Interactive Developmental Mathematics 1st edition Rockswold Test Bank

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TRUE/FALSE. Write 'T' if the statement is true and 'F' if the statement is false.

1) Recognition requires the measurement of an item for inclusion in the financial statements.
Answer: True False

2) The use of historical cost, rather than liquidation value, is supported by the continuity assumption.
Answer: True False

3) The use of fair value rather than historical cost increases both the relevance and verifiability of the financial statements.
Answer: True False

4) The separate entity assumption has more validity for a larger corporation than it would for a sole proprietorship.
Answer: True False

5) The unit of measure assumption holds that all aspects of a company's business operations can be readily quantified.
Answer: True False

6) The goal of maximizing shareholder wealth is consistent with the entity concept.
Answer: True False

7) The continuity assumption holds that a business will carry on indefinitely.
Answer: True False

8) Legally, as well as for accounting statement purposes, a corporation is treated as a separate entity apart from its stockholders, whereas a partnership is treated as one entity including the owners.
Answer: True False

9) The time period concept dictates that the reporting period or fiscal period of an entity must be for 12 months.
Answer: True False

10) Under the productive capacity capital maintenance approach, a profit is assumed to have been earned only if enough financial capital has been recovered by the end of the year to enable the business to operate at the same level as at the beginning of the year.
Answer: True False

11) "Substance over form" effectively refers to Representational Faithfulness in the conceptual framework.
Answer: True False

12) The first step in choosing an accounting policy is to understand a company's primary reporting objectives.
Answer: True False

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13) The continuity assumption assumes that a company will have a perpetual life.
Answer: True False

14) Predictive value is a component of representational faithfulness.
Answer: True False

15) Equity is a residual and as such is not specifically defined in the IFRS Conceptual Framework.
Answer: True False

16) The qualitative characteristics follow the same hierarchy under both the IFRS and ASPE Conceptual Frameworks.
Answer: True False

17) Revenues must ultimately lead to cash flows in order to be recognized.
Answer: True False

18) Assuming that the continuity assumption is valid, accrual accounting income and cash based income would be expected to "even out" over the long term.
Answer: True False

19) Deferrals are required when cash flows are received before they affect the income statement, while accruals affect the income statement prior to cash being exchanged.
Answer: True False

20) The use of deferrals and accruals in accounting relates to the Time Period Assumption.
Answer: True False

21) Under IFRS, Level 1 amounts refer to quoted prices or directly observable amounts.
Answer: True False

22) Under ASPE, capital maintenance can be said to be achieved if a company has maintained or increased its productive capacity.
Answer: True False

23) Information is reliable when it is in agreement with the actual underlying transactions and events, the agreement is capable of independent verification and the information is reasonably free from error and bias.
Answer: True False

24) The going concern principal does not apply if a company is expected to be liquidated in the next 24 months.
Answer: True False

25) Relevance is of primary importance in financial reporting, whereas comparability is of secondary importance.
Answer: True False

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26) Interperiod comparability is significantly enhanced when two similar companies use the same accounting methods during a single reporting period.
Answer: True ✓ False

27) Information is neutral when it is free from bias that would lead users towards making decisions that are influenced by the way the information is measured or presented.
Answer: ✓ True False

28) Accounting transactions must always be realized prior to being recognized.
Answer: True ✓ False

29) Accounting should provide information that is useful in assessing the "value" of an entity; however, accounting information does not necessarily report the actual "value" of the entity.
Answer: ✓ True False

30) The nominal dollar capital maintenance approach is the mostly widely used application of the stable currency assumption in North American practice.
Answer: ✓ True False

31) The nominal dollar capital maintenance approach implicitly recognizes that inflation is under control, and thus ignores inflation in the preparation of financial statements.
Answer: ✓ True False

32) The constant dollar capital maintenance approach adjusts for the decline in the asset's productive capacity when reporting earnings.
Answer: True ✓ False

33) The nominal dollar capital maintenance approach adjusts for the replacement cost of the assets when reporting earnings.
Answer: True ✓ False

34) At times, reliability must be sacrificed in order to enhance the relevance of accounting information.
Answer: ✓ True False

35) To Recording periodic depreciation on assets such as buildings or machinery is an application of the matching principle.
Answer: ✓ True False

