

Financial Accounting, 6Ce (Harrison)
Chapter 1 The Financial Statements

1.1 Explain why accounting is the language of business

1) Which of the following persons or groups have the ultimate control of a corporation?

- A) the chief executive officer
- B) the board of directors
- C) the audit committee
- D) the shareholders

Answer: D

Diff: 2 Type: MC

L.O.: 1-1

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

2) Financial statements are:

- A) reports issued by outside consultants who are hired to analyze key operations of the business
- B) reports created by management that states it is responsible for the acts of the corporation
- C) standard documents that tell us how well a business is performing and where it stands in financial terms
- D) standard documents issued by outside consultants who are hired to analyze key operations of the business in financial terms

Answer: C

Diff: 1 Type: MC

L.O.: 1-1

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3) Since they are both the same activities, the terms "accounting" and "bookkeeping" are synonymous and can be used interchangeably.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-1

CPA COMPETENCIES: Chapter 1

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4) The three forms of business organizations are sole proprietorships, partnerships, and non-profit organizations.

Answer: FALSE

Diff: 1 Type: TF

L.O.: 1-1

CPA COMPETENCIES: Chapter 1

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5) Accounting is called an information system since it measures business activities, processes data into reports, and communicates results to decision makers.

Answer: TRUE

Diff: 1 Type: TF

L.O.: 1-1

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6) From a legal perspective, sole proprietors, partners and shareholders are personally liable for the debts of their businesses they invest in.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-1

CPA COMPETENCIES: Chapter 1

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7) From an accounting viewpoint, a proprietorship is a distinct and separate entity from the proprietor.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-1

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8) The owners' equity of proprietorships and partnerships is different.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-1

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9) Financial accounting information is prepared exclusively for external users.

Answer: FALSE

Explanation: Financial accounting information is prepared for both internal and external users.

Diff: 1 Type: TF

L.O.: 1-1

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10) Management accounting is prepared primarily for external users.

Answer: FALSE

Explanation: Management accounting is prepared primarily for internal users.

Diff: 1 Type: TF

L.O.: 1-1

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11) One benefit of organizing a business as a proprietorship is that the proprietor is not required to pay income tax on the business' earnings.

Answer: FALSE

Explanation: The proprietor must report the proprietorship's income on his or her personal tax return.

Diff: 1 Type: TF

L.O.: 1-1

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12) Accounting is often referred to as "the language of business." Why is accounting described this way? How is accounting different from bookkeeping?

Answer: Accounting is the system that measures business activities, processes that information into reports, and communicates the results to decision makers. Accounting, as an information system, provides the elements necessary for management and others to make decisions and estimate how well a company may perform in the future. Accounting is the common "language" used by managers, investors, and others to communicate information about a business.

Bookkeeping is simply the procedural element of accounting that processes the accounting data.

Accounting is an information system, of which bookkeeping is a component.

Diff: 1 Type: ES

L.O.: 1-1

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13) There are several types of decision makers who use accounting information. List five of these users of accounting information and give an example of a decision each would make.

Answer: Individuals

- to manage bank accounts
- to evaluate job prospects
- to make investments
- to decide whether to rent or buy a home

Managers of businesses

- to set goals for the organization
- to evaluate progress toward those goals
- to decide how much inventory to keep on hand
- to decide how much cash to borrow

Investors and creditors

- to decide whether or not to invest in a new company
- to determine whether or not to make a loan

Government regulatory agencies (e.g., Ontario Securities Commission)

- to make sure that the company is abiding by federal or provincial regulations

Taxing authorities

- to determine the amount of tax due

Non-profit organizations

- to set goals for the organization
- to evaluate progress toward those goals
- to decide how much cash to borrow

Labour unions

- to determine wage demands

Diff: 2 Type: ES

L.O.: 1-1

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14) What are the three forms of business organizations? How do they differ?

Answer: A *proprietorship* has a single, or sole, owner who is responsible for the business and its operations. A *partnership* has two or more individuals who operate together as co-owners of the business. In both of these forms of organization, the owners are individually liable for the debts of the business. A *corporation* is a business owned by shareholders, who may or may not have a part in the day-to-day operations of the business. The shareholders of a corporation are not legally liable for the debts of the business.

It is easier to sell one's ownership of a corporation, since the ownership is evidenced by shares of stock, which can be traded. There are legal rules to be considered when a partner wishes to sell his or her interest in a partnership. Such rules make it more difficult to sell a partnership interest. A sole proprietor who sells his or her business may encounter difficulty since the business owner may be the business itself (such as a consultant or other independent contractor).

Diff: 2 Type: ES

L.O.: 1-1

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15) There are many different stakeholders in Canadian Tire Corporation. Explain why the same information may not be suitable or appropriate for all stakeholders.

Answer: Different stakeholders make different decisions that require different information. For example, lenders want to know whether the company will be able to repay its loans but the Canada Revenue Agency (CRA) wants to know the amount of taxes that should be paid for the current year. Much of the information that the lenders would request, such as who are the company's major customers and the amounts they owe the company, would be of no interest to CRA. CRA is simply interested in compliance with the income tax act.

Diff: 3 Type: ES

L.O.: 1-1

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16) Canadian Tire is a publicly owned corporation. How does it differ from a privately owned corporation?

Answer: The shares of Canadian Tire can be bought or sold on the Toronto Stock Exchange without asking the permission of the other shareholders, which is not true of a private corporation. The ownership of the shares of private corporations is limited. Shares of private corporations can only be purchased with the agreement of the existing shareholders.

Private corporations are not necessarily small. For instance, The Jim Pattison Group is Canada's third largest privately held company and has 31,000 employees and annual sales of more than \$6 billion.

