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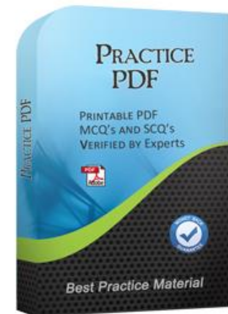

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Exam : FAR

Title : CPA Financial Accounting and Reporting

Vendor : AICPA

Version : DEMO

NO.1 Which of the following statements regarding fair value is/are correct?
I. The fair value of an asset or liability is specific to the entity making the fair value measurement.
II. Fair value is the price to acquire an asset or assume a liability.
III. Fair value includes transportation costs, but not transaction costs.
IV. The price in the principal market for an asset or liability will be the fair value measurement.
A. I & II
B. I & IV
C. II & III
D. III & IV
Answer: D
Explanation:
Choice "d" is correct. Statements III and IV are correct. Statement I is incorrect because fair value is a market-specific measure, not an entity-specific measure. Statement II is incorrect because fair value is an
exit price (the price to sell an asset or transfer a liability), not an entrance price. Choices "a", "b" and "c"
are incorrect, per the above Explanation: .

NO.2 On January 2, 1993, Quo, Inc. hired Reed to be its controller. During the year, Reed, working closely with
Quo's president and outside accountants, made changes in accounting policies, corrected several errors
dating from 1992 and before, and instituted new accounting policies.
Quo's 1993 financial statements will be presented in comparative form with its 1992 financial statements.
This question represents one of Quo's transactions. List A represents possible clarifications of these transactions as: a change in accounting principle, a change in accounting estimate, a correction of an error in previously presented financial statements, or neither an accounting change nor an accounting
error.
Item to Be Answered
Quo sells extended service contracts on its products. Because related services are performed over several years, in 1993 Quo changed from the cash method to the accrual method of recognizing income
from these service contracts.
List A (Select one)
A. Change in accounting principal.
B. Change in accounting estimate.
C. Correction of an error in previously presented financial statements.
D. Neither an accounting change nor an accounting error.
Answer: C
Explanation:
Choice "c" is correct. Change from the cash method to the accrual method is a correction of an error in
previously presented financial statements.

NO.3 Financial reporting by a development stage enterprise differs from financial reporting for an

established
operating enterprise in regard to footnote disclosures:
A. Only.
B. And expense recognition principles only.
C. And revenue recognition principles only.
D. And revenue and expense recognition principles.
Answer: A
Explanation:
Choice "a" is correct. Financial reporting by a development stage enterprise differs from financial reporting for an established operating enterprise in regard to (more extensive) footnote disclosures only.
Choices "b", "c", and "d" are incorrect. Revenue and expense recognition principles are the same.
Rule:
Development stage enterprises should present financial statements in accordance with GAAP and make
additional disclosures such as: cumulative net losses, cumulative deficit (as part of equity), cumulative
sales and expenses (as part of the income statement), cumulative statement of cash flows and supplementary "shareholders equity."

NO.4 On January 2, 1993, Quo, Inc. hired Reed to be its controller. During the year, Reed, working closely with
Quo's president and outside accountants, made changes in accounting policies, corrected several errors
dating from 1992 and before, and instituted new accounting policies.
Quo's 1993 financial statements will be presented in comparative form with its 1992 financial statements.
This question represents one of Quo's transactions. List A represents possible clarifications of these transactions as: a change in accounting principle, a change in accounting estimate, a correction of an error in previously presented financial statements, or neither an accounting change nor an accounting
error.
Item to Be Answered
As a result of a production breakthrough, Quo determined that manufacturing equipment previously depreciated over 15 years should be depreciated over 20 years.
List A (Select one)
A. Change in accounting principal.
B. Change in accounting estimate.
C. Correction of an error in previously presented financial statements.
D. Neither an accounting change nor an accounting error.
Answer: B
Explanation:
Choice "b" is correct. Change in lives of fixed assets is a change in accounting estimate.

NO.5 The summary of significant accounting policies should disclose the:
A. Maturity dates of noncurrent debts.
B. Terms for convertible debt to be exchanged for common stock.

C. Concentration of credit risk of all financial instruments by geographical region.
D. Criteria for determining which investments are treated as cash equivalents.
Answer: D
Explanation:
Choice "d" is correct. The criteria for determining which investments are treated as cash equivalents would be part of the summary of significant accounting policies. Choice "a" is incorrect. The maturity dates of noncurrent debts are required disclosures, but are not a part of the summary of significant accounting policies. Choice "b" is incorrect. The terms for convertible debt to be exchanged for common
stock are not accounting policies; they would be disclosed separately. Choice "c" is incorrect. The concentration of credit risk of all financial instruments by geographic region may be a required segment
disclosure, especially for financial institutions. However, it would not be a part of the summary of significant accounting policies.