36) The matching concept is the name applied to the process of associating expenses with revenues.
Answer: ✓ True False

37) An example of the full disclosure principle would be a firm signing a major contract in November to construct custom machinery for a client. Work in the current year is nil, yet the notes to the firm's financial statements discuss the nature and dollar amount of the contract.
Answer: ✓ True False

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38) The understandability concept states that the information contained in financial statements should be understandable to persons who have a reasonable understanding of business and economic conditions and are willing to study the information with reasonable diligence.
Answer: True False

39) One of the objectives of financial reporting is to help users assess the amounts, timing and uncertainty of prospective cash flows of the enterprise.
Answer: True False

40) The continuity assumption holds that the entity will continue in business for the foreseeable future but it does not mean that it will be a going concern forever.
Answer: True False

41) Revenue is recognized when service is rendered and collection is probable.
Answer: True False

42) Materiality is one of the underlying constraints in the application of the IFRS conceptual framework.
Answer: True False

43) Under IFRS, a change in accounting policy must result in information that is more reliable and relevant.
Answer: True False

44) Under IFRS 13, Level 3 inputs are deemed to be more reliable than Level 2 inputs.
Answer: True False

45) In order to recognize sales revenue, collection of cash from the buyer is not necessary; however, collection must be reasonably assured.
Answer: True False

46) No revenue whatsoever from the performance of a service can be recognized until all of the service has been performed.
Answer: True False

47) Warranty expense on goods sold should be recognized in the period of the sale, even though the costs to fulfill warranty claims will not be incurred until two or three years later.
Answer: True False

48) The full disclosure principle asserts that the financial reports of a business enterprise should disclose all reliable information relating to its economic affairs.
Answer: True False

49) Relevance and representation faithfulness are the fundamental qualities under IFRS.
Answer: True False

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50) The separate entity assumption applies only to legally separate entities such as corporations; it does not apply to proprietorships or other unincorporated businesses.
Answer: True False

51) Under IFRS 13, a publicly quoted share price would be an example of a Level 1 Input.
Answer: True False

52) Comparability is an enhancing quality under IFRS and ASPE.
Answer: True False

53) The cost-benefit trade-off is a persuasive constraint under both IFRS and ASPE.
Answer: True False

54) Materiality is a component of representational faithfulness under IFRS.
Answer: True False

55) Verifiability focuses on the correct application of a basis of measurement rather than its appropriateness.
Answer: True False

56) Under IFRS and ASPE, both assets and liabilities are mostly arises from past events.
Answer: True False

57) The quality of information that gives assurance that it is reasonably free of error and bias and is a faithful representation is relevance.
Answer: True False

58) A furniture builder accepts a purchase order from a client to build a customized dresser. The acceptance of this contract on that date is executory in nature and the builder must thus record a liability on that date.
Answer: True False

59) Comparability is sometimes sacrificed for consistency.
Answer: True False

60) In classifying the elements of financial statements, the primary distinction between revenues and gains is the materiality of the amounts involved.
Answer: True False

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MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

61) The going concern or continuity assumption is critical to financial accounting. The assumption
A) Supports the use of historical cost valuation for assets rather than market values.
B) Means that a corporation has a definite ending date.
C) Requires that we immediately expense prepaid accounts because they do not represent a future cash inflow.
D) Is always maintained for all firms for all years.
Answer: A

62) The objective of financial reporting is:
A) To provide information useful for decision making by investors and creditors.
B) To provide the total market value of its common stock.
C) To require all companies to comply with GAAP.
D) To provide the market value of a firm at a point in time.
Answer: A

63) A firm's accounting policy is to immediately expense the cost of metal wastebaskets it purchases for use by its employees at their desks. The total cost of wastebaskets in any year is $1,000 and the firm has $6 billion in total assets. The firm expects the wastebaskets to last indefinitely. The firm
A) Is violating GAAP
B) Is invoking the conservatism constraint
C) Is violating the relevance principle
D) Is invoking the materiality constraint
E) None of these answers are correct.
Answer: D

64) The sales manager of a firm has the use of a blue company-owned automobile to use to visit potential customers. The sales manager also owns her own identical car except that it is red. The manager paid for the red car with funds earned from her employment as sales manager. The firm will report the cost of the blue auto in its balance sheet, but not the red auto. This is an example of:
A) Reliability
B) Separate entity
C) Matching
D) Going concern
E) None of these answers are correct.
Answer: B