Diff: 3 Type: ES

L.O.: 1-1

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17) What is a not-for-profit organization?

Answer: A not-for-profit organization is organized for some other purpose than the earning of profit. Many examples are possible. For example, The Salvation Army or the University of Toronto are organized for the purpose of providing services to community stakeholders.

Many business students will eventually find employment in not-for-profit organizations or the public sector and a knowledge of accounting is just as important in these types of organizations as it is in multinational public corporations.

Diff: 3 Type: ES

L.O.: 1-1

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18) Think about the impact accounting has on our economy and our nation. Name some external groups interested in reviewing a company's financial statements.

Answer:

- shareholders and other investors
- bankers
- other creditors
- Canada Customs and Revenue Agency
- other governmental agencies
- the general public

Diff: 1 Type: ES

L.O.: 1-1

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1.2 Describe the purpose of each financial statement and explain the elements of each one

1) Accounting standards for accountants in Canada are established by:

- A) the Canadian Institute of Chartered Professional Accountants
- B) the Society of Management Accountants of Canada
- C) the Certified General Accountants Association of Canada
- D) the International Accounting Standards Board

Answer: A

Diff: 2 Type: MC

L.O.: 1-2

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2) The accounting equation can be stated as:

- A) $\text{Assets} + \text{Liabilities} = \text{Shareholders' equity}$
- B) $\text{Assets} = \text{Liabilities} + \text{Shareholders' equity}$
- C) $\text{Assets} = \text{Liabilities} - \text{Shareholders' equity}$
- D) $\text{Assets} + \text{Shareholders' equity} = \text{Liabilities}$

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

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3) The owners' interest in the assets of a corporation is known as:

- A) assets
- B) shareholders' equity
- C) expenses
- D) revenues

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

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4) If liabilities increase \$120,000 during a given period and shareholders' equity decreases \$25,000 during the same period, assets must:

- A) decrease \$145,000
- B) increase \$145,000
- C) increase \$95,000
- D) decrease \$95,000

Answer: C

Diff: 3 Type: MC

L.O.: 1-2

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5) Which of the following best describes a liability?

- A) Liabilities are a form of share capital.
- B) Liabilities are future economic benefits to which a company is entitled.
- C) Liabilities are accounts receivable of the company.
- D) Liabilities are economic obligations to creditors to be paid at some future date by the company.

Answer: D

Diff: 1 Type: MC

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6) Expenses are:

- A) increases in assets resulting from operations
- B) increases in retained earnings resulting from operations
- C) increases in liabilities resulting from purchasing assets
- D) decreases in retained earnings resulting from operations

Answer: D

Diff: 2 Type: MC

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7) On January 1, 2017, total assets for Liftoff Technologies were \$125,000; on December 31, 2017, total assets were \$145,000. On January 1, 2017, total liabilities were \$110,000; on December 31, 2017, total liabilities were \$115,000. What are the amount of the change and the direction of the change in Liftoff Technologies shareholders' equity for 2017?

- A) decrease of \$15,000
- B) increase of \$15,000
- C) increase of \$30,000
- D) decrease of \$30,000

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

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8) Receivables are classified as:

- A) increases in earnings
- B) assets
- C) decreases in earnings
- D) liabilities

Answer: B

Diff: 1 Type: MC

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9) Shareholders' equity for Raisin Corporation on January 1, 2017 and December 31, 2017 were \$60,000 and \$75,000, respectively. Assets on January 1, 2017 and December 31, 2017 were \$115,000 and \$105,000, respectively. Liabilities on January 1, 2017 were \$55,000. What is the amount of liabilities on December 31, 2017?

- A) \$40,000
- B) \$15,000
- C) \$30,000
- D) \$55,000

Answer: C

Diff: 3 Type: MC

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10) Claims held by the shareholders (owners) of a corporation are referred to as:

- A) retained earnings
- B) share capital
- C) share capital minus retained earnings
- D) share capital plus retained earnings

Answer: D

Diff: 3 Type: MC

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11) Revenues are:

- A) increases in liabilities resulting from delivering goods or services to customers
- B) increases in retained earnings resulting from delivering goods or services to customers
- C) decreases in assets resulting from delivering goods or services to customers
- D) decreases in retained earnings resulting from delivering goods or services to customers

Answer: B

Diff: 2 Type: MC

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12) If assets increase \$120,000 during a given period and liabilities decrease \$25,000 during the same period, shareholders' equity must:

- A) increase \$95,000
- B) decrease \$145,000
- C) decrease \$95,000
- D) increase \$145,000

Answer: D

Diff: 3 Type: MC

L.O.: 1-2

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13) Which of the following financial statements would a potential investor most likely use to evaluate a company's financial performance for the current period?

- A) balance sheet
- B) income statement
- C) cash flow statement
- D) retained earnings statement

Answer: B

Diff: 2 Type: MC

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14) How do revenues for a period relate to the beginning and ending balances in retained earnings?

- A) Revenues will increase the beginning balance of retained earnings for the period.
- B) Revenues will decrease the beginning balance of retained earnings for the period.
- C) Revenues less expenses will either increase or decrease the beginning balance of retained earnings for the period.
- D) Revenues less expenses will either increase or decrease the ending balance of retained earnings for the period.

Answer: D

Diff: 2 Type: MC

L.O.: 1-2

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15) Retained earnings appear on which of the following financial statements?