NO.6 Rock Co.'s financial statements had the following balances at December 31:

Extraordinary gain	$50,000
Foreign currency translation gain, net of tax	100,000
Net income	400,000
Unrealized gain on available-for-sale equity securities, net of tax	20,000

What amount should Rock report as comprehensive income for the year ended December 31?
A. $400,000
B. $420,000
C. $520,000
D. $570,000
Answer: C
Explanation:
Choice "c" is correct. Comprehensive Income includes all items included in "Net Income" plus "Other Comprehensive Income" items. Since the $50,000 extraordinary gain is already included in Net Income,
Comprehensive Income is:

Net Income	$400,000
"PUFE" adjustments:	
Foreign currency translation adj.	100,000
Unrealized gain on available-for-sale securities	20,000
	$520,000

NO.7 How should the effect of a change in accounting estimate be accounted for?
A. By restating amounts reported in financial statements of prior periods.
B. By reporting pro forma amounts for prior periods.
C. As a prior period adjustment to beginning retained earnings.
D. In the period of change and future periods if the change affects both.
Answer: D
Explanation:
Choice "d" is correct, a "change in accounting estimate" affects only the current and subsequent (future)
periods, if the change affects both. It does not affect "prior periods," nor "retained earnings." Choice

"a" is
incorrect. Restating prior years' financial statements is required when comparative financial statements
are shown for prior period adjustments of "corrections of errors," "changes in entities," and changes in
accounting principle. Choices "b" and "c" are incorrect. A "change in accounting estimate" does not affect
prior periods.

NO.8 On January 2, 1993, Quo, Inc. hired Reed to be its controller. During the year, Reed, working closely with
Quo's president and outside accountants, made changes in accounting policies, corrected several errors
dating from 1992 and before, and instituted new accounting policies.
Quo's 1993 financial statements will be presented in comparative form with its 1992 financial statements.
This question represents one of Quo's transactions. List B represents the general accounting treatment
required for these transactions. These treatments are:
. Cumulative effect approach - Include the cumulative effect of the adjustment resulting from the
accounting change or error correction in the 1993 financial statements, and do not restate the 1992
financial statements.
. Retroactive or retrospective restatement approach - Restate the 1992 financial statements and adjust
1 992 beginning retained earnings if the error or change affects a period prior to 1992.
. Prospective approach - Report 1993 and future financial statements on the new basis but do not restate
1 992 financial statements.
Item to Be Answered
Quo changed from FIFO to average cost to account for its raw materials and work in process inventories.
List B (Select one)
A. Cumulative effect approach.
B. Retroactive or retrospective restatement approach.
C. Prospective approach.
Answer: B
Explanation:
Choice "B" is correct. A change in accounting principle should be shown in the retained earnings
statement of the earliest year presented as an adjustment of the beginning balance. All prior year financial
statements are recast.

NO.9 The effect of a material transaction that is infrequent in occurrence but not unusual in nature should be
presented separately as a component of income from continuing operations when the transaction results in a:

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

A. Option A
B. Option B
C. Option C
D. Option D
Answer: A
Explanation:
Choice "a" is correct, Yes - Yes. A material transaction that is "infrequent in occurrence" but not "unusual
in nature" should be presented separately as a component of "income from continuing operations" when
the transaction results in a gain or loss.

NO.10 Which of the following should be disclosed for each reportable operating segment of an enterprise?

Profit or loss	Total assets
Yes	Yes
Yes	No
No	Yes
No	No

A. Option A
B. Option B
C. Option C
D. Option D
Answer: A
Explanation:
Choice "a" is correct. For each reportable segment of an enterprise, both profit or loss and total assets
should be disclosed. In disclosure questions, if you are not sure, disclose the most rather than the least.
Choice "b" is incorrect. For each reportable segment of an enterprise, both profit or loss and total assets
should be disclosed. Choice "c" is incorrect. For each reportable segment of an enterprise, both profit or
loss and total assets should be disclosed. Choice "d" is incorrect. For each reportable segment of an enterprise, both profit or loss and total assets should be disclosed.

NO.11 On January 2, 1993, Quo, Inc. hired Reed to be its controller. During the year, Reed, working closely with
Quo's president and outside accountants, made changes in accounting policies, corrected several errors
dating from 1992 and before, and instituted new accounting policies.
Quo's 1993 financial statements will be presented in comparative form with its 1992 financial statements.