65) Preparation of financial statements with adequate notes is primarily based on the:
A) separate entity assumption.
B) cost principle.
C) cost/benefit constraint.
D) reliability quality.
E) full-disclosure principle.
Answer: E

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66) Which of the following accounting concepts best justifies the use of accruals and deferrals?
A) Cost/benefit constraint
B) Continuity assumption
C) Materiality constraint
D) Unit-of-measure assumption

Answer: B

67) Accounting traditionally has been influenced by conservatism because of the:
A) probability of undetected errors in the financial statements.
B) large number of transactions recorded in any one period.
C) difficulty in making certain calculations.
D) inherent uncertainties of many accounting measurements.
E) difficulty in measuring net income on the accrual basis.

Answer: D

68) The organization created to develop accounting standards in Canada, the AcSB, is LEAST concerned with:
A) reporting financial position.
B) reported earnings.
C) reported comparability of results.
D) reported cash flows.
E) all of these answers are correct.

Answer: C

69) The continuity assumption is the basis for the rule that:
A) the cost of operational assets should be allocated to expense systematically and rationally over their useful lives.
B) the cost of installing a machine should not be included in the recorded cost of the machine, but rather expensed immediately.
C) treasury stock should not be reported in the balance sheet as an asset.
D) the income statement should not include material gains and losses that are both unusual and infrequent.

Answer: A

70) S Corporation offered to issue 5,000 shares of its no par value common shares to another company in exchange for a building at a time when there were 1,000,000 shares already outstanding and were selling for $02-04 Apply the fundamental and enhancing qualities and pervasive constraints of financial reporting..00 per share at the time. The owner of the building had the opportunity to sell it to a competing buyer for $26,000. However, because the seller wanted the S Corporation shares, S's offer was accepted. At what amount should the building be reported in S's financial statements?
A) $26,000
B) $20,000
C) $16,000
D) $10,000

Answer: B

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71) C Corporation exchanged 20,000 shares of its nonconvertible preferred shares for land owned by B Corporation. A competing buyer previously had offered $150,000 cash for the land. Because of tax consequences, the cash offer was not accepted and the lot was exchanged for the shares. C Corporation previously had sold only 100 shares of its preferred shares at $9 per share several months ago. Based on the cost principle, at what amount should the land be reported on C's financial statements?

A) $150,000 B) $160,000 C) $165,000 D) $180,000

Answer: A

72) The list price of a new van was $30,000 at a local car dealership. However, a customer convinced the dealer to sell the van for $25,000 (the van had cost the dealer $20,000 one year earlier). The van would cost the dealer $24,000 today. Inflation is 5% per year. The amount of profit that would be recognized by the dealer as a result of the sale using the nominal dollar approach is:

A) $6,000 B) $5,000 C) $2,500 D) $10,000

Answer: B

73) The list price of a new van was $30,000 at a local car dealership. However, a customer convinced the dealer to sell the van for $25,000 (the van had cost the dealer $20,000 one year earlier). The van would cost the dealer $24,000 today. Inflation is 5% per year. The amount of profit that would be recognized by the dealer as a result of the sale using the constant dollar financial capital maintenance approach is:

A) $5,000 B) $9,000 C) $4,000 D) $10,000

Answer: C

74) The list price of a new van was $30,000 at a local car dealership. However, a customer convinced the dealer to sell the van for $25,000 (the van had cost the dealer $20,000 one year earlier). The van would cost the dealer $24,000 today. Inflation is 5% per year. The amount of profit that would be recognized by the dealer as a result of the sale using the physical capital maintenance approach is:

A) $6,000 B) $5,000 C) $2,500 D) $1,000

Answer: D

75) Accounting information is considered to be relevant when it

A) is verifiable and neutral.

B) can be depended on to represent the economic conditions and events that it is intended to represent.

C) is understandable by reasonably informed users of accounting information.

D) is capable of making a difference to a decision-maker.

Answer: D

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76) The quality of information that gives assurance that it is reasonably free of error and bias and is a faithful representation is

A) neutrality.
B) reliability.
C) relevance.
D) verifiability.
E) None of these answers are correct.