- A) statement of retained earnings, cash flow statement, and income statement, but not the balance sheet
- B) statement of retained earnings and balance sheet, but not the income statement or cash flow statement
- C) statement of retained earnings, cash flow statement, and balance sheet, but not the income statement
- D) statement of retained earnings and cash flow statement, but not the income statement or balance sheet

Answer: B

Diff: 3 Type: MC

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16) Dividends appear on the:

- A) retained earnings statement
- B) income statement
- C) balance sheet
- D) both the retained earnings statement and the income statement

Answer: A

Diff: 2 Type: MC

L.O.: 1-2

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17) Dividends:

- A) always affect net income
- B) are distributions to shareholders of assets (usually cash) generated by net income
- C) are expenses
- D) must be paid to shareholders when the company earns a profit

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

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18) Assets appear on the:

- A) balance sheet
- B) income statement
- C) retained earnings statement
- D) cash flow statement

Answer: A

Diff: 1 Type: MC

L.O.: 1-2

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19) An investor wishes to assess a company's financial position at the end of the period. Which financial statement would the investor probably examine?

- A) the cash flow statement
- B) the income statement
- C) the balance sheet
- D) the statement of retained earnings

Answer: C

Diff: 2 Type: MC

L.O.: 1-2

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20) The balance sheet is sometimes also called the:

- A) statement of operations
- B) statement of cash position
- C) statement of financial position
- D) statement of income and expense

Answer: C

Diff: 2 Type: MC

L.O.: 1-2

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21) The cash flow statement is divided into three categories relating to cash flows from operating, investing, and:

- A) management planning activities
- B) financing activities
- C) strategic positioning activities
- D) marketing activities

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

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22) To determine a company's gross margin for the period, an investor would look on the:

- A) balance sheet
- B) cash flow statement
- C) income statement
- D) statement of retained earnings

Answer: C

Diff: 1 Type: MC

L.O.: 1-2

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23) Which financial statement is based on the accounting equation?

- A) statement of retained earnings
- B) income statement
- C) cash flow statement
- D) balance sheet

Answer: D

Diff: 1 Type: MC

L.O.: 1-2

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24) The main source of cash for a business normally arises from:

- A) current assets
- B) operating activities
- C) financing activities
- D) investing activities

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

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25) Gains and losses appear on which of the financial statements listed below?

- A) the balance sheet
- B) the income statement
- C) the retained earnings statement
- D) the cash flow statement

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

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26) The date of the income statement:

- A) covers one day in time
- B) covers a period of time, usually for an accounting period
- C) is not dated
- D) may cover a period of time or only one day in time, like a snapshot photograph

Answer: B

Diff: 3 Type: MC

L.O.: 1-2

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27) Operating expenses appear on the income statement:

- A) directly after gross margin
- B) directly after cost of goods sold
- C) directly after revenue
- D) do not appear on the income statement

Answer: A

Diff: 2 Type: MC

L.O.: 1-2

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28) Common shares is a component of:

- A) total assets
- B) total liabilities
- C) share capital
- D) retained earnings

Answer: C

Diff: 2 Type: MC

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29) Cost of goods sold is:

- A) added to sales on the income statement
- B) deducted from sales on the balance sheet
- C) deducted from sales on the income statement
- D) added to sales on the retained earnings statement

Answer: C

Diff: 2 Type: MC

L.O.: 1-2

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30) Suppose The Fruit Group buys a kiwi for \$.10 and sells the kiwi for \$.50. The cost of goods sold would be:

- A) \$.10
- B) \$.40
- C) \$.50
- D) \$.05

Answer: A

Diff: 1 Type: MC

L.O.: 1-2

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31) Net income is:

- A) deducted from beginning retained earnings on the retained earnings statement
- B) added to beginning retained earnings on the retained earnings statement
- C) added to assets on the balance sheet
- D) deducted from net sales on the income statement

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

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32) Notes receivable due in 60 days would be classified as a:

- A) non-current asset on the balance sheet
- B) current asset on the balance sheet
- C) current liability on the balance sheet
- D) non-current liability on the balance sheet

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

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33) Cash received from the issuance of share capital would appear:

- A) as an operating activity on the cash flow statement
- B) would not appear on a cash flow statement
- C) as an investing activity on the cash flow statement
- D) as a financing activity on the cash flow statement

Answer: D

Diff: 2 Type: MC

L.O.: 1-2

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34) Losses are reported on the:

- A) income statement
- B) balance sheet
- C) cash flow statement
- D) statement of retained earnings

Answer: A

Diff: 2 Type: MC

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35) What is the proper order for the cash flow statement?

- A) financing activities, investing activities, and operating activities
- B) operating activities, investing activities, and financing activities
- C) operating activities, financing activities, and investing activities
- D) investing activities, financing activities, and operating activities

Answer: B

Diff: 2 Type: MC

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36) The ending balance in retained earnings appears on the:

- A) balance sheet only
- B) balance sheet and statement of retained earnings
- C) statement of retained earnings only
- D) income statement

Answer: B

Diff: 3 Type: MC

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1.1.3 Evaluates reporting processes to support reliable financial reporting

37) Cash dividends:

- A) decrease revenue on the income statement
- B) increase expenses on the income statement
- C) decrease retained earnings on the retained earnings statement
- D) decrease operating activities on the cash flow statement

Answer: C

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

38) Common shares appear on the:

- A) balance sheet
- B) income statement
- C) cash flow statement
- D) retained earnings statement

Answer: A

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

39) The repayment of a note payable would be classified as a(n):

- A) investing activity on a cash flow statement
- B) financing activity on a cash flow statement
- C) operating activity on a cash flow statement
- D) current asset on the balance sheet

Answer: B

Diff: 3 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

40) The issuance of shares for cash would be classified as a(n):

- A) investing activity on a cash flow statement
- B) financing activity on a cash flow statement
- C) operating activity on a cash flow statement
- D) current asset on the balance sheet

Answer: B

Diff: 3 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

41) Income taxes owed to the federal government would be classified as a:

- A) current asset on the balance sheet
- B) current liability on the balance sheet
- C) non-current asset on the balance sheet
- D) financing activity on the cash flow statement

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

42) The balance sheet contains information about:

- A) liabilities, equity, and expenses
- B) assets, revenues, and liabilities
- C) assets, liabilities, and equity
- D) revenues, expenses, and equity

Answer: C

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

43) Which of the following financial statements provides a "snapshot photo" of one moment in time?

