Intermediate Accounting 3rd edition Gordon Test Bank

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Intermediate Accounting, 3e **(Gordon/Raedy/Sannella)**
Chapter 1 The Financial Reporting Environment

1.1 Overview of Financial Reporting

1) The financial reporting process generates three basic financial statements.
Answer: FALSE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

2) The demand for financial information is based on market participant demand.
Answer: TRUE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

3) Managers of economic entities are best considered to be users of financial information.
Answer: FALSE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

4) Managers of economic entities are best considered to be preparers of financial information.
Answer: TRUE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

5) The Securities and Exchange Commission (SEC) regulates financial reporting for publicly traded companies.
Answer: TRUE
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

6) The FASB gives the SEC authority to regulate accounting for publicly traded companies.
Answer: FALSE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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7) The Public Company Accounting Oversight Board (PCAOB) sets financial accounting standards and oversees the audits of public companies in the United States.
Answer: FALSE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

8) Financial accounting standards influence the behavior of managers and other internal users.
Answer: TRUE
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

9) Theories and procedures that evolve as a result of lobbying from various groups are examples of proactive factors within the legal, economic, political, and social environment.
Answer: FALSE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

10) Financial information includes information that is not governed by rules set forth by the accounting standard-setting bodies.
Answer: TRUE
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

11) What is the term that describes the process of identifying, measuring, and communicating financial information about an economic entity to various user groups?
A) financial reporting
B) accounting standard setting
C) financial statement
D) financial accounting
Answer: D
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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12) Which element of financial accounting involves identifying the individuals who demand financial information?
A) financial information
B) economic entity
C) user groups
D) legal, economic, political, and social environment
Answer: C
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

13) Which of the following is *not* one of the four basic financial statements?
A) balance sheet
B) trial balance
C) cash flows statement
D) statement of comprehensive income
Answer: B
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

14) Which organization is responsible for promulgating U.S. GAAP?
A) Financial Accounting Standards Board
B) Public Company Accounting Oversight Board
C) International Accounting Standards Board
D) Securities and Exchange Commission
Answer: A
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

15) Which organization is responsible for setting auditing standards and overseeing the audits of public companies in the United States?
A) Financial Accounting Standards Board
B) Public Company Accounting Oversight Board
C) American Institute of Certified Public Accountants
D) Securities and Exchange Commission
Answer: B
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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16) Which organization prepares and grades the Uniform CPA Examination?
A) Financial Accounting Standards Board
B) Public Company Accounting Oversight Board
C) American Institute of Certified Public Accountants
D) International Accounting Standards Board
Answer: C
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

17) Which of the following user groups consists of individuals that provide guidance to others in making investment and credit decisions?
A) financial analysts
B) equity investors
C) creditors
D) suppliers
Answer: A
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

18) Which of the following user groups consists of individuals who expect to receive a return on their investment?
A) employees
B) equity investors
C) creditors
D) suppliers and customers
Answer: B
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

19) Which of the following user groups consist of companies that analyze financial information to identify the reporting entity's objectives, assumptions, overall business strategy, and capabilities?
A) competitors
B) creditors and other debt investors
C) employees and labor unions
D) suppliers and customers
Answer: A
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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20) Which party involved in the financial reporting process provides assurance that the financial statements prepared by management fairly present the financial position and performance of the company?
A) standard setters
B) regulators
C) internal auditors
D) external auditors
Answer: D
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

21) Which regulatory body sets auditing standards and oversees the audits of public companies in the United States?
A) Public Company Accounting Oversight Board (PCAOB)
B) Financial Accounting Standards Board (FASB)
C) American Institute of Certified Public Accountants (AICPA)
D) Securities and Exchange Commission (SEC)
Answer: A
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

22) Which of the following types of information would be categorized as financial information?
A) asset values governed by accounting standards
B) footnote disclosures in annual reports
C) auditor's report
D) all of the above
Answer: D
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

23) Equity investors include all but which of the following?
A) partners
B) shareholders
C) bondholders
D) sole proprietor
Answer: C
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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24) What group or organization both protects investors and oversees the accounting standard-setting process in the United States?
A) public accounting firms
B) American Institute of Public Accountants
C) United States Securities and Exchange Commission
D) Financial Accounting Standards Board
Answer: C
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

25) _____ is the process of analyzing large data sets in order to draw useful conclusions.
A) Technology Innovation
B) Financial Reporting
C) Data Analytics
D) Data Capture
Answer: C
Diff: 1
Objective: 1.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

26) How does accounting help in the capital allocation process?
Answer: Financial accounting provides information that enables users to evaluate economic entities and make efficient resource allocation decisions based on the risks and returns of a particular investment. This process directs capital flows to their most productive uses. The notion of "efficient and effective" allocation of capital helps drive capitalist economies and societies to greater standards of living. To provide unreliable and irrelevant information leads to poor capital allocation which adversely affects the securities market. An inefficient and wasteful allocation would reward poorly run entities until they ultimately flounder or go bust.
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

27) In what ways does accounting information proactively interact with its environment?
Answer: Financial accounting is proactive in that it can change or influence its environment by providing feedback information that is used by organizations and individuals to reshape the economy. Accounting information is used to efficiently allocate capital resources throughout the economy. Accounting standards can also influence managerial behavior.
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

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28) What is meant by general-purpose financial statements?
Answer: Published financial statements are called *general-purpose financial statements* because they provide information to a wide spectrum of user groups: investors, creditors, financial analysts, customers, employees, competitors, suppliers, unions, and government agencies. Although considered general purpose, most financial information is provided to satisfy users with limited ability or authority to obtain additional information, which includes investors and creditors.
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

29) Define data analytics and explain how it can be used in financial reporting.
Answer: Data analytics is the process of analyzing large data sets to draw useful conclusions. It involves converting raw data into useful knowledge. Data analytics is playing an increasingly important role in the accounting profession. In financial reporting, we can use data analytics to improve the quality of our estimates and valuations. Auditors are using it to increase the quality and accuracy of the audit.
Diff: 2
Objective: 1.1
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

1.2 Role of Standard Setters

1) *IFRS* refers to generally accepted accounting standards that apply globally.
Answer: TRUE
Diff: 1
Objective: 1.2
IFRS/GAAP: IFRS
AACSB: Application of knowledge

2) Standard setters develop accounting standards based on natural economic laws.
Answer: FALSE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

3) The FASB and the IFRS have been working together to converge U.S. and international standards to and have eliminated most differences.
Answer: FALSE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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4) The FASB promulgates accounting standards in the U.S. and the International Accounting Standards Board (IASB) issues international accounting standards.
Answer: TRUE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

5) Accountants in the United States do not need to learn international accounting standards.
Answer: FALSE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

6) The SEC permits the use of IFRS-based financial statements by international companies with shares trading on U.S. stock exchanges.
Answer: TRUE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

7) When accountants work on the financial statements of U.S. companies with foreign subsidiaries prepared under IFRS in the home countries, the accountants do not convert the subsidiaries' financial statements to U.S. GAAP.
Answer: FALSE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

8) The American Institute of Certified Public Accountants tests IFRS on the uniform CPA exam.
Answer: TRUE
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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9) Which of the following statements correctly identifies accounting standard setters?
A) The AICPA promulgates accounting standards in the U.S. and the IFRS issues international accounting standards.
B) The AICPA promulgates accounting standards in the U.S. and the IASB issues international accounting standards.
C) The FASB promulgates accounting standards in the U.S. and the IFRS issues international accounting standards.
D) The FASB promulgates accounting standards in the U.S. and the IASB issues international accounting standards.
Answer: D
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

10) Which of the following statements is *false*?
A) The SEC permits the use of IFRS-based financial statements by international companies with shares trading on U.S. stock exchanges.
B) Non-U.S. companies operate in the United States but prepare their financial statements using IFRS.
C) Accountants must convert to U.S. GAAP the IFRS financial statements of foreign subsidiaries that belong to U.S. companies.
D) The accounting profession has determined that a working knowledge of IFRS is not important for accountants working in the United States.
Answer: D
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

11) Which of the following is *not* a reason why an accountant in the United States should learn international accounting standards?
A) The United States has plans to fully adopt IFRS in the near future.
B) The SEC permits the use of IFRS-based financial statements by international companies with shares trading on the U.S. stock exchanges.
C) An accountant may work for, or assist, a foreign company that operates in the U.S. and uses IFRS for financial reporting.
D) U.S. companies operate subsidiaries outside of the United States which report under IFRS in their home countries.
Answer: A
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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12) Accounting standards setters do which of the following?
A) protect investors and creditors
B) develop concepts, rules, and guidelines for financial reporting
C) assure transparent and truthful reporting and guarantee the efficient functioning of the capital markets
D) prosecute violators of their rules and guidelines so as to maintain the public trust and to ensure the efficient functioning of capital markets
Answer: B
Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

13) List four reasons why it is important for an accountant in the United States to learn international accounting standards.
Answer:
- U.S. companies operate subsidiaries outside of the United States.
- Non-U.S. companies operate in the United States and prepare their financial statements using IFRS.
- The SEC permits the use of IFRS-based financial statements by international companies with shares trading on U.S. stock exchanges.
- U.S. accountants and auditors need a working knowledge of IFRS to implement global standards in companies and perform audits.
- Many U.S. accountants now spend time working outside of the United States.
- The accounting profession has determined that a working knowledge of IFRS is important for today's accountant.