Answer: D

77) Timeliness is an ingredient of the qualitative criteria of

	Relevance	**Reliability**
1	Yes	Yes
2	No	Yes
3	Yes	No
4	No	No

A) Choice 1 B) Choice 2 C) Choice 3 D) Choice 4

Answer: C

78) Verifiability is an ingredient of the qualitative criteria of

	Relevance	**Reliability**
1	Yes	No
2	Yes	Yes
3	No	No
4	No	Yes

A) Choice 1 B) Choice 2 C) Choice 3 D) Choice 4

Answer: D

79) Neutrality is an ingredient of the qualitative criteria of

	Relevance	**Reliability**
1	Yes	Yes
2	No	Yes
3	Yes	No
4	No	No

A) Choice 1 B) Choice 2 C) Choice 3 D) Choice 4

Answer: B

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80) Predictive value is an ingredient of the qualitative criteria of

	Relevance	Reliability
1	Yes	No
2	Yes	Yes
3	No	No
4	No	Yes

A) Choice 1 B) Choice 2 C) Choice 3 D) Choice 4

Answer: A

81) Representational faithfulness is an ingredient of the qualitative criteria of

	Relevance	Reliability
1	Yes	Yes
2	No	Yes
3	Yes	No
4	No	No

A) Choice 1 B) Choice 2 C) Choice 3 D) Choice 4

Answer: C

82) A primary objective of financial reporting is to:

A) assist suppliers in determining an appropriate discount to offer a particular company.

B) enable banks to determine an appropriate interest rate for their commercial loans.

C) assist investors in analyzing the economy.

D) assist investors in predicting prospective cash flows.

Answer: D

83) If, in year 1, a company used LIFO; year 2, FIFO; and in year 3, moving average cost for inventory valuation, which of the following assumptions, constraints, or principles would be violated:

A) time period.

B) consistency.

C) materiality.

D) matching.

E) cost.

Answer: B

84) Which of the following qualities does the cost principle primarily support?

A) Verifiability B) Conservatism C) Predictive value D) Timeliness

Answer: A

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85) The inclusion of notes and supporting schedules in the financial statements reflect application of the:
A) comparability characteristic.
B) relevance quality.
C) industry peculiarities constraint.
D) time period assumption.
E) full-disclosure principle.
Answer: E

86) Certain costs of doing business are capitalized when incurred and then amortized over subsequent accounting periods to:
A) match the costs incurred with revenues earned.
B) conform to the comparability characteristic.
C) reduce the income tax.
D) aid management in decision-making.
E) conform to the conservatism constraint.
Answer: A

87) Adjusting entries are needed because an entity:
A) uses the accrual basis of accounting.
B) has earned revenue during the period by selling products from its central operations.
C) has expenses.
D) uses the cash basis of accounting rather than the accrual basis.
Answer: A

88) A large international corporation immediately expenses the $50 cost of a small item of office equipment. This is an example of:
A) conservatism.
B) reliability.
C) materiality.
D) an accounting error.
E) None of these answers are correct.
Answer: C

89) When an $30 asset with a six-year estimated useful life is recorded as an expense at the date of purchase, this is an application of the:
A) materiality constraint.
B) unit-of-measure assumption.
C) cost principle.
D) matching principle.
E) None of these answers are correct.
Answer: A

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90) Which of the following distinguishes the personal transactions of business owners from business transactions?

A) Materiality constraint
B) Full-disclosure principle
C) Unit-of-measure assumption
D) Separate entity assumption

Answer: D

91) A corporation needed a new warehouse; a contractor quoted a $250,000 price to construct it. The corporation believed that it could build the warehouse for $215,000 and decided to use company employees to construct the warehouse. The final construction cost incurred by the corporation was $240,000 but the asset was recorded at $250,000. This is in violation of the:

A) revenue recognition principle.
B) time period assumption.
C) cost principle.
D) matching principle.
E) None of these answers are correct.

Answer: C

92) Which of the following is the incorrect basis for recognizing the expense indicated?

A) Sales commissions expense on the basis of relationship with sales.
B) Amortization expense on the basis of time.
C) Cost of goods sold expense on a subjective or arbitrary basis.
D) Administrative salaries expense recognized as incurred.

Answer: C

93) When a corporation buys a portion of its own common shares, the recording must conform to the:

A) matching principle.
B) revenue recognition principle.
C) cost principle.
D) accrual principle.