- A) balance sheet
- B) income statement
- C) statement of retained earnings
- D) cash flow statement

Answer: A

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

44) Assets are generally divided into:

- A) current assets and solvent assets
- B) current assets and reliable assets
- C) non-current assets and solvent assets
- D) current assets and non-current assets

Answer: D

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

45) Current assets are assets expected to be converted to cash, sold, or consumed:

- A) within the next 12 months or within the business's normal operating cycle if less than a year
- B) within the next 12 months or within the business's normal operating cycle if longer than a year
- C) within the next 6 months
- D) within the next 24 months

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

- 46) Equipment would appear on the:
- A) income statement with the revenues
 - B) balance sheet with the non-current assets
 - C) balance sheet with the current assets
 - D) income statement with the operating expenses

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

- 1.1.1 Evaluates financial reporting needs
- 1.1.2 Evaluates the appropriateness of the basis of financial reporting
- 1.1.3 Evaluates reporting processes to support reliable financial reporting

- 47) Depreciation is normally associated with which asset on the balance sheet?

- A) land
- B) accounts receivable
- C) inventory
- D) equipment

Answer: D

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

- 1.1.1 Evaluates financial reporting needs
- 1.1.2 Evaluates the appropriateness of the basis of financial reporting
- 1.1.3 Evaluates reporting processes to support reliable financial reporting

- 48) Cash would appear on the:

- A) income statement with the revenues
- B) retained earnings statement with the net income
- C) balance sheet with the current assets
- D) balance sheet with the current liabilities

Answer: C

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

- 1.1.1 Evaluates financial reporting needs
- 1.1.2 Evaluates the appropriateness of the basis of financial reporting
- 1.1.3 Evaluates reporting processes to support reliable financial reporting

- 49) Accounts payable would appear on the:

- A) income statement with the expenses
- B) retained earnings statement with the dividends
- C) balance sheet with the current assets
- D) balance sheet with the current liabilities

Answer: D

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

- 1.1.1 Evaluates financial reporting needs
- 1.1.2 Evaluates the appropriateness of the basis of financial reporting
- 1.1.3 Evaluates reporting processes to support reliable financial reporting

50) When accounting for cash collected from customers, the transaction would appear on the cash flow statement as a(an):

- A) operating activity
- B) financing activity
- C) investing activity
- D) activity that would not appear on the cash flow statement

Answer: A

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

51) When a repurchase of shares is done by a company it:

- A) increases the amount of owners' equity
- B) decreases the amount of owners' equity
- C) decreases the amount of total liabilities
- D) increases the amount of total liabilities

Answer: B

Diff: 3 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

52) All of the following are considered standard financial statements *except* the:

- A) statement of earnings
- B) statement of assets
- C) statement of retained earnings
- D) cash flow statement

Answer: B

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

53) The statement that presents a summary of the revenues and expenses of an entity is called the:

- A) balance sheet
- B) cash flow statement
- C) statement of retained earnings
- D) income statement

Answer: D

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

54) The income statement presents a summary of the:

- A) revenues and expenses of an entity for a specific time period
- B) assets and liabilities of an entity
- C) cash inflows and outflows of an entity
- D) changes that occurred in the shareholders' equity of an entity

Answer: A

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

55) Increases in shareholders' equity arise from:

- A) investments by the owner
- B) payment of dividends
- C) net income earned during the period
- D) both investments by the owner and net income earned during the period

Answer: D

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

56) Decreases in shareholders' equity result from:

- A) owner investments
- B) a net loss during the period
- C) a net income during the period
- D) owner investments and a net loss during the period

Answer: B

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

57) Purchases and sales of non-current assets are examples of:

- A) investing activities
- B) dividend activities
- C) financing activities
- D) operating activities

Answer: A

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

58) Cash spent to purchase a new building would appear on the cash flow statement as:

- A) a financing activity
- B) an operating activity
- C) an investing activity
- D) a dividend activity

Answer: C

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

59) The payment of the chief financial officer's salary would appear:

- A) on the cash flow statement with the operating activities
- B) on the balance sheet with the current liabilities
- C) on the income statement with the revenues
- D) on the income statement as part of cost of goods sold

Answer: A

Diff: 3 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

60) Which of the following financial statements shows the net increase or decrease in cash during the period?

- A) balance sheet
- B) income statement
- C) statement of retained earnings
- D) cash flow statement

Answer: D

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

61) Which of the following statements should be prepared before the balance sheet is prepared?

- A) statement of retained earnings
- B) cash flow statement
- C) statement of financial position
- D) income statement

Answer: A

Diff: 3 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

62) The amount of net income shown on the income statement also appears on the:

- A) balance sheet
- B) statement of assets
- C) statement of financial position
- D) statement of retained earnings

Answer: D

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

63) The balance sheet contains:

- A) the amount of net income
- B) the beginning balance in retained earnings
- C) the ending balance in retained earnings
- D) the amount of dividends paid to shareholders

Answer: C

Diff: 2 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

64) What is one component of shareholders' equity?