Diff: 1
Objective: 1.2
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

1.3 The Standard-Setting Process

1) The U.S. Congress has given the Securities and Exchange Commission the power to promulgate accounting standards for all publicly traded firms.
Answer: TRUE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

2) Accounting standard setting began in the United States with the 1934 Securities Exchange Act.
Answer: TRUE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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3) The Securities and Exchange Commission currently delegates its standard-setting power to the AICPA, a private sector organization.
Answer: FALSE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

4) Official U.S. GAAP consist of the bulletins, opinions, and statements issued by the CAP, the APB, and the FASB.
Answer: FALSE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

5) The FASB Accounting Standards Codification is the single source of GAAP in the United States.
Answer: TRUE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

6) Both financial and governmental accounting standards are under the auspices of the Financial Accounting Foundation.
Answer: TRUE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

7) The FASB is a subcommittee of the AICPA.
Answer: FALSE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

8) The FAF is financed primarily by funds from the Public Company Accounting Oversight Board which assesses fees against companies that issue equity securities.
Answer: TRUE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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9) The Private Company Council has authority to make the final decision about changing U.S. GAAP for private companies.
Answer: FALSE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

10) Both FASB and IASB, through their standard-setting process, require a post-implementation review of each new standard.
Answer: FALSE
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

11) Which of the following is *not* true of FASB?
A) The FASB is a full-time board of seven members.
B) Board members must sever all relationships with outside entities.
C) Board members must be CPAs.
D) The FASB is not a subcommittee of the AICPA.
Answer: C
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

12) Currently, what is the single source of generally accepted accounting principles in the United States?
A) Financial Accounting Statements
B) APB Opinions
C) Accounting Standards Codification
D) Accounting Research Bulletins
Answer: C
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

13) The _____ obtains funds primarily through the Public Company Accounting Oversight Board (PCAOB), which assesses charges known as accounting support fees against issuers of equity securities based on their market capitalization.
A) American Institute of Certified Public Accountants (AICPA)
B) Financial Accounting Foundation (FAF)
C) Securities and Exchange Commission (SEC)
D) Financial Accounting Standards Advisory Council (FASAC)
Answer: B
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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14) Which of the following organizations is responsible for setting accounting standards for state and local governments?
A) Government Issues Task Force (GITF)
B) Government Accounting Standards Board (GASB)
C) Securities and Exchange Commission (SEC)
D) Government Accounting Standards Advisory Council (GASAC)
Answer: B
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

15) During the standard-setting process, an _____ is issued by the FASB to solicit input from financial statement preparers, auditors, and other users of financial statements.
A) exposure draft
B) accounting standards update
C) accounting research bulletin
D) accounting comment letter
Answer: A
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

16) Which of the following statements about the global standard-setting structure is *false*?
A) The IFRS Interpretations Committee is similar to the EITF in the U.S.
B) The Monitoring Board was formed to enhance public accountability of the IFRS Foundation.
C) The IASB oversees the IFRS Advisory Council which advises the Monitoring Board.
D) The IFRS Foundation oversees the IASB and finances IASB operations.
Answer: C
Diff: 1
Objective: 1.3
IFRS/GAAP: IFRS
AACSB: Application of knowledge

17) In addition to the comments obtained from responses to the exposure drafts and public round tables, the U.S. standard setting process relies on the information gathered and opinions from all of the following *except* _____.
A) the Monitoring Board
B) users
C) managers
D) auditors
Answer: A
Diff: 2
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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18) The _____ is responsible for oversight, administration, and finances of the Financial Accounting Standards Board (FASB).
A) General Accounting Standards Board (GASB)
B) Financial Accounting Foundation (FAF)
C) Public Company Accounting Oversight Board (PCAOB)
D) Financial Accounting Standards Advisory Council (FASAC)
Answer: B
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

19) Which organization exists to advise the Financial Accounting Standards Board (FASB) on technical issues?
A) General Accounting Standards Board (GASB)
B) Financial Accounting Foundation (FAF)
C) Emerging Issues Task Force (EITF)
D) Financial Accounting Standards Advisory Council (FASAC)
Answer: D
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

20) The Governmental accounting Standards Advisory Council (GASAC) serves as an advisory board to the _____.
A) General Accounting Standards Board (GASB)
B) Financial Accounting Foundation (FAF)
C) Emerging Issues Task Force (EITF)
D) Financial Accounting Standards Advisory Council (FASAC)
Answer: A
Diff: 1
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

21) List the seven steps of the FASB standard-setting process.
Answer: Step 1: Identification of an issue.
Step 2: Decision to pursue.
Step 3: Public meetings.
Step 4: Exposure Draft.
Step 5: Public roundtables.
Step 6: Redeliberation.
Step 7: Publication of the final standard.
Diff: 2
Objective: 1.3
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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1.4 Trends in Standard Setting

1) In recent years, the FASB standards that have been set indicate that the income statement is more important than the balance sheet.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

2) Principles-based standards are deemed to be more optimal than rules-based standards and objectives-based standards.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

3) Objectives-based standards are deemed to be more optimal than rules-based standards and principles-based standards.
Answer: TRUE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

4) Rules-based standards rely on theories and concepts that are linked to a well-developed theoretical framework.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

5) Principles-based standards involve few, if any, exceptions.
Answer: TRUE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

6) Principles-based standards typically provide sufficient guidance to implement a standard.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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7) Rules-based standards require a significant amount of professional judgment.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

8) Rules-based standards result in inconsistencies between standards.
Answer: TRUE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

9) U.S. GAAP contains more rules-based standards than IFRS.
Answer: TRUE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

10) Principles-based standards are more consistent with the asset/liability approach and rules-based standards are more consistent with the income statement approach.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

11) Fair value of an asset is the amount at which the asset could be bought in a current transaction between willing parties.
Answer: TRUE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

12) Fair value measurements have a long-standing tradition in U.S. GAAP.
Answer: FALSE
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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13) Which of the following is *not* a current trend in accounting-standards setting?
A) increase in political involvement
B) move toward principles-based system
C) focus on asset/liability approach
D) emphasis on measuring fair value
Answer: A
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

14) Which type of standard relies on theories and concepts that are linked to a well-developed theoretical framework?
A) objectives-based standard
B) principles-based standard
C) theories-based standard
D) rules-based standard
Answer: B
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

15) Which of the following is a characteristic of rules-based standards?
A) involve few, if any, exceptions
B) result in inconsistencies between standards
C) contain no bright-line tests
D) provide insufficient guidance
Answer: B
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

16) Which of the following is a characteristic of objectives-based standards?
A) do not rely on professional judgment
B) increase bright-line tests
C) somewhere between principles-based and rules-based
D) no exceptions
Answer: C
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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17) Which financial statement is implicitly considered dominant as standard setting shifts toward the asset/liability approach?
A) statement of financial position
B) statement of cash flows
C) statement of shareholders' equity
D) statement of comprehensive income
Answer: A
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

18) _____ is the amount at which a liability could be incurred or settled in a current transaction between willing parties.
A) Income value
B) Settlement value
C) Current value
D) Fair value
Answer: D
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

19) Which of the following is a bright-line test?
A) An item is deemed material if it is large enough to influence the CEO's decision making.
B) An item is deemed material if it exceeds 10% of net income.
C) An item is deemed material if it is large in size.
D) An item is deemed material if it is large enough to influence an investor's decision making.
Answer: B
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

20) Which of the following *best* defines fair value?
A) The amount at which an asset could be bought or sold in a current transaction between willing parties.
B) The market value of an asset determined by a transaction between related parties.
C) The amount at which an asset could be sold in a transaction occurring within the last year.
D) The amount at which an asset could be bought or sold in a current transaction between any two parties.
Answer: A
Diff: 1
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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21) Contrast the differences between rules-based standards and principles-based standards.
Answer:

Principles-based	Rules-based
Few exceptions	Many exceptions
No bright-line tests	Many bright-line tests
Provide less guidance	Provide more guidance
Involve much interpretation	Involve little interpretation
Few inconsistencies between standards	Many inconsistencies between standards

Diff: 2
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

22) Give two examples of assets that may be valued at fair value as opposed to historical cost.
Answer: Firms must report some investments in equity securities that have a readily determinable fair value and some investments in debt at fair value, as opposed to historical cost.
Diff: 2
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

23) Describe rules-based vs. principles-based standards.
Answer: A principles-based standard relies on theories, concepts, and principles of accounting that are linked to a well-developed theoretical framework. A rules-based standard contains specific, prescriptive procedures rather than relying on a consistent theoretical framework.
Diff: 2
Objective: 1.4
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

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Intermediate Accounting, 3e **(Gordon/Raedy/Sannella)**
Chapter 2 Financial Reporting Theory

2.1 Overview of the Conceptual Framework

1) U.S. GAAP and IFRS set forth the same objective of financial reporting and the same qualitative characteristics in their respective conceptual frameworks.
Answer: TRUE
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

2) The purpose of the conceptual framework is to assist standard setters in developing and revising accounting standards.
Answer: TRUE
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

3) Under U.S. GAAP, the conceptual framework overrides accounting standards.
Answer: FALSE
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

4) At the present time, the FASB and IASB are working together on the conceptual framework.
Answer: FALSE
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

5) The FASB is currently working on the objectives of financial reporting and presentation.
Answer: FALSE
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

6) Before issuing a new standard, the standard setters weigh constraints, which may deter requiring the new standard.
Answer: TRUE
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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7) Based on the information in the textbook at the time of printing, the FASB has completed the conceptual framework chapters on the objective of financial reporting, qualitative characteristics, and notes to the financial statements.
Answer: TRUE
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

8) What is the primary purpose of the conceptual framework?
A) to override accounting standards
B) to assist standard setters in developing and revising accounting standards
C) to revise the objective of financial reporting
D) All of the above
Answer: B
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

9) The conceptual framework assists with _____.
A) the development of a set of standards which provide absolute answers for accounting questions
B) the development of a set of standards for auditors to use when looking for material misstatements or fraud
C) the development of a set of standards which ensure that accounting standards are coherent and uniform
D) All of the above
Answer: C
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

10) Which of the following is *not* a purpose of FASB's conceptual framework?
A) aid in development of new standards
B) support understanding of accounting standards
C) assist with revision of accounting standards
D) override existing accounting standards
Answer: D
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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11) _____ are identical under U.S. GAAP and IFRS.
A) Elements and Recognition
B) Presentation and Disclosure
C) Objective and Qualitative Characteristics
D) Subjective and Quantitative Characteristics
Answer: C
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

12) When developing new standards, the standard setters must first determine _____.
A) which elements of the financial statements are affected by the proposed standard
B) if the proposed standard possesses the qualitative characteristics that make accounting information useful
C) if the proposed standard meets the objective of financial reporting
D) which recognition and measurement concepts are used to support the proposed standard
Answer: C
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

13) When developing a new proposed accounting standard, after FASB has determined that the proposed standard meets the objective of financial reporting, the next step in the development process is to _____.
A) determine which elements of the financial statements are affected by the proposed standard
B) consider whether the proposed standard possesses the qualitative characteristics that make accounting information useful
C) weigh constraints on issuing the new standard, which may deter requiring the new standards
D) identify recognition and measurement concepts used to support the proposed standard
Answer: B
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