Answer: C

94) A corporation reports the sale of some of its shares to a shareholder in its financial statements, and the shareholder reports the same transaction as an investment. Therefore,

A) no accounting concept has been violated.
B) the double entry accounting concept has been violated.
C) the separate entity assumption has been violated.
D) the revenue recognition principle has been violated.

Answer: A

95) The separate entity assumption:

A) is not applicable to an unincorporated business.
B) requires periodic income measurement.
C) is applicable to both incorporated and unincorporated businesses.
D) recognizes the legal nature of a business organization.

Answer: C

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96) An accounting error may be all of the following except:

A) An inaccurate estimate made in good faith. B) A mistake.

C) intentional. D) unintentional.

Answer: D

97) Under which of the following will revenues and expenses most likely be reported in the period they are earned or incurred?

A) Accrual basis accounting

B) Single entry accounting

C) Cash basis accounting

D) A combination of accrual and cash basis accounting

Answer: A

98) Estimating bad debt expense for the period is based primarily on the:

A) full-disclosure principle.

B) matching principle.

C) revenue recognition principle.

D) cost principle.

E) conservatism constraint.

Answer: B

99) A corporation made the following entries:

A	Prepaid insurance	900	
	Cash		900
B	Depreciation expense	10,000	
	Accumulated depreciation		10,000
C	Wages payable	3,000	
	Cash		3,000
D	Inventory of Merchandise	4,000	
	Accounts payable		4,000

Which entry must have been made as a direct result of the matching principle?

A) A B) B C) C D) D

Answer: B

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100) The assumption that dollars will buy the same quantity of goods and services today as they would have five years ago is the:
A) time period assumption.
B) separate entity assumption.
C) continuity assumption.
D) revenue recognition principle.
E) unit-of-measure assumption.
Answer: E

101) Revenues and expenses often are recognized in income statement accounts even though no cash has been received or paid. This is primarily a result of applying the:
A) revenue recognition principle.
B) full-disclosure principle.
C) accrual basis of accounting.
D) continuity assumption.
Answer: C

102) The underlying assumptions of accounting include all of the following except:
A) separate entity.
B) continuity.
C) conservatism.
D) unit-of-measure.
E) time period.
Answer: C

103) The measurement conventions of accounting include all of the following except:
A) revenue recognition.
B) matching.
C) continuity.
D) historical cost.
E) full-disclosure.
Answer: C

104) The implementation constraints include all of the following except:
A) separate entity.
B) conservatism.
C) cost/benefit.
D) materiality.
Answer: A

105) The underlying concept that the value of accounting information must exceed the expenditures incurred to provide it is called the:
A) conservatism.
B) full-disclosure principle.
C) substance over form.
D) cost/benefit implementation constraint.
Answer: D

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106) The materiality constraint:
A) is the only defence for gross negligence by an independent accountant.
B) does not necessarily imply that an immaterial amount can be ignored for accounting purposes.
C) is applicable only for low-cost items that cost less than, say, $500.
D) is only relevant when preparing annual financial statements as opposed to quarterly statements.
Answer: B

107) The use of deferrals and accruals is a direct result of the:
A) cost/benefit constraint.
B) separate entity assumption.
C) unit-of-measure assumption.
D) time period assumption.
Answer: D

108) An item is not material if:
A) The accounting equation (A = L + OE) does not include the item.
B) Its omission will not influence the judgement of a reasonable person.
C) It decreases the qualitative usefulness of the financial statements, but not the quantitative usefulness.
D) Its cost is less than $25.
Answer: B

109) Financial information exhibits the characteristic of consistency when
A) Accounting entities give "accountable" events the same accounting treatment from period to period.
B) accounting procedures are adopted which give a consistent rate of net income.
C) Unusual or infrequent gains and losses are not included on the income statement.
D) Expenses are reported as charges against revenue in the period in which they are paid.
Answer: A

110) Valuing assets at their liquidation values rather than their cost is inconsistent with the
A) time period assumption.
B) historical cost principle.
C) matching principle.
D) materiality constraint.
Answer: B

111) Which of the following is NOT a time when revenue may be recognized?
A) At time of sale of goods.
B) Sale of Property of a manufacturing company.
C) During production of goods.
D) At receipt of cash from sale of goods.
Answer: B