- A) common shares
- B) notes payable
- C) property, plant, and equipment
- D) cash

Answer: A

Diff: 1 Type: MC

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

65) Generally accepted accounting principles, or GAAP, are the rules and procedures established by the Canadian Institute of Chartered Professional Accountants (CICPA Handbook).

Answer: TRUE

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

66) All corporations have to follow the same sections of the CICPA Handbook.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

67) In accounting, the word "net" means after a subtraction.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

68) Net earnings are calculated by taking a company's earnings less their dividends paid out.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

69) Retained earnings represent cash that is available to a company for future operations and expansion.

Answer: FALSE

Diff: 3 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

70) Liabilities are often referred to as "outsider claims" and owners' equity as "insider claims" to assets.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

71) It would be unusual for the balance sheet of a proprietorship to include the term "retained earnings."

Answer: TRUE

Diff: 3 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

72) A form of the accounting equation can be stated as Assets - Liabilities = Share capital + Retained earnings.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

73) The income statement measures the company's financial position at the end of the year.

Answer: FALSE

Explanation: The balance sheet measures the company's financial position at the end of the year.

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

74) The balance sheet measures how well the company performed during the year.

Answer: FALSE

Explanation: The income statement measures how well the company performed during the year.

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

75) The basic component of share capital is retained earnings.

Answer: FALSE

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

76) Shareholders' equity is often referred to as "net assets" and represents the residual amount of business assets that can be claimed by the owners.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

77) The accounting equation must always be in balance.

Answer: TRUE

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

78) The statement of retained earnings discloses the amount of dividends declared during the year.

Answer: TRUE

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

79) The statement of cash flows categorizes the sources and uses of the net cash flow generated by the company during the year.

Answer: TRUE

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

80) Expenses are increases in retained earnings that result from operations.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

81) For business purposes, dividend payments are classified as expenses.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

82) Revenues less cash outflow equals net income (or net loss).

Answer: FALSE

Diff: 1 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

83) The Cash Flow Statement is organized in terms of the organization's operating, investing, and financing activities.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

84) The payment of interest is a financing activity.

Answer: FALSE

Explanation: The payment of interest (under ASPE) is an operating activity.

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

85) Dividends are a form of expenses.

Answer: FALSE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

86) Revenues are increases in retained earnings from the delivery of goods or services.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

87) Closing retained earnings as reported on the balance sheet represent a company's net income from its formation, less the cumulative dividends declared to-date.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

88) Your friend has asked you to review and analyze the financial status of her company before she goes to the bank to request a loan. Answer the following questions:

- a. What will you need to review in order to make a sound decision?
- b. What will the bank be looking for? Be specific.

Answer:

a. A decision maker would like to have access to all the financial statements of a company for several years, including the income statement, balance sheet, statement of retained earnings, and cash flow statement.

b. The bank will be looking at the company's ability to repay the loan. The bank will look at the amount of income generated by the company for the past several years as well as whether or not it has been increasing or decreasing. The amount of debt already owed by the company will also be an issue. The bank would like to see that shareholders' equity exceeds total liabilities at the time of the loan request. Also, dividends paid to the owner should not exceed the net income in any given period. These are indications that the owner is as much at risk as the bank would be if the loan were granted.

Diff: 3 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

89) Following is an alphabetical list of the assets, liabilities, revenues, and expenses of Keykin Inc. Prepare an income statement for the year ended September 30, 2017.

Accounts payable	\$2,800	Note payable	\$4,000
Accounts receivable	5,400	Rent expense	10,200
Advertising expense	3,600	Salary expense	12,100
Cash	9,100	Salary payable	900
Cost of goods sold	31,700	Sales revenue	75,800
Inventory	7,900	Supplies	1,800
Interest expense	800	Utilities expense	700

Answer: Keykin Inc.

Income Statement

For the Year Ended September 30, 2017

Revenues:

Sales revenue	\$75,800
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Expenses:

Cost of goods sold	\$31,700	
Rent expense	10,200	
Salary expense	12,100	
Advertising expense	3,600	
Interest expense	800	
Utilities expense	<u>700</u>	<u>59,100</u>

Net income		<u>\$16,700</u>
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Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

90) Snow Inc. gathered together the following information regarding the asset, liability, shareholders' equity, revenue, and expense accounts as of the end of its first year in operations, July 31, 2017:

Rent expense	\$7,500	Dividends	\$10,200
Truck	14,600	Accounts payable	6,700
Supplies	2,500	Service revenue	45,500
Salary expense	19,400	Salary payable	1,200
Accounts receivable	8,200	Utilities expense	5,000
Note payable	11,000	Interest expense	1,500
Common shares	25,000	Cash	20,800

Prepare an income statement for Snow Inc. for the year ended July 31, 2017.

Answer:

Snow Inc.

Income Statement

For the Year Ended July 31, 2017

Revenues:

Service revenue	\$45,500
-----------------	----------

Expenses:

Salary expense	\$19,400	
Rent expense	7,500	
Utilities expense	5,000	
Interest expense	<u>1,500</u>	<u>33,400</u>

Net income	<u>\$12,100</u>
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Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

91) The following alphabetical listing shows the assets, liabilities, and shareholders' equity for Zap Ltd. as of December 31, 2014. Prepare a balance sheet dated December 31, 2017.

Accounts payable	\$12,200	Inventory	\$23,500
Accounts receivable	21,000	Note payable	11,000
Cash	21,600	Retained earnings	17,100
Common shares	50,600	Salary payable	2,300
Equipment	24,600	Supplies	2,500

Answer:

Zap Ltd.