14) Which of the following best characterizes the current situation concerning revisions to the conceptual framework?
A) The FASB is considering revisions to their conceptual framework but IASB is not.
B) The IASB is considering revisions to the conceptual framework but FASB is not.
C) The FASB and the IASB are working independently on their conceptual frameworks.
D) The FASB and the IASB are working cooperatively on a single conceptual framework.
Answer: C
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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15) All of the following are components of the conceptual framework for financial reporting *except* _____.
A) qualitative characteristics
B) standards
C) principles of recognition and measurement
D) elements of the financial reporting system
Answer: B
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

16) The IASB and FASB share the goal that standards will be based on an agreed set of fundamental _____.
A) practices
B) constraints
C) standards
D) concepts
Answer: D
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

17) When comparing FASB's Conceptual Framework to the IASB's Conceptual Framework, _____.
A) the objective and qualitative characteristics are closely related
B) FASB includes an additional chapter on Financial Statements and the Reporting Entity
C) FASB includes an additional chapter on Concepts of Capital and Capital Maintenance
D) All of the above
Answer: A
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

18) The purpose of the conceptual framework is to provide guidance to _____.
A) preparers of financial statements
B) auditors
C) standard setters
D) CEOs
Answer: C
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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19) List the active phases in the FASB conceptual framework project.
Answer: Three active phases in the FASB conceptual framework project are:
- Elements
- Measurement
- Presentation
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

20) List the completed phases in the FASB conceptual framework project.
Answer: Three completed phases in the FASB conceptual framework project are:
- Objective
- Qualitative Characteristics
- Notes to the Financial Statements
Diff: 1
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

21) Discuss how standard setters use the conceptual framework in developing new standards.
Answer: Standard setters will:
- Determine if the proposed standard meets the objective of financial reporting.
- Establish that the information provided by the new standard possesses qualitative characteristics that make accounting information useful.
- Consider the elements of the financial statements affected and the recognition and measurement concepts used to support the new standard.
- Weigh constraints such as the cost and benefit of issuing the new standard, which may deter requiring the new standard.
Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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22) List the three primary components of the conceptual framework for financial reporting and the two subcomponents of each component.
Answer: The primary components of the conceptual framework for financial reporting and related subcomponents are:
- Qualitative characteristics
  - Fundamental characteristics
  - Enhancing characteristics
- Elements
  - Point-in-time elements
  - Period-of-time elements
- Principles
  - Recognition
  - Measurement

Diff: 2
Objective: 2.1
IFRS/GAAP: GAAP
AACSB: Application of knowledge

2.2 The Objective of Financial Reporting

1) The conceptual framework defines the objective of financial reporting as providing financial information that is useful to existing and potential investors, lenders, and other creditors in making decisions.
Answer: TRUE
Diff: 1
Objective: 2.2
IFRS/GAAP: GAAP
AACSB: Application of knowledge

2) The conceptual framework indicates that the primary users of financial information are investors, lenders, and other creditors who cannot demand information from the entity.
Answer: TRUE
Diff: 1
Objective: 2.2
IFRS/GAAP: GAAP
AACSB: Application of knowledge

3) Which of the following is *not* considered to be a primary user of financial information for which financial reporting standards are designed?
A) creditors that are suppliers
B) investors such as stockholders and bondholders
C) regulators
D) lenders such as banks
Answer: C
Diff: 2
Objective: 2.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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4) Which of the following types of information is *not* a focus of the primary objective of financial reporting?
A) information that helps a banker decide to provide a loan
B) information that helps a manager assess the efficiency and effectiveness of operations
C) information that helps a creditor evaluate the amount and timing of cash flows of its customers
D) information that helps an investor form an opinion about a company's future cash flows
Answer: B
Diff: 2
Objective: 2.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

5) _____ is the careful and responsible management of something entrusted in one's care.
A) Regulation
B) Stewardship
C) Financial planning
D) Financial reporting
Answer: B
Diff: 1
Objective: 2.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

6) Who are the primary users of financial information? Discuss how FASB and IASB take them into account.
Answer: Primary users are investors, lenders, and other creditors that cannot demand information from the entity. Whereas a large creditor such as Bank of America may be able to demand certain information that meets their needs, many investors and creditors may not have that same ability. As a result, when making decisions regarding the conceptual frameworks, the boards consider the needs of these groups.
Diff: 2
Objective: 2.2
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

7) What is the purpose of the conceptual framework?
Answer: The purpose of the conceptual framework is to establish objectives and fundamental concepts that are the basis for developing and revising financial accounting and reporting standards.
Diff: 1
Objective: 2.2
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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8) Frank Smith is a student getting his degree in business administration. He does not like his accounting class very much, and doesn't understand why he needs to study accounting — stating "I'm never going to be an accountant — why do I need to know this?" Explain to Frank why it is important for business students to learn about accounting and give examples.
Answer: Answers will vary — should include discussion on accountability and transparency. Other points could be the need to talk intelligently with their accountant, to know which gauges to watch (and be able to understand their meaning and consequence), and be able to identify economic events that could impact the company. (If open book exam, they could reference the interview with Paul Pacter from Section 2.2.)
Diff: 2
Objective: 2.2
IFRS/GAAP: GAAP
AACSB: Analytical thinking

2.3 The Qualitative Characteristics of Financial Information

1) The two types of qualitative characteristics are fundamental characteristics and elective characteristics.
Answer: FALSE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

2) The role of qualitative characteristics in the conceptual framework is to increase the decision usefulness of financial information.
Answer: TRUE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

3) Information exhibits the characteristic of faithful representation if it is complete, neutral, and free from error.
Answer: TRUE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

4) Information is relevant if it reliably depicts the substance of an economic event.
Answer: FALSE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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5) Information has predictive value if it provides feedback about prior evaluations.
Answer: FALSE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

6) Information that is not material is never relevant.
Answer: TRUE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

7) Verifiability is a characteristic of faithful representation.
Answer: FALSE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

8) Relevance is an enhancing characteristic of financial information.
Answer: FALSE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

9) Information that is not accurate can be considered faithfully representative.
Answer: FALSE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

10) Materiality cannot always be expressed quantitatively and sometimes requires professional judgment.
Answer: TRUE
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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11) In the conceptual framework, what are the two types of qualitative characteristics of financial information?
A) fundamental and enhancing
B) point-in-time and period-of-time
C) recognition and measurement
D) elements and principles
Answer: A
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

12) The two fundamental characteristics of financial information are _____.
A) comparability and understandability
B) relevance and timeliness
C) reliability and faithful representation
D) faithful representation and relevance
Answer: D
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

13) Information that is reported free from error _____.
A) contains no mistakes or omissions in the description of an event or in the process used to produce financial information
B) is accurate in all respects
C) does not include estimates
D) All of the above
Answer: A
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

14) _____ characteristics distinguish useful financial information from information that is not useful.
A) Representative
B) Relevant
C) Fundamental
D) Quantitative
Answer: C
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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15) What are the attributes of relevant information?
A) predictive value, timeliness, free from error
B) materiality, predictive value, and confirmatory value
C) comparability, verifiability, and predictive value
D) complete, neutral, free from error
Answer: B
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

16) Which of the following is *not* a characteristic of relevance?
A) confirmatory value
B) materiality
C) free from error
D) predictive value
Answer: C
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

17) _____ indicates whether financial information depicts an economic event in a way that is complete, neutral, and free from error.
A) Relevance
B) Faithful representation
C) Verifiability
D) Truthfulness
Answer: B
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

18) Which of the following is a characteristic of faithful representation?
A) timely
B) comparable
C) material
D) complete
Answer: D
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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19) The attribute _____ relates to information that is relevant.
A) comparative value
B) predictive value
C) neutrality
D) verifiability
Answer: B
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

20) All of the following are enhancing characteristics *except* _____.
A) understandability
B) verifiability
C) consistency
D) comparability
Answer: C
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

21) _____ means that a group of reasonably informed financial statement users are able to reach a consensus decision that reported information is a faithful representation of an underlying economic event.
A) Comparability
B) Verifiability
C) Understandability
D) Freedom from error
Answer: B
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

22) Financial statements should provide *all* financial information that is relevant and faithfully representative within the limitations of the _____ constraint.
A) benefit
B) materiality
C) usefulness
D) cost
Answer: D
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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23) Baxter Company issues its annual financial reports within one month of the end of the year. This is an example of which enhancing quality of accounting information?
A) confirmatory value
B) relevance
C) verifiability
D) timeliness
Answer: D
Diff: 1
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

24) Southcoast Warehousing Inc. reported earnings per share of $3.41. This surpassed the average analyst forecast of $2.90. This information has _____ to users of financial information.
A) confirmatory value
B) comparable value
C) consistent value
D) both A & C
Answer: A
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

25) Coffee Mugs Inc. is aware that a large portion of its receivables may become uncollectible because the customer is in talks for bankruptcy. By choosing not to disclose this information, the information provided in the statements _____.
A) is not verifiable
B) does not faithfully represent the firm's financial position
C) both A & B
D) neither A nor B
Answer: B
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

26) Which of the following characteristics is fulfilled by separating current and noncurrent assets on the balance sheets?
A) relevance
B) faithful representation
C) comparability
D) understandability
Answer: D
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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27) Do you agree or disagree with the following statement: "Financial statements that are free from error are accurate." Explain your answer.
Answer: A financial statement that is free from error is not the same thing as an accurate statement. The nature of accrual accounting is one that relies on estimates; therefore, when saying information reported is free from error, it is really referring to the process used to generate the financial statements being error-free. The amounts reported may be different than the actual amounts because they rely on estimates.
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

28) What is the cost constraint and how does it affect financial reporting?
Answer: The conceptual framework stipulates that standard setters should compare the cost of requiring information to the benefits derived from presenting this information when developing accounting standards. The FASB and the IASB must determine that the costs of implementing a standard will not exceed the benefits that might be derived from it. Standard setters consider costs for both financial statement reporters and users. To be reported, accounting information not only must be relevant and faithfully represented but it also must pass an economic test by satisfying the cost constraint.
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

29) Caesar & Company is planning a major expansion, and is in negotiations with their bank for a loan. The bank requested that Caesar & Co provide them with financial statements as soon as possible after the end of the year. Caesar & Co has several suppliers that are slow to submit invoices, so they are considering making estimates for the amounts associated with those liabilities in order to expedite the preparation of the financial statements for the bank. Discuss the qualitative characteristics that they need to consider.
Answer: This will be a trade-off between faithful representation and timeliness. By estimating the amounts for the liabilities, the statements will be less faithfully representative — because the associated invoices will not be available. To be faithfully representative, information must be complete, neutral and free from error. Estimates of the liabilities may not be free of error. However, this will allow them to prepare the statements quickly — and timeliness stipulates that financial information is available to users early enough to assist with decision making.
Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

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30) Complete the following table — identify which fundamental characteristic and which attribute are indicated in each independent scenario.