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112) Application of the full disclosure principle
A) requires that the financial statements be consistent and comparable.
B) is violated when important financial information is buried in the notes to the financial statements.
C) is demonstrated by the use of supplementary information presenting the effects of changing prices.
D) is theoretically desirable but not practical because the costs of complete disclosure exceed the benefits.
Answer: C

113) Which of the following relates to both relevance and reliability?
A) Predictive value.
B) Cost-benefit constraint.
C) Representational faithfulness.
D) Verifiability.
E) None of these answers are correct.
Answer: D

114) Charging off the cost of a calculator with an estimated useful life of 10 years as an expense of the period when purchased is an example of the application of the
A) materiality constraint.
B) historical cost principle.
C) matching principle.
D) consistency characteristic.
Answer: A

115) Which of the following accounting concepts states that before a transaction is recorded, sufficient evidence must exist to allow two or more knowledgeable individuals to reach essentially the same conclusion about the transaction?
A) Materiality constraint
B) Separate entity assumption
C) Cost principle
D) Continuity assumption
E) Reliability quality
Answer: E

116) The recognition of periodic amortization expense on company-owned automobiles requires estimating both salvage or residual value, and the useful life of the vehicles. The use of estimates in this case is an example of:
A) Invoking the materiality constraint rather than the cost benefit constraint
B) Conservatism
C) Providing relevant data at the expense of reliability
D) Maintaining consistency
E) None of these answers are correct.
Answer: C

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117) A firm does not know exactly how long its equipment will last. The firm decides to use shorter rather than longer useful lives for amortizing the equipment. This is an example of:
A) Materiality
B) Conservatism
C) Reliability
D) Unit of measure
E) None of these answers are correct.
Answer: B

118) Revenue is recognized when
A) The contract is signed
B) When the customer places the order
C) Service is rendered
D) It is collected in cash
E) Service is rendered and collection is probable
Answer: E

119) The matching concept
A) Treats all costs as being directly related to revenue generation
B) Treats all costs as expenses
C) Requires that a debit is matched or posted for every credit
D) Is the name applied to the process of associating expenses with revenues
Answer: D

120) A firm signs a major contract in December to construct custom machinery for a client. No work is begun the current year, yet the notes to the firm's financial statements discuss the nature and dollar amount of the contract. This is an example of
A) Historical cost
B) Conservatism
C) Full disclosure
D) Reliability
E) None of these answers are correct.
Answer: C

121) A firm purchased $40,000 of supplies in its first year of operations but used up only $30,000 of the supplies during the year. Therefore:
A) Under the matching concept, the firm should report $30,000 of expense
B) Because the firm is a going concern, the firm should record $40,000 of supplies in the balance sheet at the end of the year
C) Under the relevance characteristic, the firm should expense $40,000
D) Under the materiality constraint, it makes no difference what the firm does with respect to accounting for supplies
Answer: A

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122) J. Green is the sole owner and manager of the ABC Lawn and Grass Service. Green purchased a new station wagon only for personal use. Green uses a dump truck in the business. Which of the following assumptions, principles, or constraints would be violated if Green recorded the cost of the station wagon as an asset of the business?

A) Continuity assumption
B) Conservatism constraint
C) Materiality constraint
D) Full-disclosure principle
E) Separate entity assumption

Answer: E

123) Recording periodic depreciation on assets such as buildings or machinery is an application of the:

A) matching principle.
B) cost principle.
C) materiality constraint.
D) unit-of-measure assumption.
E) conservatism constraint.

Answer: A

124) When assets are acquired, they should be recorded in the accounts in conformity with the:

A) cost principle.
B) separate entity assumption.
C) materiality constraint.
D) matching principle.
E) full-disclosure principle.

Answer: A

125) Under ASPE (Private Entity GAAP), which of the following is an ingredient of reliability?

