	30 000
Income tax payable	4 000	Income tax expense	110 000

Calculate profit for 2016.

ANS: \$101 000 PTS: 1 DIF: 2 OBJ: 1-2 | 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

18. Several amounts from Chan Company at 31 Dec 2016 are listed below.

Service revenue	\$545 000	Salaries expense	\$229 000
Dividends paid	50 000	Rent expense	86 000
Buildings	110 000	Land	100 000
Accounts payable	40 000	Accounts receivable	28 000
Ordinary share	60 000	Retained earnings, 1 Jan. 2016	400 000
Electricity expense	19 000	Notes payable	30 000
Income tax payable	4 000	Income tax expense	110 000

How much is Chan Company's retained earnings at the end of 2016?

ANS: \$451 000 PTS: 1 DIF: 2 OBJ: 1-2 | 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

19. Cardinal Company reported the following information at 30 June 2017:

Accounts payable	\$400 000	Dividends paid	\$100 000
Cash	\$100 000	Expenses	\$600 000
Inventories	\$700 000	Revenue	\$750 000

Calculate Cardinal Company's total assets.

ANS: \$800 000 PTS: 1 DIF: 1 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

20. Cardinal Company reported the following information at 30 June 2017:

Accounts payable	\$400 000	Dividends paid	\$100 000
Cash	\$100 000	Expenses	\$600 000
Inventories	\$700 000	Revenue	\$750 000

Calculate Cardinal Corporations' Profit for the financial year ended June 30, 2017.

ANS: \$150 000 PTS: 1 DIF: 1 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

21. Cardinal Company reported the following information at 30 June 2017:

Accounts payable	\$400 000	Dividends paid	\$100 000
Cash	\$100 000	Expenses	\$600 000
Inventories	\$700 000	Revenue	\$750 000

Calculate Cardinal Corporation's Total Equity at June 30, 2017.

ANS: \$400 000 PTS: 1 DIF: 1 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB
Analytic | APO-09-Financial statements

22. Newton Corporation began operations on 2 July 2015, with a total investment of \$150 000 by its shareholders. Net loss for its first year of business was \$20 000. During 2017 and 2018, profit increased to \$120 000 and to \$150 000, respectively. Newton paid \$50 000 per year in dividends to its shareholders in 2017 and 2018.

In good form, prepare a statement of changes in equity for the year ended 30 June 2018.

ANS:

Newton Corporation Statement of changes in equity For the Year Ended 30 June 2018	
Beginning balance, 1 July 2017	\$(20 000)*
Add: Profit for 2016/17	120 000
Less: Dividends paid during the year	<u>(50 000)</u>
Ending balance, 30 June 2018	<u>\$ 50 000</u>

\$-20 000 Net Loss for 2016 – \$0 Dividends paid = \$(20 000) Balance, 1 July 2015

PTS: 1 DIF: 2 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB Analytic | APO-09-Financial statements

23. Newton Corporation began operations on 2 July 2015, with a total investment of \$150 000 by its shareholders. Net loss for its first year of business was \$20 000. During 2017 and 2018, profit increased to \$120 000 and to \$150 000, respectively. Newton paid \$50 000 per year in dividends to its shareholders in 2017 and 2018.

How much is total retained earnings on 30 June 2018?

ANS: Retained earnings at 30 June 2018 = \$150 000

PTS: 1 DIF: 2 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB Analytic | APO-09-
Financial statements

- 24.** Newton Corporation began operations on 2 July 2015, with a total investment of \$150 000 by its shareholders. Net loss for its first year of business was \$20 000. During 2017 and 2018, profit increased to \$120 000 and to \$150 000, respectively. Newton paid \$50 000 per year in dividends to its shareholders in 2017 and 2018

Explain the link between the statement of changes in equity and the balance sheet.

ANS: The ending balance of the retained earnings statement represents the cumulative earnings less all the dividends declared and paid for the life of the business. This amount appears on the balance sheet as a component of shareholders' equity.

PTS: 1 DIF: 2 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB Analytic | APO-09-
Financial statements

Essay

- 1.** Identify which assumption or principles apply to the following and explain why.

Globall is an Australian company that has divisions in several countries around the world. Each country has a currency different than the Australian dollar. Globall must include the financial data of its worldwide divisions in its financial statements.

ANS: The monetary unit assumption. Financial statements must be reported in monetary terms, and the standard monetary unit should be denominated in one currency.

PTS: 1 DIF: 2 OBJ: 1-1 NAT: | AACSB Communication | APO-02-
GAAP

- 2.** Identify which assumption or principles apply to the following and explain why.

Chow and Howell operate a security business as a partnership. The partners are considering a change to the corporate form of business organisation.

ANS: Economic entity assumption. A business can take three forms. Regardless of the form, however, the unit itself is distinct from its owners.

PTS: 1 DIF: 2 OBJ: 1-1 NAT: | AACSB Communication | APO-02-
GAAP

- 3.** Identify which assumption or principles apply to the following and explain why.

Yum Shop is a locally owned and operated confectionary store. The owners have decided to expand into nearby cities. Expansion will require more capital, but management does not expect it will stay in business for more than one year regardless of its expansion plans.

ANS: Continuity (going concern) assumption. A business is assumed to continue to operate long enough to carry out its obligations, to more accurately reflect the valuation of assets and appropriately allocate costs to accounting periods.

PTS: 1 DIF: 2 OBJ: 1-1 NAT: | AACSB Communication | APO-02-GAAP

4. What is the purpose of an income statement?

ANS: An income statement (or income statement) reports the company's revenues and expenses for a period of time and shows the company's profitability (or lack of). The income statement is sometimes called the 'profit or loss statement.'

PTS: 1 DIF: 1 OBJ: 1-2 NAT: | AACSB Communication | APO-09-Financial statements

5. List the four financial statements. Explain the connection between these four statements.

ANS:

- The balance sheet (Balance Sheet)
- The income statement (Income Statement)
- The statement of changes in equity
- The statement of cash flows

Profit on the income statement increases retained earnings on the statement of changes in equity. The balance in the statement of changes in equity goes to the balance sheet. The ending balance for cash on the statement of cash flows is also shown on the balance sheet.

PTS: 1 DIF: 3 OBJ: 1-2 | 1-3 | 1-4 NAT: | AACSB Analytic | APO-09-Financial statements

6. Paige Company claims that its financial information is useful. What four qualities must be present in order to have 'useful' accounting information? Explain these four qualities.

ANS:

The four qualitative characteristics of useful accounting information are relevance, reliability, comparability and consistency.

- Relevant information has the capacity to make a difference in a decision. It helps users predict future events or provides feedback.
- Reliable information is dependable, verifiable and free from bias.
- Comparability allows comparisons to be made between or among companies.
- Consistency refers to the application of the same accounting principles over time.

PTS: 1 DIF: 1 OBJ: 1-6 | 1-7 NAT: | AACSB Communication |
APO-02-GAAP

7. What is the difference between comparability and consistency?

ANS:

- Comparability allows comparisons to be made between or among companies. Even though a certain amount of freedom exists in selecting accounting principles, when this information is disclosed in the financial statements, users can still compare the information when they know what principle is used.
- Consistency refers to the application of the same accounting principles over time. It involves the relationships between a set of numbers over several periods, but within one company only, unlike comparability that can be between or among companies.

PTS: 1 DIF: 1 OBJ: 1-6 | 1-7 NAT: | AACSB Communication |
APO-02-GAAP