Scenario	Fundamental Characteristics	Attribute
Moss Inc.'s accountant has verified that all equipment has been depreciated according to the company's depreciation schedule.		
Cross & Grant Company includes in a note all relevant details relating to the company's equipment — including depreciation method, estimated useful life, historical cost, and accumulated depreciation.		
Excellent Foundation discloses plans to dispose of a major operating segment.		
TLR Studios discloses information relating to a pending lawsuit that is likely to have an unfavorable outcome.		

Answer:

Scenario	Fundamental Characteristics	Attribute
Moss Inc.'s accountant has verified that all equipment has been depreciated according to the company's depreciation schedule.	Faithful Representation	Free from error
Cross & Grant Company includes in a note all relevant details relating to the company's equipment — including depreciation method, estimated useful life, historical cost, and accumulated depreciation.	Faithful Representation	Complete
Excellent Foundation discloses plans to dispose of a major operating segment.	Relevance	Materiality
TLR Studios discloses information relating to a pending lawsuit that is likely to have an unfavorable outcome.	Faithful Representation	Neutral

Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

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31) Complete the following table — identify which enhancing characteristic is indicated in each independent scenario and whether it was satisfied or violated.

Scenario	Enhancing Characteristics	Satisfied or Violated
Search Engine Corporation reports the historical cost of its archery park on the balance sheet.		
Creighton's Fine Products produces very basic financial statements, without classification or notes. They do have complicated lease and borrowing agreements, and have changed depreciation estimates.		
Realistic Ventures Company switched to fair value accounting for standing timber, which is the method used by most companies in the industry.		
Roy & Quinn's Lakeside Properties provides financial statement information every other year.		

Answer:

Scenario	Enhancing Characteristics	Satisfied or Violated
Search Engine Corporation reports the historical cost of its archery park on the balance sheet.	Verifiability	Satisfied
Creighton's Fine Products produces very basic financial statements, without classification or notes. They do have complicated lease and borrowing agreements, and have changed depreciation estimates.	Understandability	Violated
Realistic Ventures Company switched to fair value accounting for standing timber, which is the method used by most companies in the industry.	Comparability	Satisfied
Roy & Quinn's Lakeside Properties provides financial statement information every other year.	Timeliness	Violated

Diff: 2
Objective: 2.3
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

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2.4 Elements of Financial Reporting

1) U.S. GAAP and IFRS identify the same seven period-of-time elements.
Answer: FALSE
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

2) U.S. GAAP and IFRS identify the same three point-in-time elements.
Answer: TRUE
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

3) According to U.S. GAAP, elements are categorized by whether they are relevant or faithfully representative.
Answer: FALSE
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

4) According to IFRS, point-in-time elements include assets, liabilities, and equity.
Answer: TRUE
Diff: 1
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

5) According to IFRS, period-of-time elements include income, expenses, performance, and transactions with owners.
Answer: FALSE
Diff: 1
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

6) Comprehensive income is the residual interest in the assets of an entity that remains after deducting its liabilities.
Answer: FALSE
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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7) According to U.S. GAAP, period-of-time elements include performance, income, expenses, and capital maintenance adjustments.
Answer: FALSE
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

8) IFRS does not treat transactions with owners as separate elements.
Answer: TRUE
Diff: 1
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

9) The IFRS element *Income* is identical to the GAAP element *comprehensive income.*
Answer: FALSE
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

10) According to IFRS, two type of income would be revenues and gains.
Answer: TRUE
Diff: 2
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

11) In the conceptual framework, what are the two types of elements of financial reporting?
A) fundamental and enhancing
B) point-in-time and period-of-time
C) recognition and measurement
D) elements and principles
Answer: B
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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12) Under U.S. GAAP, comprehensive income includes which of the following?

A)

Investments by Owners	Operating Income
No	Yes

B)

Investments by Owners	Operating Income
Yes	No

C)

Investments by Owners	Operating Income
No	No

D)

Investments by Owners	Operating Income
Yes	Yes

Answer: A
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Analytical thinking

13) According to the FASB's conceptual framework, gains include increases in equity from which of the following activities?

A)

Investments by Owners	Peripheral Transactions
Yes	No

B)

Investments by Owners	Peripheral Transactions
Yes	Yes

C)

Investments by Owners	Peripheral Transactions
No	No

D)

Investments by Owners	Peripheral Transactions
No	Yes

Answer: D
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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14) Which term is described as the building blocks of the financial statements?
A) fundamental characteristics
B) enhancing characteristics
C) elements
D) assets
Answer: C
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

15) _____ elements appear on the balance sheet.
A) Period-of-time
B) Point-in-time
C) Piece-of-time
D) Phase-in-time
Answer: B
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

16) Under U.S. GAAP, _____ is an example of a period-of-time element and appears on the _____.
A) accounts receivable; balance sheet
B) depreciation expense; statement of shareholders' equity
C) salary payable; balance sheet
D) sales revenue; income statement
Answer: D
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

17) IFRS and U.S. GAAP both identify assets as _____ elements.
A) phase-in-time
B) period-of-time
C) point-in-time
D) piece-of-time
Answer: C
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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18) U.S. GAAP identifies _____ point-in-time elements.
A) two
B) three
C) four
D) five
Answer: B
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

19) U.S. GAAP identifies _____ period-in-time elements.
A) four
B) five
C) six
D) seven
Answer: D
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

20) IFRS identifies _____ point-in-time elements.
A) one
B) three
C) five
D) seven
Answer: B
Diff: 1
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

21) IFRS identifies _____ period-in-time elements.
A) two
B) four
C) five
D) seven
Answer: A
Diff: 1
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

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22) According to U.S. GAAP, changes in equity that result from the company's central business operations are _____.
A) revenues and gains
B) gains and losses
C) revenues and expenses
D) losses and expenses
Answer: C
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

23) Which of the following terms describe probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events?
A) performance
B) income
C) equity
D) asset
Answer: D
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

24) _____ include(s) all changes in equity during a period except those resulting from transactions with owners.
A) Performance
B) Revenues
C) Comprehensive income
D) Period-of-time elements
Answer: C
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

25) Which element of the financial statements results from peripheral or incidental transactions?
A) gains
B) revenues
C) equity
D) liabilities
Answer: A
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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26) Which of the following statements is *not* true about distributions to owners?
A) Distributions to owners represent a decrease in equity.
B) Distributions to owners result from incurring liabilities by the enterprise to owners.
C) Distributions to owners are included in other comprehensive income.
D) Distributions to owners result from rendering services by the enterprise to owners.
Answer: C
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

27) The primary distinction between expenses and losses is _____.
A) the verifiability of the transactions
B) the nature of the activities that bring about the transactions
C) the timing of the transactions
D) the amount and materiality of the transactions
Answer: B
Diff: 1
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

28) IFRS identifies two period-of-time elements as _____.
A) Assets and Liabilities
B) Assets and Equity
C) Income and Expenses
D) Revenues and Gains
Answer: C
Diff: 1
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

29) The IFRS element *income* relates to which U.S. GAAP element(s)?
A) comprehensive income
B) cash flows and gains
C) revenues and expenses
D) revenues and gains
Answer: D
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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30) The IFRS element *expenses* encompasses which U.S. GAAP elements?
A) revenues and expenses
B) losses and expenses
C) gains and expenses
D) expenses only
Answer: B
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

31) A period-of-time element under GAAP that increases equity in a business by transferring something of value from other entities is _____.
A) Distribution to owners
B) Investments by owners
C) Gains
D) Revenues
Answer: B
Diff: 2
Objective: 2.4
IFRS/GAAP: IFRS
AACSB: Application of knowledge

32) Which of the following is a point-in-time element?
A) Income
B) Liabilities
C) Expenses
D) Distributions to owners
Answer: B
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

33) Which of the following is a period-of-time element?
A) Liabilities
B) Equity
C) Assets
D) Gains
Answer: D
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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34) Which of the following is a point-in-time element?
A) Fees Earned
B) Notes Payable
C) Cost of Goods Sold
D) Dividends
Answer: B
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

35) Which of the following is a period-of-time element?
A) Unearned Revenue
B) Common Stock
C) Accounts Receivable
D) Gain on the Disposal of Equipment
Answer: D
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

36) What is the relationship between the point-in-time elements and the period-of-time elements?
Answer: The period-of-time elements provide a way to describe how the point-in-time elements change during the accounting period.
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Reflective thinking

37) What is equity and how does it change during a period of time?
Answer: Equity is the residual interest in the assets of an entity that remains after deducting its liabilities. It changes when there are investments by the owners, distributions to the owners, and increases or decreases in comprehensive income.
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

38) Explain comprehensive income in terms of other elements of the financial statements.
Answer: Comprehensive income includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. That is, comprehensive income includes revenues, expenses, gains, and losses, and all other changes to equity not resulting from transactions with the owners.
Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Reflective thinking

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39) Identify the element, and whether it is point-in-time or period-of-time.

Definition	Element	Point-in-time or Period-of-time
Increases in equity (net assets) from peripheral or incidental transactions and from all other transactions and other events and circumstances affecting the entity with the exception of revenues or investments by owners.		
Probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.		
Increases in equity resulting from transfers to it from other entities of something valuable to obtain or increase ownership interests (or equity) in it.		
Outflows or other consumption of assets, incurrence of liabilities, or both — from delivering or producing goods, rendering services, or carrying out other activities that constitute the company's ongoing major or central operations.		

Answer:

Definition	Element	Point-in-time or Period-of-time
Increases in equity (net assets) from peripheral or incidental transactions and from all other transactions and other events and circumstances affecting the entity with the exception of revenues or investments by owners.	Gains	Period-of-time
Probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.	Assets	Point-in-time
Increases in equity resulting from transfers to it from other entities of something valuable to obtain or increase ownership interests (or equity) in it.	Investments by Owners	Period-of-time
Outflows or other consumption of assets, incurrence of liabilities, or both — from delivering or producing goods, rendering services, or carrying out other activities that constitute the company's ongoing major or central operations.	Expenses	Period-of-time

Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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40) Identify the element, and whether it is point-in-time or period-of-time.