A) Materiality
B) Predictive value
C) Understandability
D) Verifiability

Answer: D

126) Under ASPE, feedback value is an ingredient of:

	Relevance	**Reliability**
1	Yes	Yes
2	Yes	No
3	No	No
4	No	Yes

A) Choice 1
B) Choice 2
C) Choice 3
D) Choice 4

Answer: B

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127) The information provided by financial reporting pertains to:
A) individual business enterprises, industries and the economy as a whole, rather than to members of society as consumers.
B) individual business enterprises and industries rather than to the economy as a whole or to members of society as consumers.
C) individual business enterprises and the economy as a whole, rather than to industries or to members of society as consumers.
D) individual business enterprises, rather than to industries of the economy as a whole or to members of society as consumers.
Answer: D

128) Relevance is sometimes sacrificed for:
A) Comparability B) Conservatism. C) Objectivity. D) Reliability.
Answer: B

129) If accounting information is timely and has predictive and feedback value, then it can be characterized as:
A) Relevant. B) Reliable. C) Qualitative. D) Verifiable.
Answer: A

130) The primary qualitative criteria of accounting information include which of the following:
A) Understandability. B) Relevance.
C) Comparability (including consistency). D) Materiality.
Answer: B

131) Relevance is not a function of:
A) timeliness. B) feedback value. C) verifiability. D) predictive value.
Answer: C

132) Accrual accounting is essentially an application of:
A) the historical cost principle. B) the materiality constraint.
C) the conservatism principle. D) the matching principle.
Answer: D

133) Increases in equity (net assets) from peripheral or incidental transactions of an entity are called:
A) revenues. B) net income.
C) gains. D) economic benefits.
Answer: C

134) At the date of purchase of a service which is not immediately used up, the cost of such unused service is a(n):
A) asset. B) liability. C) expense. D) revenue.
Answer: A

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ESSAY. Write your answer in the space provided or on a separate sheet of paper.

135) State the accounting assumption, principle, information characteristic, or constraint that is most applicable in the following cases.

1. All significant post-balance sheet events are reported.

_____

2. Personal transactions of the proprietor are distinguished from business transactions.

_____

3. Goodwill is capitalised and amortised over the periods benefited.

_____

4. Assuming that dollars today will buy as much as 10 years ago.

_____

5. Rent paid in advance is recorded as prepaid rent.

_____

6. Financial statements are prepared each year.

_____

7. All payments less than $25 are expensed as incurred. (Do not use conservatism.)

_____

8. The company employs the same inventory valuation method from period to period. _____

Answer: 1. Full disclosure principle.
2. Separate entity assumption.
3. Matching principle.
4. Monetary unit assumption.
5. Matching principle.
6. Time period assumption.
7. Materiality constraint.
8. Consistency characteristic.

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136) State the accounting assumption, principle, information characteristic or constraint that is most applicable:

1. An officer of Nanuck Inc. purchased a new home computer for personal use with company money, charging miscellaneous expense.

_____

2. A machine, which cost $60,000, is reported at its current market value of $90,000.

_____

3. Nanuck Inc. decides to establish a large loss and related liability this year because of the possibility that it may lose a pending patent infringement lawsuit. The possibility of loss is considered remote by its lawyers.

_____

4. Because the company's income is low this year, a switch from accelerated depreciation to straight-line depreciation is made this year.

_____

5. The president of Nanuck Inc. believes it is foolish to report financial information on a yearly basis. Instead, the president believes that financial information should be disclosed only when significant new information is available related to the company's operations. _____

Answer: 1. Separate entity.
2. Historical cost
3. Matching (also, conservatism)
4. Consistency.
5. Time period

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137) Fill in the blanks below with the accounting principle, assumption, or related item that BEST completes each sentence.

1. Recognition of revenue at the end of production is an allowable exception to the _____ principle.
2. Parenthetical balance sheet disclosure of the inventory method utilised by a particular company is an application of the _____ principle.
3. Corporations must prepare accounting reports at least yearly due to the _____ assumption.
4. Some costs, which give rise to future benefits cannot be directly associated with the revenues they generate. Such costs are allocated in a _____ and _____ manner to the periods expected to benefit from the cost.
5. _____ would allow the expensing of all repair tools when purchased, even though they have ar estimated life of 3 years.
6. The _____ characteristic requires that the same accounting method be used from one accounting period to the next, unless it becomes evident that an alternative method will bring about a better description of a firm's financial situation.
7. _____ and _____ are the two primary qualities that make accounting information useful fo decision making.
8. Information which helps users confirm or correct prior expectations has _____.
9. _____ enables users to identify the real similarities and differences in economic phenomena because the information has been measured and reported in a similar manner for different enterprises

Answer: 1. revenue realisation
2. full disclosure
3. time period
4. rational; systematic
5. materiality convention
6. consistency
7. relevance, reliability
8. feedback value
9. comparability

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138) Explain how the continuity assumption and the historical cost principle are related.