Balance Sheet

December 31, 2017

Assets		Liabilities	
Cash	\$21,600	Accounts payable	\$12,200
Accounts receivable	21,000	Note payable	11,000
Inventory	23,500	Salary payable	<u>2,300</u>
Supplies	2,500	Total liabilities	25,500
Equipment	<u>24,600</u>		
		Shareholders' equity	
		Common shares	50,600
		Retained earnings	<u>17,100</u>
		Total shareholders' equity	67,700
		Total liabilities and	
Total assets	<u>\$93,200</u>	shareholders' equity	<u>\$93,200</u>

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

92) Following is an alphabetical list of the assets, liabilities, and shareholders' equity accounts of Bliz Inc. Prepare a balance sheet dated April 30, 2017.

Accounts payable	\$10,200	Note payable	\$15,000
Accounts receivable	17,000	Retained earnings	27,500
Cash	32,900	Salary payable	10,700
Common shares	34,400	Supplies	13,900
Inventory	34,000		

Answer:

Bliz Inc.
Balance Sheet
April 30, 2017

Assets		Liabilities	
Cash	\$32,900	Accounts payable	\$10,200
Accounts receivable	17,000	Note payable	15,000
Inventory	34,000	Salary payable	<u>10,700</u>
Supplies	<u>13,900</u>	Total liabilities	35,900
		Shareholders' equity	
		Common shares	34,400
		Retained earnings	<u>27,500</u>
		Total shareholders' equity	61,900
Total assets	<u>\$97,800</u>	Total liabilities and shareholders' equity	<u>\$97,800</u>

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

93) Keria Corp. prepared the following random list of assets, liabilities, revenues, and expenses from its December 31, 2017, accounting records. The beginning retained earnings as of January 1, 2014, was \$43,100 and the owner, Keria Staple, received dividends of \$14,600 during the year. Prepare the balance sheet for Keria Corp. as of December 31, 2017.

Accounts receivable	\$15,700	Service revenue	\$50,500
Interest expense	4,900	Cash	128,000
Supplies	1,500	Note payable	17,000
Accounts payable	106,100	Salary expense	18,000
Utilities expense	5,200	Interest payable	1,600
Furniture	18,000	Rent expense	9,400
Salary payable	2,400	Automobiles	12,900
Common shares	30,500	Land	23,000

Answer:

Keria Corp.
Balance Sheet
December 31, 2017

Assets		Liabilities	
Cash	\$128,000	Accounts payable	\$106,100
Accounts receivable	15,700	Note payable	17,000
Supplies	1,500	Interest payable	1,600
Furniture	18,000	Salary payable	<u>2,400</u>
Automobiles	12,900	Total liabilities	127,100
Land	<u>23,000</u>		
		Shareholders' equity	
		Common shares	30,500
		Retained earnings	<u>41,500</u> *
		Total shareholders' equity	72,000
		Total liabilities and	
Total assets	<u>\$199,100</u>	shareholders' equity	<u>\$199,100</u>

* $\$41,500 = \$43,100 + \$13,000$ (which is net income) - $\$14,600$

Net income = $\$50,500 - \$4,900 - \$5,200 - \$18,000 - \$9,400 = \$13,000$

Diff: 3 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

94) Tall Tree Ltd. gathered together the following information regarding the asset, liability, shareholders' equity, revenue, and expense accounts as of the end of its first year in operation, May 31, 2017:

Accounts payable	\$9,600	Rent expense	\$6,500
Accounts receivable	3,200	Salary expense	19,400
Cash	13,800	Salary payable	1,300
Common shares	15,000	Service revenue	45,500
Dividends	8,300	Supplies	2,500
Interest expense	1,200	Truck	34,600
Note payable	21,000	Utilities expense	5,000

Prepare the Statement of Retained Earnings for Tall Tree Ltd. for the year ended May 31, 2017.

Answer: Tall Tree Ltd.

Statement of Retained Earnings
For the Year Ended May 31, 2017

Retained earnings, June 1, 2016	\$0
Add: Net income	<u>13,400</u>
	13,400
Deduct: Dividends	<u>8,300</u>
Retained earnings, May 31, 2017	<u><u>\$5,100</u></u>

*Net income \$13,400 = 45,500 - 1,200 - 6,500 - 19,400 - 5,000

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

95) A cash flow statement is divided into the following sections: cash flows from operating activities, cash flows from investing activities, and cash flows from financing activities. For each of the following events, state the section in which it would be listed.

- a. Received cash from issuance of long-term note payable
- b. Payment of interest (ASPE)
- c. Repurchase of shares
- d. Sale of land
- e. Received cash from customers
- f. Payment of dividends
- g. Purchase of equipment
- h. Issuance of 50 shares of common stock

Answer:

- a. financing activity
- b. operating activity
- c. financing activity
- d. investing activity
- e. operating activity
- f. financing activity
- g. investing activity
- h. financing activity

Diff: 3 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

96) Classify each statement below as an operating activity, investing activity, or a financing activity.

- a. Sold 12,000 shares for cash.
- b. Paid salaries of employees.
- c. Paid amount due for income taxes.
- d. Paid interest expense (ASPE).
- e. Purchased office equipment for cash.
- f. Sold old office equipment and received cash.
- g. Received interest income.
- h. Paid interest on a bank loan.
- i. Paid dividends to shareholders.

Answer:

- a. financing activity
- b. operating activity
- c. operating activity
- d. operating activity
- e. investing activity
- f. investing activity
- g. operating activity
- h. operating activity
- i. financing activity

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

97) Prepare a Statement of Retained Earnings: On October 31, 2017, Lariat Inc. reported retained earnings of \$250,000. For the year ended October 31, 2017, Lariat had a net income of \$80,000 and paid dividends of \$50,000.

