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**QUESTION 1**

ABC Co., a development stage enterprise, incurred the following costs during its first year of operations:

Legal fees for incorporation and other related matters	55,000
Underwriters' fees for initial stock offering	40,000
Exploration costs and purchases of mineral rights	60,000

ABC had no revenue during its first year of operation. What amount may ABC capitalize as organizational costs?

A. \$115,000

B. \$95,000

C. \$55,000

D. \$0

Correct Answer: D

Explanation:

	<i>Capitalize as organizational costs</i>
Legal fees for incorporation and other related matters should be expensed as start-up costs	-
Underwriting fees for initial stock offering should be recorded as a reduction of contributed capital	-
Exploration costs should be expensed as research & development	-
Purchases of mineral rights should be capitalized as fixed assets	-
Capitalize as organizational costs	<u>0</u>

Choice "d" is correct. \$0.

All organizational costs (start-up costs) should be expensed when incurred (per SOP 98-5).

QUESTION 2

Which of the following audit procedures is best for identifying unrecorded trade accounts payable?

A. Examining unusual relationships between monthly accounts payable balances and recorded cash payments.

B. Reconciling vendors' statements to the file of receiving reports to identify items received just prior to the balance sheet date.



C. Reviewing cash disbursements recorded subsequent to the balance sheet date to determine whether the related payables apply to the prior period.

D. Investigating payables recorded just prior to and just subsequent to the balance sheet date to determine whether they are supported by receiving reports.

Correct Answer: C

Explanation: Choice "c" is correct. Unrecorded trade accounts payable are best identified by reviewing cash disbursements recorded subsequent to the balance sheet date to determine whether the related payables apply to the prior period. Choice "a" is incorrect. There is not usually a predictable relationship between accounts payable and cash payments, because management can pay cash or incur additional liabilities at its discretion. Choice "b" is incorrect. Reconciling vendors' statements to the file of receiving reports would not identify unrecorded payables, as the vendor statement would still agree with the receiving report even if the payable were not recorded. Choice "d" is incorrect. Investigating payables already recorded would not help identify unrecorded trade payables.

QUESTION 3

Tracing bills of lading to sales invoices provides evidence that:

A. Shipments to customers were recorded as sales.

B. Recorded sales were shipped.

C. Invoiced sales were shipped.

D. Shipments to customers were invoiced.

Correct Answer: D

Explanation:

Choice "d" is correct. Tracing from a population of bills of lading (shipping documents) to sales invoices provides evidence that shipments to customers were invoiced.

Choice "a" is incorrect. Tracing bills of lading to the sales invoice provides assurance that shipments to customers were invoiced, not that they were recorded as sales.

Choice "b" is incorrect. Tracing from the sales journal to bills of lading provides evidence that recorded sales were shipped.

Choice "c" is incorrect. Tracing from a population of sales invoices to the bills of lading provides evidence that invoiced sales were shipped.

QUESTION 4

Eller, Fort, and Owens do business as Venture Associates, a general partnership. ABC Corp. brought a breach of contract suit against Venture and Eller individually. ABC won the suit and filed a judgment against both Venture and Eller. ABC will generally be able to collect the judgment from:



- A. Partnership assets only.
- B. The personal assets of Eller, Fort, and Owens only.
- C. Eller's personal assets only after partnership assets are exhausted.
- D. Eller's personal assets only.

Correct Answer: C

Explanation:

Choice "c" is correct. When a judgment is obtained against both a partnership and an individual general partner, the plaintiff must proceed against the partnership assets first and then the assets of any individual general partner. The partnership assets must be exhausted before any general partner's individual assets can be attached. Choices "a", "b", and "d" are incorrect, per the above rule.

QUESTION 5

ABC Corp. discloses supplemental industry segment information. The following information is available for 1992:

<u>Segment</u>	<u>Sales</u>	<u>Traceable operating expenses</u>
A	\$ 20,000	\$ 12,000
B	16,000	10,000
C	12,000	7,000
	<u>\$ 48,000</u>	<u>\$ 29,000</u>

Additional 1992 expenses, not included above, are as follows:

Indirect operating expenses \$7,200 General corporate expenses 4,800

Segment C's 1992 operating profit was:

- A. \$5,000
- B. \$3,200
- C. \$2,600
- D. \$2,000

Correct Answer: A

Explanation:

Choice "a" is correct. \$5,000 operating profit for Segment C.



Rule: Operating profit by segments is based on the measure of profit reported to the "Chief Operating Decision Maker."

Interest expense, income taxes, and general corporate expenses are not allocated to the divisions solely for the purposes of segment disclosures; they may be allocated if that is how the segments report to the "Chief Operating Decision Maker."

Segment C's sales	\$12,000
Less traceable operating expenses	(7,000)
Segment C operating profit	<u>\$ 5,000</u>

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