Answer: Expenses, a component of earnings, are measured in terms of the historical cost of resources (assets) consumed or used in producing revenue because, under the continuity assumption, there is no assumption that the assets used in operations will be sold. Using historical cost allows an evaluation of how management created value with the assets entrusted to them, measured at the actual cost of those resources. Thus, income reflects the excess of revenues ov the historical cost, rather than market value, of the resources used.
An alternative approach to earnings measurement, not supported by the continuity assumption, would employ market values of revenues and costs (expenses) to determine an "opportunity" cost measure of earnings.
The continuity assumption also supports the inclusion of certain costs in assets used in operations, as opposed to immediate expensing of those costs, even though there is no expectation that such costs will be recouped on sale of the asset. The value of such operational assets is derived through use, rather than from sale, under the continuity assumption. Specific examples include installation costs of equipment, and many prepaid assets such as prepaid rent. In the latter example, if the firm were not a going concern, prepaid rent would not represent an asset beyond the liquidation date.

139) Stratford decided in October of the current fiscal year to start a massive advertising campaign to enhance the marketability of its product. In November, the company paid $750,000 for advertising time on a major radio chain to advertise its product during the next 12 months. The chief accountant expensed the $750,000 in the current fiscal year on the basis that "once the money was spent, it coulc never be recovered from the radio chain".
State whether or not you agree with the accounting treatment given to this disbursement and support your opinion with principles discussed in the chapter on the Criteria for Accounting Choices.

Answer: This treatment violates the matching principle because the revenues to be gained for the advertising campaign will only be experienced in the accounting period in which the advertising will be aired. The $750,000 disbursement should be set up as a prepaid expense to be expensed in the proportion of the advertising incurred to the total advertising contract cost.

140) ABC Inc. is being sued by a client for an alleged breach of contract. The company's lawyers are uncertain as to what the outcome of the case will be. The client is suing ABC for $500,000 plus arrearages. Should ABC record a liability on its books due to the impending litigation? Why or why not?

Answer: No. Although some might argue that not recording a liability in this case would be a violation of the conservatism principle, no liability should be recorded, as the outcome of the litigation is uncertain. Kindly recall that to qualify as liabilities obligations must require a future transfer of assets, be an unavoidable current obligation and result from a past transaction. Although the lawsuit arose as a result of ABC's actions in a prior period, there is no transfer of assets or unavoidable current obligation, since the outcome of the litigation has not yet been determined.

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141) Explain how revenues and gains are similar and how they differ.

Answer: Both revenues and gains increase net income and net assets. However, revenues arise more from a company's day-to-day operations and routine transactions (usually from the company's line of business) while gains arise from non day-to-day non routine transactions such as the sale of assets. In the latter case, a gain would arise if the company sold an asset for an amount greater than the book value of that asset.

142) A mining company with global operations sets up a mining operation in Northern Quebec. Five years later, the mine is completely depleted and the area abandoned. The company has an excellent track record, both with respect to its corporate citizenship and environmental responsibility, having always restored all mining sites to their original state, regardless of any contractual obligations. However, the company did not restore the land on its Northern Quebec mining site, citing recent cash flow issues and the absence of any written agreement to do so with the Quebec government.
The Quebec government then decides to sue the company, for damages to its land.
Do you think the Quebec government has a strong case here? Why or why not?

Answer: While there is no legal obligation for the company to restore the land, there may well be a morale (constructive) obligation to do so. For obvious reasons, the ethical thing for the company to do would be to restore the land. The Quebec government may argue that they granted the company mining rights because they had a reasonable expectation that the company would restore the land since it had always done so in the past. Indeed, the Quebec government may have a strong case here. The company should restore the land, and should accrue a liability for its best estimate of the cost of doing so. Failure to do so would compromise the representational faithfulness of the company's statements by understating its liabilities. Even if the company refused to voluntarily restore the land, a judge would likely side with the Quebec government here.
Note that IFRS requires the recognition of constructive obligations such as these when they are likely and measurable, in addition to recognizing legal obligations. ASPE is less specific, recognition of legal obligations only.

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