Henderson, Issues in Financial Accounting 16e

Chapter 2: The conceptual framework: Purpose, reporting entity, the objective of financial reporting, and qualitative characteristics

1) Which of the following is not a fundamental issue when an accountant faces a new type of transaction?

A) recognition
B) measurement
C) disclosure
D) issuance
Answer: D
AACSB: Analytical Thinking
Topic: 2.2 The nature and purpose of a conceptual framework.
Learning Objective: LO 2.1. Describe the purpose of a conceptual framework.
Difficulty: Easy

2) The major beneficiary from the development of a conceptual framework is expected to be:

A) governments
B) preparers of financial reports
C) accounting standard setters
D) managers
Answer: C
AACSB: Analytical Thinking
Topic: 2.2 The nature and purpose of a conceptual framework.
Learning Objective: LO 2.1. Describe the purpose of a conceptual framework.
Difficulty: Medium

3) Which of the following is <u>not</u> one of the major potential benefits of a conceptual framework for accounting standards setters?

A) Improve the communication process
B) More consistent and logical accounting standards
C) Savings in auditing costs
D) Improved accountability
Answer: C
AACSB: Analytical Thinking
Topic: 2.2 The nature and purpose of a conceptual framework.
Learning Objective: LO 2.1. Describe the purpose of a conceptual framework.
Difficulty: Easy

4) The elements of financial statements, as outlined in the conceptual framework, are:

A) assets, liabilities, equity, income, expenses
B) balance sheet, income statement, cash flow statement
C) materiality, comparability, relevance, reliability
D) historical cost, current cost, net market value, constant purchasing power
Answer: A
AACSB: Written and Oral Communication
Topic: 2.2. The nature and purpose of a conceptual framework.
Learning Objective: LO 2.1. Describe the purpose of a conceptual framework.
Difficulty: Medium

5) Financial statements prepared by non-reporting entities are known as:

A) Entity financial statements
B) Special purpose financial statements
C) Quarterly mandated financial reports
D) General purpose financial statements
Answer: B
AACSB: Written and Oral Communication
Topic: 2.2. The nature and purpose of a conceptual framework.
Learning Objective: LO 2.1. Describe the purpose of a conceptual framework.
Difficulty: Medium

6) List and briefly explain the four fundamental issues that accountants address when developing the appropriate accounting policy for a new type of transaction.

Answer: *Definitions* – what are the components of the transaction for financial reporting purposes? That is, we must identify what assets, liabilities, equity, revenue or expenses are generated by the transaction. *Recognition* – having identified the elements of a transaction, the second issue is when, if at all, should those elements be incorporated into the body of the financial statements? *Measurement* – having identified and recognised the elements, it is then necessary to measure the financial effects of the transaction. *Disclosure* – as some transactions might give rise to elements that cannot yet be recognised or because users of financial statements might need extra information about particular transactions, a fourth issue is whether additional information should be provided in the notes to the financial statements.
AACSB: Analytical Thinking
Topic: 2.2. The nature and purpose of a conceptual framework.
Learning Objective: LO 2.1. Describe the purpose of a conceptual framework.
Difficulty: Medium

7) Which statement is incorrect?

A) APB statement No. 4. 'Basic-Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises' was the US profession's first conceptual framework
B) The trend in accounting over many years has been to reduce disclosure in published reports
C) The double-entry bookkeeping system was developed in Italy during the 13th and 14th centuries
D) In earlier times many present-day transactions were not contemplated by accountants
Answer: B
AACSB: Written and Oral Communication
Topic: 2.3 The history, structure and status of the Australian conceptual framework.
Learning Objective: LO 2.2. Describe the structure of the Australian conceptual framework.
Difficulty: Medium

8) From 1 January 2005 the Australian conceptual framework includes:

A) SAC 1-2 and the IASB conceptual framework
B) SAC 1-4 and the IASB conceptual framework
C) the IASB conceptual framework
D) none of the above
Answer: A
AACSB: Written and Oral Communication
Topic: 2.3. The history structure, and status of the Australian conceptual framework.
Learning Objective: LO 2.2. Describe the structure of the Australian conceptual framework.
Difficulty: Medium

9) Which components of the conceptual framework were withdrawn upon adoption of the IASB conceptual framework?