Answer:

Lariat Inc.

Statement of Retained Earnings

For the year ended October 31, 2017

Retained Earnings, November 1, 2016	\$ 250,000
Net income for the year	80,000
Less dividends	<u>(50,000)</u>
Retained Earnings, October 31, 2017	<u>\$ 280,000</u>

Diff: 3 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

98) A cash flow statement is divided into the following sections: cash flows from operating activities, cash flows from investing activities, and cash flows from financing activities. For each of the following events, state the section in which it would be listed.

- a. Paid cash to retire long-term note payable
- b. Payment of wages
- c. Issuance of shares
- d. Purchase of land
- e. Amortization expense
- f. Payment of dividends
- g. Sale of equipment
- h. Equipment rental fee

Answer:

- a. financing activity
- b. operating activity
- c. financing activity
- d. investing activity
- e. operating activity (be careful - it is a non-cash item but still shows up here)
- f. financing activity
- g. investing activity
- h. operating activity

Diff: 3 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

99) A company's management makes three major types of decisions on an ongoing basis: decisions regarding *operating* activities, decisions regarding *investing* activities, and decisions regarding *financing* activities. Discuss each of these three types of activities, including examples of each type.

Answer: *Operating* activities relate to deciding how to operate the business and involves decisions such as what products and/or services to sell, what prices to sell those products and services for, and how to market those products and services. *Investing* activities relate to deciding what kinds of investments to make and involve decisions such as what types of non-current assets to buy. *Financing* activities relate to deciding how to finance the company's operations and involve decisions such as whether to obtain cash by selling shares or by borrowing from a bank.

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

100) What do shareholders look for when reviewing and analyzing the income statement?

Answer: When reviewing the income statement, shareholders look for steadily increasing levels of net income over time. Net income on an income statement means the company is profitable. A steady increase in net income indicates the company's profits are solid. Net income affects both stock prices and future dividends. A shareholder's personal wealth will be enhanced through an increase in the market price of the company's stock and future dividends to be received.

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

101) What do creditors such as bankers look for when reviewing assets and liabilities on the balance sheet?

Answer: Assets show what the company can pledge as collateral that a creditor can collect in the event of the company failing to pay its debts. Liabilities indicate how much the company owes other creditors. Assets should be increasing faster than liabilities over time. The amount of assets should exceed the amount of liabilities.

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

102) What is the purpose of a cash flow statement?

Answer: A cash flow statement reports how the company generates and uses its cash. Wise use of cash generates revenues and additional cash. Operating activities should be the main source of cash. The cash flow statement provides information that would be difficult to obtain from analyzing the other financial statements.

Diff: 2 Type: ES

L.O.: 1-2

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

1.3 Explain the relationships among the financial statements

1) Which financial statement must be prepared before the others?

- A) income statement
- B) balance sheet
- C) cash flow statement
- D) retained earnings statement

Answer: A

Diff: 2 Type: MC

L.O.: 1-3

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

2) Describe the relationship between the Income Statement, Statement of Retained Earnings and the Balance Sheet.

Answer: The income statement needs to be prepared first as the net income figure is part of the calculation of ending retained earnings on the Statement of Retained Earnings. Once the Statement of Retained Earnings has been prepared this figure is then inserted in the Balance Sheet in the Shareholders' Equity section.

Diff: 2 Type: ES

L.O.: 1-3

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

3) The closing retained earnings balance as determined by compiling the balance sheet is used to complete the statement of retained earnings.

Answer: FALSE

Explanation: The closing retained earnings balance as determined by completing the statement of retained earnings is reported as part of shareholders' equity on the balance sheet.

Diff: 2 Type: TF

L.O.: 1-3

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

4) Tap Corporation gathered together the following information regarding the asset, liability, shareholders' equity, revenue, and expense accounts as of the end of its first year in operations, August 31, 2017:

Rent expense	\$ 7,500	Dividends	\$10,200
Truck	23,600	Accounts payable	6,700
Supplies	2,500	Service revenue	45,600
Salary expense	19,400	Salary payable	12,200
Accounts receivable	8,200	Utilities expense	5,000
Note payable	10,000	Interest expense	1,200
Common shares	25,000	Cash	21,900

Prepare a balance sheet for Tap Corporation dated August 31, 2017.

Answer:

Tap Corporation
Balance Sheet
August 31, 2017

Assets		Liabilities	
Cash	\$21,900	Accounts payable	\$6,700
Accounts receivable	8,200	Note payable	10,000
Supplies	2,500	Salary payable	<u>12,200</u>
Truck	<u>23,600</u>	Total liabilities	28,900
		Shareholders' equity	
		Common shares	25,000
		Retained earnings	<u>2,300</u> *
		Total shareholders' equity	27,300
		Total liabilities and	
Total assets	<u>\$56,200</u>	Shareholders' equity	<u>\$56,200</u>

* \$2,300 = \$0 + \$12,500 (net income) - \$10,200

Net income = \$45,600 - \$7,500 - \$19,400 - \$5,000 - \$1,200 = \$12,500

Diff: 3 Type: ES

L.O.: 1-3

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

5) Choose the appropriate definition for the terms below.