This question represents one of Quo's transactions. List A represents possible clarifications of these transactions as: a change in accounting principle, a change in accounting estimate, a correction of an error in previously presented financial statements, or neither an accounting change nor an accounting error.
Item to Be Answered
Quo manufactures heavy equipment to customer specifications on a contract basis. On the basis that it is
preferable, accounting for these long-term contracts was switched from the completed-contract method to
the percentage-of-completion method.
List A (Select one)
A. Change in accounting principal.
B. Change in accounting estimate.
C. Correction of an error in previously presented financial statements.
D. Neither an accounting change nor an accounting error.
Answer: A
Explanation:
Choice "a" is correct. Switching from the completed-contract method of accounting to the percentage-of
completion method is a "change in accounting principle."

NO.12 In general, an enterprise preparing interim financial statements should:
A. Defer recognition of seasonal revenue.
B. Disregard permanent decreases in the market value of its inventory.
C. Allocate revenues and expenses evenly over the quarters, regardless of when they actually occurred.
D. Use the same accounting principles followed in preparing its latest annual financial statements.
Answer: D
Explanation:
Choice "d" is correct. Generally accepted accounting principles that were used in the most recent annual
report of an enterprise should be applied to interim financial statements of the current year, unless a change in accounting principle is adopted in the current year.
Choices "a", "b", and "c" are incorrect, per above.

NO.13 During 1990, Fuqua Steel Co. had the following unusual financial events occur:
. Bonds payable were retired five years before their scheduled maturity, resulting in a $260,000 gain. Fuqua has frequently retired bonds early when interest rates declined significantly.
. A steel forming segment suffered $255,000 in losses due to hurricane damage. This was the fourth similar loss sustained in a 5-year period at that location.
. A component of Fuqua's operations, steel transportation, was sold at a net loss of $350,000.
This was Fuqua's first divestiture of one of its operating segments.
Before income taxes, what amount should be disclosed as the gain (loss) from extraordinary items in 1 990?
A. $0
B. $5,000
C. $(90,000)

D. $(350,000)
Answer: A
Explanation:
Choice "a" is correct. $0. Note: The sale of the steel transportation component resulted in a loss from discontinued operations and is reported after "income from continuing operations." The steel forming
segment's hurricane damage (4th in 5 years) of $255,000 is only "unusual in nature" and does not occur
infrequently, therefore, it is not an "extraordinary item," and should be reported separately as a component of "income from continuing operations." The retirement of debt, although unusual, is not infrequent for the company; therefore, the gain does not qualify for classification as an extraordinary item
per APBO No. 30 (and SFAS No. 145).

NO.14 According to the FASB conceptual framework, the process of reporting an item in the financial statements
of an entity is:
A. Allocation.
B. Matching.
C. Realization.
D. Recognition.
Answer: D
Explanation:
Choice "d" is correct. Recognition is the process of recording an item in the financial statements of an entity. SFAC 5 para. 6 Choice "a" is incorrect. Allocation is the accounting process of assigning or distributing an amount according to a plan or a formulA. SFAC 6 para. 142 Choice "b" is incorrect. Matching of costs and revenues is simultaneous or combined recognition of the revenues and expenses
that result directly and jointly from the same transactions or other events. SFAC 6 para. 146 Choice "c" is
incorrect. Realization is the process of converting noncash resources and rights into money. SFAC 6 para.
1 43

NO.15 Conceptually, interim financial statements can be described as emphasizing:
A. Timeliness over reliability.
B. Reliability over relevance.
C. Relevance over comparability.
D. Comparability over neutrality.
Answer: A
Explanation:
Choice "a" is correct. Interim financial statements emphasize timeliness (an element of relevance) by providing financial information based on actual performance to date and estimates prior to year end. Information must be available when it is needed to be useful. Reliability is impeded by the extensive use
of estimates; however, the lag until verifiability is obtained detracts from usefulness. SFAC 2 para. 56 Choice "b" is incorrect. Relevance (particularly timeliness) of information in interim financial

statements is
emphasized more than reliability. Reliability is impeded by the extensive use of estimates in interim data.
Choice "c" is incorrect. Since comparability is a secondary quality of information, there should be no need
to trade off comparability for relevance (a primary quality). Choice "d" is incorrect. Neutrality is an element
of reliability (a primary quality of information. There should be NO need for a trade-off for comparability
over neutrality.