Definition	Element	Point-in-time or Period-of-time
Probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.		
The change in equity of a business during a period from transactions and other events and circumstances from nonowner sources.		
The net assets or residual interest in the assets of an entity that remains after deducting its liabilities.		

Answer:

Definition	Element	Point-in-time or Period-of-time
Probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.	Liabilities	Point-in-time
The change in equity of a business during a period from transactions and other events and circumstances from nonowner sources.	Comprehensive income	Period-of-time
The net assets or residual interest in the assets of an entity that remains after deducting its liabilities.	Equity	Point-in-time

Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

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41) Identify the element, and whether it is point-in-time or period-of-time.

Definition	Element	Point-in-time or Period-of-time
Probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.		
Decreases in equity resulting from transferring assets, rendering services, or incurring liabilities by the enterprise to owners.		
Decreases in equity (net assets) from peripheral or incidental transactions and from all other transactions and other events and circumstances affecting the entity except those that result from expenses or distributions to owners.		
Inflows or other enhancements of an entity's assets, settlements of liabilities, or both, from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.		

Answer:

Definition	Element	Point-in-time or Period-of-time
Probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.	Assets	Point-in-time
Decreases in equity resulting from transferring assets, rendering services, or incurring liabilities by the enterprise to owners.	Distribution to Owners	Period-of-time
Decreases in equity (net assets) from peripheral or incidental transactions and from all other transactions and other events and circumstances affecting the entity except those that result from expenses or distributions to owners.	Losses	Period-of-time
Inflows or other enhancements of an entity's assets, settlements of liabilities, or both, from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.	Revenues	Period-of-time

Diff: 2
Objective: 2.4
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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2.5 Principles of Recognition and Measurement

1) The FASB and IASB are converged in general recognition principles.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

2) Recognition is the process of reporting an economic event in the financial statements.
Answer: TRUE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

3) The cost constraint means that an item is not recognized in the financial statements unless its omission would significantly influence the judgment of an informed user.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

4) The major difference between cash and accrual accounting is the timing of revenue and expense recognition.
Answer: TRUE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

5) Under the principles of accrual accounting, revenues are considered earned when a company exchanges a good or service for cash or claims for cash.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

6) According to the expense recognition principle in U.S. GAAP, firms recognize expenses when only one requirement is met: an asset has a reduced future benefit or when a liability is incurred or increased without an associated economic benefit.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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7) Current cost is the amount of cash received in exchange for an asset less the direct costs of disposal.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

8) U.S. GAAP does not allow companies to prepare financial statements using a cash-basis system.
Answer: TRUE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

9) Quoted prices in active markets are the measure of fair value that is neither the most observable nor the least observable.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

10) Revenue and expense recognition under the current IFRS conceptual framework is the same as under the U.S. GAAP conceptual framework.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

11) Unobservable values cannot be used to report the fair value of assets and liabilities in the financial statements.
Answer: FALSE
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

12) Which of the following is *not* an underlying principle of accrual accounting?
A) bases of measurement
B) monetary unit assumption
C) revenue and expense recognition
D) general recognition
Answer: B
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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13) The process of reporting an economic event in the financial statements is known as _____.
A) recording
B) writing
C) recognition
D) transcribing
Answer: C
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

14) Which of the following is *not* one of the four general recognition criteria under U.S. GAAP?
A) relevant
B) measurable
C) reliable
D) material
Answer: D
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

15) Under IFRS, which of the following is *not* a criterion for recognizing items in the financial statements?
A) The item is measurable with a high degree of certainty.
B) The item is relevant.
C) The item meets the definition of an element.
D) Economic benefits from the item are probable.
Answer: D
Diff: 1
Objective: 2.5
IFRS/GAAP: IFRS
AACSB: Application of knowledge

16) A Fortune-500 company purchases a new clock for $35. The clock is expected to last for five years. According to the materiality threshold, this would be treated as an _____ in the accounting records.
A) asset
B) expense
C) equipment
D) none of the above
Answer: B
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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17) Under IFRS, which of the following is considered to be a measure of current cost?
A) systematic value
B) direct cost
C) present value of future cash flows
D) historical cost
Answer: C
Diff: 1
Objective: 2.5
IFRS/GAAP: IFRS
AACSB: Application of knowledge

18) Under U.S. GAAP, what is a condition for revenue to be realized or realizable?
A) Cash or fixed claims to cash are received.
B) Contracts are written as per negotiations.
C) The company exchanges a good or service.
D) Both A & C
Answer: D
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

19) Under U.S. GAAP, revenues are considered _____ when the seller has accomplished what it must do to be entitled to the revenues.
A) recognized
B) earned
C) realized
D) entitled
Answer: B
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

20) IFRS includes _____ as bases of measurement.
A) present value of future cash flows and historical cost
B) historical cost and net realizable value
C) historical cost and current value
D) net realizable value and current value
Answer: C
Diff: 1
Objective: 2.5
IFRS/GAAP: IFRS
AACSB: Application of knowledge

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21) Under IFRS, revenue is recognized simultaneously with _____.
A) increases in assets or increases in liabilities
B) decreases in assets or increases in liabilities
C) increases in assets or decreases in liabilities
D) decreases in assets or decreases in liabilities
Answer: C
Diff: 2
Objective: 2.5
IFRS/GAAP: IFRS
AACSB: Analytical thinking

22) Under the U.S. GAAP, which of the following is *not* an approach used to determine when to report an expense?
A) systematic allocation
B) when incurred
C) match with revenues
D) net realizable value
Answer: D
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

23) U.S. GAAP identifies _____ measurement bases used in financial reporting and IFRS identifies _____.
A) three; four
B) four; two
C) five; two
D) four; three
Answer: C
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

24) The _____ cost is the amount of cash (or equivalent) that a firm paid to acquire an asset, whereas _____ is the amount the firm would pay if the asset were purchased today.
A) historical; current cost
B) present value; current market value
C) historical; current market value
D) realized; present value
Answer: A
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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25) _____ is the amount of cash that the firm actually paid to acquire an asset.
A) Current market value
B) Current cost
C) Historical cost
D) Net realizable value
Answer: C
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

26) When the buyer and seller are unrelated and independent, the transaction is considered to be _____.
A) a bad deal
B) an arms-length transaction
C) an independent contract
D) a bribe
Answer: B
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

27) Are the identified measurement bases consistent with fair value reporting?

A)

Current market value	Net realizable value
Yes	No

B)

Current market value	Net realizable value
No	No

C)

Current market value	Net realizable value
Yes	Yes

D)

Current market value	Net realizable value
No	Yes

Answer: C
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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28) When deciding how to measure the fair value of an asset or liability, there is sometimes a trade-off between _____.
A) understandability and comparability
B) faithful representation and neutrality
C) verifiability and neutrality
D) relevance and faithful representation
Answer: D
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

29) _____ accounting measures cash receipts and disbursements, leaving out economic activity.
A) Accrual
B) Cash-basis
C) Cloud
D) Historic
Answer: B
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

30) _____ accounting measures noncash transactions.
A) Accrual
B) Cash-basis
C) Cloud
D) Historic
Answer: A
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

31) Purrfect Pets, Inc. provides animal daycare for $29 per day. Customers buy three month packages, which provide 15 days of care per month. In January they received cash payments from 10 customers. For the month of January, they will recognize _____ of revenue under the cash basis, and _____ of revenue under the accrual basis.
A) $435; $1305
B) $13,050; $13,050
C) $13,050; $4350
D) $4350; $4350
Answer: C
Explanation: Cash basis they recognize the cash received ($29 × 45 days × 10 customers = $13,050); accrual basis they recognize the revenue of the 15 days of care provided that month ($29 × 15 days × 10 customers = $4350).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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32) Purrfect Pets, Inc. provides animal daycare for $31 per day. Customers buy three month packages, which provide 15 days of care per month. In January, they received cash payments from 13 customers. For the month of February, they will recognize _____ of revenue under the cash basis, and _____ of revenue under the accrual basis.
A) $0; $403
B) $6045; $6045
C) $403; $403
D) $0; $6045
Answer: D
Explanation: Cash basis is zero, because no cash was collected during February. Accrual basis they recognize the revenue for the 15 days of care provided that month ($31 × 15 days × 13 customers = $6045).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

33) Shadow's Cleaning Service provides weekly cleaning services for $41 per week. In January, they collected payments from 60 customers for 3 months (12 weeks) of service each. For the month of January, they will recognize _____ of revenue under the cash basis, and _____ under the accrual basis.
A) $2460; $720
B) $3180; $0
C) $9840; $29,520
D) $29,520; $9840
Answer: D
Explanation: Using cash basis they recognize what is collected in January ($41 × 12 weeks × 60 customers = $29,520). Using the accrual basis they recognize what was earned in January ($41 × 4 weeks × 60 customers = $9840).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

34) Shadow's Cleaning Service provides weekly cleaning services for $48 per week. In January, they collected payments from 57 customers for 3 months (12 weeks) of service each. For the month of February, they will recognize _____ of revenue under the cash basis, and _____ under the accrual basis.
A) $0; $10,944
B) $10,944; $10,944
C) $10,944; $32,832
D) $32,832; $10,944
Answer: A
Explanation: Using cash basis they recognize what is collected in February — which was zero. Using the accrual basis they recognize what was earned in February ($48 × 4 weeks × 57 customers = $10,944).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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35) Southeast Industries Inc. charges $185 per month for a storage unit. In the first quarter of the year, they collected $9065. Ten customers pre-paid for three months' rental in January, seven customers pre-paid for two months rental in February, and five customers paid for one month rental in March. Using the cash basis of accounting, Southeast will recognize _____ in revenue for January and _____ using the accrual basis.
A) $9065; $5550
B) $5550; $9065
C) $1850; $5550
D) $5550; $1850
Answer: D
Explanation: Cash basis recognizes the cash collected in January ($185 × 3 months × 10 people = $5550). Accrual recognizes the amount earned in January ($185 for January × 10 people = $1850).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