- a. a business owned by a single owner
- b. a statement summarizing the revenues and expenses for a given period
- c. resources that provide future economic benefits to a business
- d. claims by outsiders on the resources of a business
- e. revenues less expenses
- f. a business owned by shareholders
- g. shows the net change in the cash account for a given period
- h. a formal listing of the accounting equation on a specified date

- _____ 1. corporation
- _____ 2. cash flow statement
- _____ 3. income statement
- _____ 4. net income
- _____ 5. proprietorship
- _____ 6. balance sheet
- _____ 7. liabilities
- _____ 8. assets

Answer:

- 1. f
- 2. g
- 3. b
- 4. e
- 5. a
- 6. h
- 7. d
- 8. c

Diff: 2 Type: ES

L.O.: 1-3

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

1.4 Explain accounting's conceptual framework and underlying assumptions

1) In order for information to be considered a faithful representation it must be all of the following *except*:

- A) complete
- B) predictive
- C) without material error
- D) neutral

Answer: B

Diff: 2 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

2) The primary objective of financial reporting is to provide information:

- A) to the federal government about tax matters
- B) useful for making investment and lending decisions
- C) regarding the cash flows of the business
- D) about the profitability of the business

Answer: B

Diff: 2 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

3) The _____ assumption assumes that the organization will continue operating normally for the foreseeable future.

- A) cost
- B) stable monetary unit
- C) entity
- D) going-concern

Answer: D

Diff: 1 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

4) The accounting concept that maintains that each organization or section of an organization stands apart from other organizations and individuals is known as the:

- A) reliability principle
- B) going-concern assumption
- C) entity assumption
- D) monetary unit assumption

Answer: C

Diff: 2 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

5) The principle that states that assets acquired by the business should be recorded at their actual price is the:

- A) objectivity assumption
- B) stable monetary unit assumption
- C) cost assumption
- D) reliability assumption

Answer: C

Diff: 1 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

6) The relevant measure of value of the assets of a company that is going out of business is its:

- A) historical cost
- B) recorded value
- C) book value
- D) liquidation value

Answer: D

Diff: 2 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

7) The CEO of a business owns a home and two automobiles. The company the CEO works for also owns automobiles and a home in a remote area used for strategic planning meetings by its executives. Which principle or assumption "draws a sharp boundary" around the possessions of the CEO and the assets of the business for which he works?

- A) the entity assumption
- B) the stable-monetary-unit assumption
- C) the going-concern assumption
- D) the objectivity assumption

Answer: A

Diff: 2 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

8) The stable-monetary-unit assumption is the basis for ignoring:

- A) the possibility that the value of inventory might drop below its historical cost
- B) fluctuations in the value of the Canadian dollar relative to foreign currencies
- C) the effect of inflation in the accounting records
- D) the difference between the appraised value and the actual cost when recording an asset at its historical cost

Answer: C

Diff: 3 Type: MC

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

9) The reliability principle states that assets and services should be recorded at their actual cost, since cost is a reliable measure to use in financial accounting.

Answer: FALSE

Diff: 1 Type: TF

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

10) Relevance and comparability are the two fundamental qualitative characteristics of accounting.

Answer: FALSE

Explanation: Comparability is an enhancing qualitative characteristic; faithful representation is the other fundamental qualitative characteristic.

Diff: 2 Type: TF

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

11) Materiality is a component of the faithful representation qualitative characteristic.

Answer: FALSE

Explanation: Materiality is a component of the relevance qualitative characteristic.

Diff: 2 Type: TF

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

12) Financial statement information that reflects the economic substance of a transaction is considered to be representationally faithful.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

13) Choose the appropriate definition for the terms below.

- a. professional guidelines followed by accountants
- b. corporations that have issued shares in public markets
- c. organizations that do not issue information used by the public
- d. set of standards used by public corporations
- e. the group responsible for Canadian GAAP
- f. issues International Financial Reporting Standards
- g. designates the CICPA Handbook as GAAP
- h. this group was established to oversee accounting and reporting standards for both Canadian companies and not-for-profits

- _____ 1. International Accounting Standards Board
- _____ 2. Canadian Business Corporations Act
- _____ 3. publicly accountable enterprises
- _____ 4. Canadian Institute of Chartered Professional Accountants
- _____ 5. GAAP
- _____ 6. Accounting Standards Board
- _____ 7. International Financial Reporting Standards
- _____ 8. private enterprises

Answer:

- 1. f
- 2. g
- 3. b
- 4. e
- 5. a
- 6. h
- 7. d
- 8. c

Diff: 2 Type: ES

L.O.: 1-4

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

1.5 Make ethical business decisions

1) All of the following are purposes of internal control *except*:

- A) to safeguard assets
- B) to ensure accurate and reliable accounting records
- C) to encourage adherence to company policies
- D) to promote operational inefficiency

Answer: D

Diff: 1 Type: MC

L.O.: 1-5

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

2) The CICPA has a code of professional conduct.

Answer: TRUE

Diff: 1 Type: TF

L.O.: 1-5

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

3) The most common form of management fraud is earnings management.

Answer: TRUE

Diff: 2 Type: TF

L.O.: 1-5

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

4) Identify and briefly describe the two most common types of fraud that impact financial statements.

Answer: The two most common types of fraud that impact financial statements are misappropriation of assets and fraudulent financial reporting. Misappropriation of assets involves employees stealing cash or other assets such as inventory from the company. Fraudulent financial reporting occurs when managers make false and misleading entries in the books making financial results of the company appear better than they actually are.

Diff: 2 Type: ES

L.O.: 1-5

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting

5) Fraudulent financial reporting is a type of fraud than impacts on financial statements. Why do managers undertake this type of fraudulent activity?

Answer: Managers falsify financial reporting to deceive investors and creditors into loaning money to or investing in the company when they may not have done so otherwise.

Diff: 2 Type: ES

L.O.: 1-5

CPA COMPETENCIES: Chapter 1

1.1.1 Evaluates financial reporting needs

1.1.2 Evaluates the appropriateness of the basis of financial reporting

1.1.3 Evaluates reporting processes to support reliable financial reporting