A) SAC 1 and SAC 2
B) Statements on Financial Accounting Concepts
C) SAC 3 and SAC 4

D) All of the above
Answer: C
AACSB: Written and Oral Communication
Topic: 2.3. The history structure, and status of the Australian conceptual framework.
Learning Objective: LO 2.2. Describe the structure of the Australian conceptual framework.
Difficulty: Medium

10) Which term defines a 'financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of the information needs'.

A) Balance Sheet
B) Auditor's Report
C) General Purpose Financial Statements
D) Management Discussion and Analysis
Answer: C
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.
Difficulty: Easy

12) SAC1 defines an entity which has users who are dependent on general purpose financial reports as a/an:

A) accounting entity
B) reporting entity
C) company entity
D) legal entity
Answer: B
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.
Difficulty: Easy

13) What is not a key characteristic concerning users of general purpose financial statements?

A) The users do not necessarily have to be known to the entity
B) The users are internal to the entity
C) The users lack the power to demand that the entity provides them with specific information
D) All of the above are key characteristics
Answer: B
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.
Difficulty: Medium

14) In establishing reporting requirements, the Corporations Act distinguishes between:

A) large and small proprietary companies
B) service and non-service entities
C) legal and non-legal entities
D) reporting and non-reporting entities
Answer: A
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.

Difficulty: Medium

15) Which factor(s) is/are identified in SAC1 to assist in determining whether an entity has users dependent on general purpose financial reports?

A) Type of accounting system
B) Classes of issued shares
C) Separation of management and ownership
D) All of the above
Answer: C
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.
Difficulty: Medium

16) When deciding whether an entity is a reporting entity reference should be made to:

A) relevant legislation rather than SAC1
B) SAC1 rather than relevant legislation
C) ASX listing rules rather than Australian Accounting Standards
D) Australian Accounting Standards rather than ASX listing rules
Answer: A
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.
Difficulty: Medium

17) Distinguish between general purpose and special purpose financial statements. Give examples of each type of report.

Answer: General purpose financial statements are prepared to meet the common interests of a wide range of stakeholders, with no particular stakeholder's information needs taking priority. Special purpose financial statements are prepared for specific users who have the power to demand that the entity provides financial information directly relevant to that user's specific needs. For example, a small family-owned business may be seeking a loan from a bank.
AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial reporting.
Difficulty: Medium

18) Describe the various factors in determining the existence of dependent users of financial statements.

Answer: Where the existence of dependent users is not readily obvious, then paragraph 19 of *SAC1* states that it is necessary to look at other indicative factors, which include whether:
- there is a separation of management from the entity's owners or members
- the entity is of such economic or political importance that it is likely to have an impact on the welfare of parties external to it; or
- its financial characteristics are such that it would have external stakeholders who need information about the entity. For example, the larger the entity, the more likely it is that it will have external parties, such as employees or creditors, who need, but cannot demand, financial information.

AACSB: Written and Oral Communication
Topic: 2.4. The reporting entity concept and general purpose financial reporting
Learning Objective: LO 2.3. Describe the reporting entity concept and the role of general purpose financial

reporting.
Difficulty: Medium

19) According to a study from the 1980's, what are the three components of the objective of accounting?

A) Relevance, control, and reliability
B) Faithful representation, control, and fair value
C) Accountability, decision usefulness, and control
D) Accountability, relevance, and decision usefulness
Answer: C
AACSB: Analytical Thinking
Topic: 2.5. The objective of general purpose financial reporting
Learning Objective: LO 2.4. Describe the objective of general purpose financial reporting.
Difficulty: Medium

20) The IASB Framework defines the objective of general purpose financial reporting as:

A) to provide about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity
B) to decide whether the reporting entity is achieving its objectives in accordance with Generally Accepted Accounting Principles
C) to give a true and fair view of the financial position and performance of the entity
D) None of the above
Answer: A
AACSB: Written and Oral Communication
Topic: 2.5. The objective of general purpose financial reporting
Learning Objective: LO 2.4. Describe the objective of general purpose financial reporting.
Difficulty: Medium

21) Assisting the users to assess the amount, timing and uncertainty associated with an entity's future cash flows is a decision common to:

A) the not-for-profit sector
B) auditors
C) standards setters
D) for-profit sector
Answer: D
AACSB: Written and Oral Communication
Topic: 2.5. The objective of general purpose financial reporting
Learning Objective: LO 2.4. Describe the objective of general purpose financial reporting.
Difficulty: Medium

22) What is one difficulty encountered with asking users of financial information what they want?