36) Southern Light Container Corp. charges $105 per month for a storage unit. In the first quarter of the year, they collected $5145. Ten customers pre-paid for three months' rental in January, seven customers pre-paid for two months rental in February, and five customers paid for one month rental in March. Using the cash basis of accounting, Southern will recognize _____ in revenue for February and _____ using the accrual basis.
A) $0; $735
B) $735; $1470
C) $1470; $1785
D) $1785; $2520
Answer: C
Explanation: Cash basis recognizes cash collected in February ($105 × 2 months × 7 people = $1470). Accrual recognizes the amount earned in February ($105 for February × 17 people = $1785).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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37) Southern Light Containers charges $125 per month for a storage unit. In the first quarter of the year, they collected $6125. Ten customers pre-paid for three months' rental in January, seven customers pre-paid for two months rental in February, and five customers paid for one month rental in March. Using the cash basis of accounting, Southern will recognize _____ in revenue for March and _____ using the accrual basis.
A) $0; $3375
B) $625; $0
C) $1250; $2500
D) $625; $2750
Answer: D
Explanation: Cash basis recognizes cash collected in March ($125 × 1 month × 5 people = $625). Accrual recognizes the amount earned in March ($125 for March × 22 people = $2750).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

38) Angelo's charges $280 per month for catering services. In the first quarter of the year, they collected $19,600. Fifteen customers pre-paid for three months of catering beginning in January, ten customers pre-paid for two months of catering beginning in February, and five customers paid for one month of catering in March. Using the cash basis of accounting, Angelo's will recognize _____ in revenue for January and _____ using the accrual basis.
A) $4200; $0
B) $7000; $4200
C) $12,600; $4200
D) $0; $12,600
Answer: C
Explanation: Cash basis recognizes cash collected in January ($280 × 3 months × 15 customers = $12,600). Accrual basis recognizes the amount earned in January ($280 for January × 15 customers = $4200).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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39) Angelo's charges $240 per month for catering services. In the first quarter of the year, they collected $16,800. Fifteen customers pre-paid for three months of catering beginning in January, ten customers pre-paid for two months of catering beginning in February, and five customers paid for one month of catering in March. Using the cash basis of accounting, Angelo's will recognize _____ in revenue for February and _____ using the accrual basis.
A) $0; $3600
B) $4800; $6000
C) $3600; $7200
D) $4800; $0
Answer: B
Explanation: Cash basis recognizes cash collected in February ($240 × 2 months × 10 customers = $4800). Accrual basis recognizes the amount earned in February ($240 for February × 25 customers = $6000).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

40) Angelo's charges $280 per month for catering services. In the first quarter of the year they collected $19,600. Fifteen customers pre-paid for three months of catering beginning in January, ten customers pre-paid for two months of catering beginning in February, and five customers paid for one month of catering in March. Using the cash basis of accounting, Angelo's will recognize _____ in revenue for March and _____ using the accrual basis.
A) $0; $1400
B) $8400; $1400
C) $1400; $0
D) $1400; $8400
Answer: D
Explanation: Cash basis recognizes cash collected in March ($280 × 1 month × 5 customers = $1400). Accrual basis recognizes the amount earned in March ($280 for March × 30 customers = $8400).
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

41) Sydney & Caesar Law Firm uses the accrual basis to keep their accounting records. During 2022, they collected $460,000 from clients. On December 31, 2021 they had accounts receivable of $50,000. On December 31, 2022 they had accounts receivable of $70,000 and unearned revenue of $27,000. Using the accrual basis, how much is Sydney & Caesar Law Firm's service revenue for 2022?
A) $410,000
B) $467,000
C) $453,000
D) $480,000
Answer: C
Explanation: $460,000 cash collected - $50,000 A/R earned in 2021 + $70,000 A/R earned in 2022 - $27,000 unearned = $453,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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42) TLR Consulting keep their accounting records using the accrual basis. During 2022, they collected $425,000 from clients. On December 31, 2021 they had accounts receivable of $61,000 and on December 31, 2022 they had accounts receivable of $46,000. Additionally, they had unearned revenues of $7000. Using the accrual basis of accounting, what did TLR Consulting earn in service fees for 2022?
A) $403,000
B) $417,000
C) $433,000
D) $447,000
Answer: A
Explanation: $425,000 cash collected - $61,000 A/R earned in 2021 + $46,000 A/R earned in 2022 - $7000 unearned = $403,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

43) Hanker LLC uses the accrual basis to keep his accounting records. During 2022, he collected $374,000 from clients. At December 31, 2021 he had accounts receivable of $139,000. At December 31, 2022 he had accounts receivable of $164,000 and unearned revenue of $41,000. What did Hanker LLC earn in service revenue for 2022 using the accrual basis of accounting?
A) $194,000
B) $308,000
C) $349,000
D) $358,000
Answer: D
Explanation: $374,000 cash collected - $139,000 A/R earned in 2021 + $164,000 A/R earned in 2022 - $41,000 unearned = $358,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

44) On May 2, Johnson's Landscaping LLC paid $4700 for repairs made to equipment during April. During May fuel costs for its machinery were $5800 to be paid in June. Johnson's lawn mowers were depreciated for May by an amount of $1000 using the straight-line method. What would be the company's equipment-related expenses for May under cash accounting and what would the expenses be under the accrual basis for May?
A) $10,500 under both cash and accrual basis
B) $4700 under cash basis; $5800 under accrual basis
C) $4700 under the cash basis; $6800 under the accrual basis
D) $4700 under the cash basis; $10,500 under accrual basis
Answer: C
Explanation: The only cash outlay for expenses in May is $4700. Under accrual basis, expenses are recognized when incurred — regardless of when the cash is paid. Therefore, the expenses for May are $6800 ($5800 for fuel and $1000 for depreciation.) Depreciation is a noncash expense.
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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45) On April 2, the salaried employees of LaSalle Company receive their paychecks representing 8 workdays in March and 2 days in April for a total gross pay of $15,000. Other expenditures paid in April include advertising from March of $500 and property taxes for the first quarter of the year of $5700. Property taxes for the second quarter are also expected to be $5700. The company's vehicle was repaired on April 1 for an amount of $460 to be paid May 1. What are the expenses for April under the cash accounting method and what would they be under accrual basis accounting?
A) $21,200 under both cash and accrual basis
B) $21,200 under cash basis and $5360 under accrual basis accounting
C) $15,000 under the cash basis; $6660 under the accrual basis
D) $12,000 under the cash basis; $12,460 under accrual basis
Answer: B
Explanation: The cash outlays for expenses in April total $21,200 ($15,000 salaries + $500 advertising + $5700 property taxes). Under accrual basis, expenses are recognized when incurred – regardless of when the cash is paid. Therefore, the expenses for April are $5360 ($15,000 × 2/10 = $3000 of salary for April + $460 of vehicle repairs + $1900 property taxes ($5700/3)).
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

46) Axe Furniture and Accessories Inc. sold an oak custom-designed harvest table for $4,000 on July 31, 2022. The wood, labor, and overhead costs of $1,200 were incurred during the three months leading up to the sale (May, June, and July). Under the expense recognition principle, which of the following statements would be true?
A) The costs of $1,200 should be expensed as cost of goods sold in the month of July under the concept of matching costs with related revenue in the period the revenue occurred.
B) The costs of $1,200 should be systematically recognized by spreading the costs as cost of goods sold over the three months that the production of the table took place.
C) The cost of the table should not be recognized as an expense as it is an asset called merchandise inventory and therefore it is a point-in-time element.
D) The cost of the table should be recognized as cost of goods sold in the earliest period in which the company knew that the table would eventually be sold and, in this case, that would be in May.
Answer: A
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

47) Materially (significantly) large amounts of supplies should be recognized as an expense under which of the following approaches?
A) when purchased
B) upon use in operations
C) strictly as a function of time
D) in a systematic allocation as services of laborers are performed
Answer: B
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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48) Depreciation expense is recognized over time and systematically allocated over the periods of use of the related asset. When depreciation expense is recognized, what related balance sheet line item is also impacted?
A) Equipment
B) Machinery
C) Accumulated Depreciation
D) Supplies
Answer: C
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

49) Yellow Pencil Company pays Helen, a staff accountant, a $10,000 a month salary. How should the salary be recognized as an expense?
A) matched with revenue earned by the Yellow Pencil Company
B) systematically allocated with the use of the pencil making machinery of the Yellow Pencil Company factory
C) upon the sale of pencils and in proportion to those sales
D) recorded as a measure of the effort expended by the staff accountant in the periods in which she works
Answer: D
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

50) In using fair value as a measurement for assets, a company _____.
A) would always use level 1 inputs
B) ideally would use level 1 inputs but if that is not possible would use the highest level of reliability possible
C) would calculate the present value of the expected future cash flows of the asset and use that as a measure regardless of what other inputs are available
D) would only value an asset with input levels 1 or 2 if the asset is impaired
Answer: B
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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51) Identify the three main approaches to expense recognition under U.S. GAAP and provide examples of each. How does IFRS expense recognition principles differ?
Answer: Under U.S. GAAP, the three main approaches are to match the expense with the related revenue, to expense it in the period incurred, or to systematically allocate the expense over periods of use. An example of matching the expense to the revenue would be matching the cost of goods sold expense to the related revenue recognized when the inventory is sold. Expensing in the period incurred would be recording supplies expense during the period that they were consumed. Depreciating a piece of equipment over its useful life is an example of systematic allocation. Under current IFRS conceptual framework, firms recognized expenses in the income statement at the same time as the initial recognition or increase of a liability or the derecognition or decrease in an asset. IFRS does not use the matching approach for expense recognition.
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP/IFRS
AACSB: Analytical thinking

52) Under the new revenue standard, what drives the measurement and timing of revenue recognition?
Answer: Companies should recognize revenue when there is a transfer of control of goods or services. This occurs when a company satisfies its performance obligations specified in the contract with a customer.
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Reflective thinking

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53) Identify the measurement base described in each definition, then indicate whether it applies to U.S. GAAP, IFRS, or both.

Definition	Measurement Base	U.S. GAAP or IFRS or both
The amount of cash (or equivalent) to be received in exchange for an asset, less the direct costs of disposal. In the case of a liability, it is the amount of cash (or equivalent) expected to be paid to liquidate the obligation, including any direct costs of liquidation.		
The amount of cash (or equivalent) that the firm would receive by selling the asset in an orderly liquidation.		
The amount of cash (or equivalent) that the firm paid to acquire the asset. In the case of a liability, this is the amount that the firm received when it incurred the obligation.		
The amount of cash (or equivalent) that would be required if the firm acquired the asset currently.		

Answer:

Definition	Measurement Base	U.S. GAAP or IFRS or both
The amount of cash (or equivalent) to be received in exchange for an asset, less the direct costs of disposal. In the case of a liability, it is the amount of cash (or equivalent) expected to be paid to liquidate the obligation, including any direct costs of liquidation.	Net realizable value	U.S. GAAP
The amount of cash (or equivalent) that the firm would receive by selling the asset in an orderly liquidation.	Current market value	Both
The amount of cash (or equivalent) that the firm paid to acquire the asset. In the case of a liability, this is the amount that the firm received when it incurred the obligation.	Historical cost	Both
The amount of cash (or equivalent) that would be required if the firm acquired the asset currently.	Current cost	U.S. GAAP

Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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54) Freddie's Fish Store maintains saltwater aquariums for office buildings in Anchorage. The following events occurred during the first two months of 2022. For each event, determine the revenue or expense under the cash and accrual bases of accounting.

a. In January, Freddie's purchased a new industrial vacuum for cleaning tanks - it is expected to last 5 years, and cost $5,000.
b. In January, Freddie's collected $30,000 prepayment for cleaning services to be completed during January and February.
c. In February, Freddie's signed a new client, collecting $6,000 for six months of services.
d. In February, Freddie's paid its bimonthly utility bill of $500 for two months of utilities. The bill covers the current and prior months. They are always billed this amount and are paid at the end of every two months.
Answer:
a. Cash basis recognize $5,000 expense in January; accrual basis will allocate this over 5 years through depreciation expense. The annual depreciation expense is $1,000 ($5,000/5 = $1,000). The monthly depreciation expense is $83.33 ($1,000/12 = $83.33).
b. Cash basis recognizes $30,000 revenue in January; accrual basis recognizes $15,000 revenue in January and February.
c. Cash basis recognizes $6,000 revenue in February; accrual basis recognizes $1,000 revenue for February - July.
d. Cash basis recognizes $500 expense in February; accrual basis recognizes $250 expense in January and February.
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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55) Freddie's Fish Store maintains saltwater aquariums for office buildings in Anchorage. The following events occurred during the first two months of 2022. Determine the net income for each month using both the cash and accrual bases. For depreciable items use straight line depreciation with no salvage value.
a. In January, Freddie's purchased a new industrial vacuum for cleaning tanks - it is expected to last 5 years, and cost $5,000.
b. In January, Freddie's collected $30,000 prepayment for cleaning services to be completed during January and February.
c. In February, Freddie's signed a new client, collecting $6,000 for six months of services.
d. In February, Freddie's paid its bimonthly utility bill of $500 for two months of utilities. The bill covers the current and prior months. They are always billed this amount and are paid at the end of every two months.
Answer:
January
Cash basis: revenue $30,000 - expense $5,000 = $25,000
Accrual basis: revenue $15,000 - expense ($83.33 depreciation + $250 utility bill) = $14,666.67

February
Cash basis: revenue $6,000 - expense $500 = $5,500
Accrual basis: revenue $16,000 - expense ($83.33 depreciation + $250 utility bill) = $15,666.67
Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

56) Krump's Pie Company reported revenue of $500,000 in its accrual basis income statement for the year ended December 31, 2022. Additional information from the books:

Accounts receivable December 31, 2021	$150,000
Accounts receivable December 31, 2022	310,000
Uncollectible accounts written off during 2022	20,000

What would Krump's revenue be under the cash basis of accounting?
Answer: $500,000 + $150,000 - $310,000 - $20,000 = $320,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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57) Jimmy's Jelly Company reported revenue of $250,000 in its accrual based income statement for the year ended December 31, 2022. Additional information from the books:

Accounts receivable December 31, 2021	$75,000
Accounts receivable December 31, 2022	80,000
Uncollectible accounts written off during 2022	3,000

What would Jimmy's Jelly Company's revenue be under the cash basis of accounting?
Answer: $250,000 + $75,000 - $80,000 - $3,000 = $242,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

58) Afternoon Dessert's Inc. reported revenue of $200,000 in its cash basis income statement for the year ended December 31, 2022. Additional information from the books:

Accounts receivable December 31, 2021	$10,000
Accounts receivable December 31, 2022	5,000
Prepaid subscription in 2022	1,000

What would Afternoon Dessert's revenue be under the accrual basis of accounting?
Answer: $200,000 - $10,000 + $5,000 - $1,000 = $194,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

59) John's Shoe Store reported revenue of $375,000 in its cash basis income statement for the year ended December 31, 2022. Additional information from the books:

Accounts receivable December 31, 2021	$50,000
Accounts receivable December 31, 2022	75,000
Deposits on custom orders in 2022	10,000

What would John's Shoe Store's revenue be under the accrual basis of accounting?
Answer: $375,000 - $50,000 + $75,000 - $10,000 = $390,000
Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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60) Grinnell and Griffin (G&G) Company services fire protection systems at a fee of $200 per month. Clients pay in advance every quarter - and the company currently services 100 buildings. During the first quarter of the year, G&G collected all service fees on January 1; they also incurred the following expenses: $9,000 in January, $14,000 in February, and $8,000 in March. They paid half of the expense total in February and the rest in March, they did not pay expenses in January. Determine G&G's net income for each month, as well as the quarterly total, under both the cash and accrual bases. Is the quarterly total the same? If it is different, what would account for this?
Answer: The quarterly total is the same.

	Revenue	Recognition	Expense	Recognition	Net Income	Net Income
Month	Cash Basis	Accrual Basis	Cash Basis	Accrual Basis	Cash Basis	Accrual Basis
January	60,000	20,000		9,000	60,000	11,000
February		20,000	15,500	14,000	(15,500)	6,000
March		20,000	15,500	8,000	(15,500)	12,000
Total	60,000	60,000	31,000	31,000	29,000	29,000

Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

61) Brendan's Alarm Company sells subscriptions to its monitoring service at a fee of $75 per month. Clients pay bimonthly, every two months. As of January 1, Brendan currently has 50 clients paying on an even month rotation (February, April, etc.) and 30 clients paying on an odd month rotation (January, March, etc.). Brendan incurs expenses each month for $100 in electric bills and pays the bill every other month. The next payment for utilities is due in February. Determine Brendan's Alarm Company's net income for each month for the first quarter of the year, as well as the quarterly total, under both the cash and accrual bases. Is the quarterly total the same? If it is different, what would account for this?
Answer: The quarterly total is different – due to bimonthly collections and payments – the cash basis recognizes less revenue and expense during the quarter.

	Revenue	Recognition	Expense	Recognition	Net	Income
Month	Cash Basis*	Accrual Basis**	Cash Basis	Accrual Basis	Cash Basis	Accrual Basis
January	4,500	6,000	0	100	4,500	5,900
February	7,500	6,000	200	100	7,300	5,900
March	4,500	6,000	0	100	4,500	5,900
Total	16,500	18,000	200	300	16,300	17,700

*30 × $75 × 2 = $4,500; 50 × $75 × 2 = $7,500
**80 × $75 = $6,000
Diff: 1
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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62) The following events took place at Forrest's Tree Service during the first quarter of the year. Determine Forrest's net income for each month, including a quarterly total, under both the cash and accrual bases of accounting.

a. Performed tree services in January - billed clients for $5,000.
b. Monthly saw sharpening — January, February, March - paid $500 per month.
c. Collected $2,500 from January clients on February 10th.
d. Performed tree services in February — billed clients for $8,000.
e. Employees are paid every other month; salary expense is $5,000 per month — paid on February 28.
f. Performed tree services in March — billed clients for $10,000 - also collected remaining January balance and $5,000 due from February.

Answer:

	Revenue	Recognition	Expense	Recognition	Net	Income
Month	Cash Basis	Accrual Basis	Cash Basis	Accrual Basis	Cash Basis	Accrual Basis
January	0	5,000	500	5,500	(500)	(500)
February	2,500	8,000	10,500	5,500	(8,000)	2,500
March	7,500	10,000	500	5,500	7,000	4,500
Total	10,000	23,000	11,500	16,500	(1,500)	6,500

Diff: 3
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

63) Perfect Tournaments Inc. (PTI), a sports venue in Atlanta, Georgia that has gross sales of over $30 million a year, has added a check box to the registration form that allows it to retain sports statistics from all the games and as a result of the performance of all participants (players) who compete in its amateur tournaments. The rights do not cost the company anything; however, there is some debate as to whether acquiring and retaining this information offers value to PTI. The controller has asked for the advice of experts and believes that the current database of statistics would have a market value of no more than $1,000. There is speculation that at some point in the future, such statistical information may have some significant value but that is not currently the case. As a result, the controller has decided not to disclose the value of the information rights on the balance sheet or in the notes to the financial statements. Explain what may have guided his decision.

Answer: Even those a case might be made that the information rights are something of value, the value is difficult to measure, it is not significant and its omission would most likely have no influence on the decision made by users of the financial statements.