A) Cost-benefit constraint
B) Lack of available information
C) The decision making process is not the same for all decision makers.
D) Choice of information sources
Answer: C
AACSB: Analytical Thinking
Topic: 2.6. The qualitative characteristics of useful financial information.
Learning Objective: LO 2.4. Describe the objective of general purpose financial reporting.
Difficulty: Hard

23) Which of the following is a characteristic of financial information as suggested by the American Accounting Association?

A) Faithful Representation
B) Reliability
C) Relevance
D) Consistency
Answer: C
AACSB: Analytical Thinking
Topic: 2.6. The qualitative characteristics of useful financial information.
Learning Objective: LO 2.5. Describe the qualitative characteristics of useful financial information.
Difficulty: Hard

24) Which fundamental qualitative characteristic best describes the capability of financial information making a difference in decisions made by users?

A) Faithful representation
B) Relevance
C) Reliability
D) Comparability
Answer: B
AACSB: Analytical Thinking
Topic: 2.5. The objective of general purpose financial reporting
Learning Objective: LO 2.6. Identify the fundamental characteristics of useful financial information.
Difficulty: Medium

25) Which qualitative characteristic of financial information focuses on the inclusion of relevant information?

A) Faithful representation
B) Materiality
C) Comparability
D) Cost constraint
Answer: B
AACSB: Analytical Thinking
Topic: 2.6. The qualitative characteristics of useful financial information.
Learning Objective: LO 2.6. Identify the fundamental characteristics of useful financial information.
Difficulty: Medium

26) Which term best illustrates the assurance that financial information faithfully represents the economic phenomena it purports to represent?

A) Timeliness
B) Understandability
C) Verifiability
D) Comparability
Answer: C
AACSB: Analytical Thinking
Topic: 2.6. The qualitative characteristics of useful financial information.
Learning Objective: LO 2.7. Identify the characteristics that enhance the usefulness of financial information.
Difficulty: Medium

27) What are the two aspects related to the timeliness of financial information?

A) Relevance and comparability
B) Frequency and timing
C) Faithful representation and frequency
D) Timing and relevance
Answer: B
AACSB: Analytical Thinking
Topic: 2.6. The qualitative characteristics of useful financial information.

Learning Objective: LO 2.7. Identify the characteristics that enhance the usefulness of financial information.
Difficulty: Easy

28) Explain the differences between verifiability and understandability of financial information.

Answer: Framework 2014 identifies verifiability as an enhancing qualitative characteristic. Verifiability helps to assure users that financial information faithfully represents the economic phenomena it purports to represent. Verifiability means that different knowledgeable and independent observers could reach consensus that a particular item in the financial statements is a faithful representation. Financial information is understandable when users of that information are able to comprehend its meaning. The understandability of financial information may be influenced by the amount of detail, the use of technical language, the format of the financial statements, the headings used and so on.
AACSB: Analytical Thinking
Topic: 2.6. The qualitative characteristics of useful financial information.
Learning Objective: LO 2.7. Identify the characteristics that enhance the usefulness of financial information.
Difficulty: Medium

29) Which considerations are considered basic constraints on the preparation and presentation of financial information?

A) Relevance and reliability
B) Timeliness and faithful representation
C) Costs and benefits
D) Understandability and Verifiability
Answer: C
AACSB: Written and Oral Communication
Topic: 2.6. The qualitative characteristics of useful financial information.
Learning Objective: LO 2.8. Identify the nature of the cost constraint on the provision of useful information.
Difficulty: Medium