Diff: 2
Objective: 2.5
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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2.6 Disclosure in the Notes to the Financial Statements

1) The primary purpose of the notes to the financial statements is to further explain the information that is recognized on the face of the financial statements.
Answer: TRUE
Diff: 1
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Application of knowledge

2) If the nature of the entity's primary activities isn't well known or if the activities are complex, then they do *not* need to be disclosed as a note on the financial statements.
Answer: FALSE
Diff: 1
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Application of knowledge

3) Entities should also disclose in the notes to the financial statement's information about the disaggregation of consolidated entities or other units that are managed separately.
Answer: TRUE
Diff: 1
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Application of knowledge

4) Under IFRS, aggregation is useful to summarize a large amount of detail.
Answer: TRUE
Diff: 1
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Application of knowledge

5) The _____ on the financial statements is a unit of information, a heading or a category presented on its own line on the face of the financial statements.
A) line item
B) line disclosure
C) line note
D) line presentation
Answer: A
Diff: 1
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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6) Which is *not* an example of a type of event that is not currently recognized in the financial statements but could impact future cash flows?
A) litigations against the company
B) a contract to deliver goods
C) services that were billed to a customer on account but payment has not been received
D) existing contract to preform services
Answer: C
Diff: 1
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Application of knowledge

7) Under IFRS, _____ includes sorting assets, liabilities, equity income, or expenses based on shared characteristics such as the nature of the item, its role in business activities, or how it is measured.
A) disclosure
B) classification
C) aggregation
D) conceptual framework
Answer: B
Diff: 1
Objective: 2.6
IFRS/GAAP: IFRS
AACSB: Application of knowledge

8) Under IFRS, _____ is the adding together of assets, liabilities, equity, income, or expenses that have shared characteristics and are included in the same classification.
A) disclosure
B) classification
C) aggregation
D) conceptual framework
Answer: C
Diff: 1
Objective: 2.6
IFRS/GAAP: IFRS
AACSB: Application of knowledge

9) What three items should be contained in a note to the financial statements?
Answer:
1. The line items on the financial statements to which the note refers,
2. The reporting entity, or
3. Past events and current conditions that have not yet been recognized in the financial statements but that might affect the entity's cash flows.
Diff: 2
Objective: 2.6
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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10) Under IFRS, effective communication in the financial statements requires:
1.
2.
3.
Answer:
1. *Focusing* on objectives and principles as opposed to focusing on rules.
2. *Classifying* information in a way that groups similar items.
3. *Aggregating* information in a way that does not provide excessive detail but is segregated.
Diff: 2
Objective: 2.6
IFRS/GAAP: IFRS
AACSB: Analytical thinking

2.7 Additional Conceptual Framework Topics: IFRS

1) IASB includes three chapters in its conceptual framework that FASB does not include.
Answer: FALSE
Diff: 1
Objective: 2.7
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

2) The IFRS Conceptual Framework provides a distinction between the objective of financial reporting and the objective of the financial statements.
Answer: TRUE
Diff: 1
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

3) In the IFRS Conceptual Framework, the objective of financial statements is to provide information about the entity's assets, liabilities, equity, income, and expenses that is useful both for assessing future net cash inflows and for assessing the stewardship of economic resources by the entity's management.
Answer: TRUE
Diff: 1
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

4) Chapters that the IASB includes in its conceptual framework but the FASB does not are _____.
A) "Financial Reporting Records" and "Capital Concepts"
B) "Financial Reporting Records" and "Capital Maintenance"
C) "Financial Statements and the Reporting Entity" and "Conceptual Framework"
D) "Financial Statements and the Reporting Entity" and "Concepts of Capital and Capital Maintenance"
Answer: D
Diff: 2
Objective: 2.7
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

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5) Financial reporting is broader and can include financial information outside of the financial statements. For example, other forms of financial reporting include all of the following *except* _____.
A) physical capital maintenance
B) management commentaries
C) interim financial reports
D) press releases
Answer: A
Diff: 2
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

6) Under the concept of _____, capital is regarded in terms of the productive capacity of a company.
A) physical capital maintenance
B) fiscal capital maintenance
C) financial capital maintenance
D) profit capital maintenance
Answer: A
Diff: 2
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

7) Financial capital maintenance refers to the concept that capital is viewed in terms of _____.
A) the comprehensive income
B) the changes in equity for the period
C) the monetary investment in the company
D) the closing cash account
Answer: C
Diff: 2
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

8) Under the concept of _____, capital is viewed as the financial amount, or money amount, invested in a company.
A) physical capital maintenance
B) fiscal capital maintenance
C) financial capital maintenance
D) profit capital maintenance
Answer: B
Diff: 2
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

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9) Describe what is meant by capital maintenance adjustments.
Answer: IFRS defines capital maintenance adjustments as restatements or revaluations of reported amounts of assets and liabilities that companies do not report in net income.
Diff: 2
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

10) What are the two concepts of capital maintenance?
Answer:
1. Financial capital maintenance
2. Physical capital maintenance
Diff: 2
Objective: 2.7
IFRS/GAAP: IFRS
AACSB: Application of knowledge

2.8 Assumptions in Financial Reporting

1) IFRS explicitly addresses the going concern concept.
Answer: TRUE
Diff: 1
Objective: 2.8
IFRS/GAAP: IFRS
AACSB: Application of knowledge

2) Following U.S. GAAP, the going concern concept justifies accounting practices such as depreciation.
Answer: TRUE
Diff: 1
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

3) The going concern concept is explicitly stated in the IFRS conceptual framework but is only implicit in the U.S. GAAP conceptual framework.
Answer: TRUE
Diff: 1
Objective: 2.8
IFRS/GAAP: GAAP/IFRS
AACSB: Application of knowledge

4) The periodicity assumption stipulates that the entity will continue to operate for an indefinite period of time.
Answer: FALSE
Diff: 1
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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5) The economic entity concept stipulates that an entity will measure and report economic activities in monetary units.
Answer: FALSE
Diff: 1
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

6) Which of the following is *not* an underlying assumption in U.S. GAAP financial reporting?
A) economic entity concept
B) monetary unit assumption
C) reliability concept
D) periodicity assumption
Answer: C
Diff: 1
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

7) A company reports financial results each year with the issuance of its income statement and balance sheet. Which underlying assumption is illustrated by this example?
A) economic entity concept
B) going concern concept
C) monetary unit assumption
D) periodicity assumption
Answer: D
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Analytical thinking

8) The _____ justifies the use of depreciation on buildings.
A) economic entity concept
B) monetary unit assumption
C) going concern concept
D) historical cost assumption
Answer: C
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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9) The _____ ignores inflation.
A) economic entity concept
B) monetary unit assumption
C) historical cost assumption
D) business entity concept
Answer: B
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

10) If a company is facing a bankruptcy from which it is quite doubtful that the firm may ever recover, which underlying assumption would *not* be valid?
A) periodicity assumption
B) economic entity concept
C) monetary unit assumption
D) going concern concept
Answer: D
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Analytical thinking

11) Classification of assets on the company's balance sheet into current and long-term illustrates which assumption?
A) going concern concept
B) economic entity concept
C) monetary unit assumption
D) historical cost assumption
Answer: A
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

12) The _____ justifies the use of accrual accounting.
A) historical cost concept
B) going concern concept
C) monetary unit assumption
D) business entity concept
Answer: B
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

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13) Which underlying assumption presumes that the owner's personal residence should *not* be included as an asset on the company balance sheet?
A) monetary unit assumption
B) periodicity assumption
C) economic entity concept
D) common sense assumption
Answer: C
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

14) The _____ stipulates that an entity measure and report its economic activities in dollars (or some other monetary unit).
A) monetary unit assumption
B) business entity concept
C) U.S. banking assumption
D) going concern concept
Answer: A
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

15) Which attribute of a fundamental characteristic makes explicit the assumption of the full disclosure principle?
A) relevance
B) materiality
C) verifiability
D) completeness
Answer: D
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Application of knowledge

16) Recording online sales transactions in bitcoin currency is a violation of _____.
A) the business entity concept
B) common sense
C) the monetary unit assumption
D) the going concern concept
Answer: C
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Analytical thinking

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17) The economic entity concept _____.
A) stipulates all transactions are stated in economic units
B) is applicable to all forms of business organizations
C) requires periodic income measurement
D) recognizes the legal aspects of business organizations
Answer: B
Diff: 2
Objective: 2.8
IFRS/GAAP: GAAP
AACSB: Analytical thinking

18) Preparation of consolidated financial statements when a parent-subsidiary relationship exists is an example of the _____.
A) monetary unit assumption
B) periodicity assumption
C) economic entity concept
D) common sense assumption
Answer: C
Diff: 2
Objective: 2.8
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AACSB: Application of knowledge

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19) Identify the assumption represented in each scenario, and then decide if it is satisfied or violated.

Scenario	Assumption	Satisfied or violated?
Extensive Products Corporation is a publicly traded company. They only issue financial statements to external users every other year.		
Creative Merchandise Inc. adds the cost of land purchased in 2014 to the balance of land purchased in 2000.		
Gary Corp pays the CEO's mortgage and records it as miscellaneous expense.		
Jackson & Company depreciates property, plant, and equipment over their useful lives.		

Answer:

Scenario	Assumption	Satisfied or violated?
Extensive Products Corporation is a publicly traded company. They only issue financial statements to external users every other year.	Periodicity	Violated
Creative Merchandise Inc. adds the cost of land purchased in 2014 to the balance of land purchased in 2000.	Monetary Unit	Satisfied
Gary Corp pays the CEO's mortgage and records it as miscellaneous expense.	Economic Entity	Violated
Jackson & Company depreciates property, plant, and equipment over their useful lives.	Going Concern	Satisfied

Diff: 3
Objective: 2.8
IFRS/GAAP: GAAP
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20) Identify the assumption represented in each scenario, and then decide if it is satisfied or violated.

Scenario	Assumption	Satisfied or violated?
Harold Inc. adjusted the valuation of balance sheet items to keep up with changes in inflation.		
Campers Inc. is facing bankruptcy — they choose not to list assets and liabilities at liquidation values on the balance sheet.		
Template Co. issues quarterly and annual financial statements to external users.		
Texas Studio's president only uses the company limo for business purposes.		

Answer:

Scenario	Assumption	Satisfied or violated?
Harold Inc. adjusted the valuation of balance sheet items to keep up with changes in inflation.	Monetary Unit	Violated
Campers Inc. is facing bankruptcy — they choose not to list assets and liabilities at liquidation values on the balance sheet.	Going concern	Violated
Template Co. issues quarterly and annual financial statements to external users.	Periodicity	Satisfied
Texas Studio's president only uses the company limo for business purposes.	Economic Entity	Satisfied

Diff: 3
Objective: 2.8
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21) Identify the assumption represented in each scenario, and then decide if it is satisfied or violated.

Scenario	Assumption	Satisfied or violated?
Danios Inc. distributes an annual report to shareholders.		
Illeo Industries does not regularly prepare financial statements.		
Maynard Inc.'s president purchases a car to be used solely for personal purposes with company funds.		
Archer Corporation, a publicly traded U.S. company measures financial elements using the dollar.		

Answer:

Scenario	Assumption	Satisfied or violated?
Danios Inc. distributes an annual report to shareholders.	Periodicity	Satisfied
Illeo Industries does not regularly prepare financial statements.	Periodicity	Violated
Maynard Inc.'s president purchases a car to be used solely for personal purposes with company funds.	Economic Entity	Violated
Archer Corporation, a publicly traded U.S. company measures financial elements using the dollar.	Monetary Unit	Satisfied

Diff: 3
Objective: 2.8
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AACSB: Analytical thinking

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