CPA-TEST Q&As

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QUESTION 1

In open market transactions, ABC Corp. simultaneously sold its long-term investment in XYZ Corp. bonds and purchased its own outstanding bonds. The broker remitted the net cash from the two transactions. ABC\\'s gain on the purchase of its own bonds exceeded its loss on the sale of the XYZ bonds. Assume the transaction to purchase its own outstanding bonds is unusual in nature and has occurred infrequently. ABC should report the:

A. Net effect of the two transactions as an extraordinary gain.

B. Net effect of the two transactions in income before extraordinary items.

C. Effect of its own bond transaction gain in income before extraordinary items, and report the Iron bond transaction as an extraordinary loss.

D. Effect of its own bond transaction as an extraordinary gain, and report the XYZ bond transaction loss in income before extraordinary items.

Correct Answer: D

Explanation: Choice "d" is correct, these are two separate transactions because ABC Corp. (1) sold XYZ Corp. bonds (an investment) for a loss, and, (2) bought back its own (ABC) Corp. bonds (a debt) for a gain. This is not a

"refinancing" (where one would sell new bond debt to buy back old bond debt outstanding).

The gain from the purchase of its own bonds is an "extraordinary gain" because it is both unusual in nature

and infrequently occurring (per APB Opinion No. 30 and SFAS No. 145). The XYZ Corp. transaction is a

loss in "income before extraordinary items."

Choices "a" and "b" are incorrect. The two transactions are separate and cannot be netted.

Choice "c" is incorrect. Just the opposite. The sale of the investment is a loss in "income before

extraordinary items," while the purchase of its bond debt is an "extraordinary gain" according to the

provisions of APB Opinion No. 30.

QUESTION 2

Equipment acquisitions that are misclassified as maintenance expense most likely would be detected by an internal control activity that provides for:

A. Segregation of duties of employees in the accounts payable department.

B. Independent verification of invoices for disbursements recorded as equipment acquisitions.

C. Investigation of variances within a formal budgeting system.

D. Authorization by the board of directors of significant equipment acquisitions.

Correct Answer: C

Explanation:

Choice "c" is correct. Equipment acquisitions that are misclassified as maintenance expense most likely would be detected by internal control procedures that provide for investigation of variances within a formal budgeting system.

Choice "a" is incorrect. Segregation of duties of employees in the accounts payable department would not prevent the misclassification of equipment acquisitions as maintenance expense.

Choice "b" is incorrect. Verifying invoices for disbursements already recorded as equipment acquisitions would not include examining invoices for disbursements recorded as maintenance expense.

Choice "d" is incorrect. Since the authorization by the board of directors occurs before the disbursement is recorded, this control would not prevent any misclassification.

QUESTION 3

Lisa is a limited partner in a limited partnership. Jen, one of the other limited partners, is seeking to sell her interest in the partnership to Karen and allow Karen to become a new limited partner. Which of the following statements is true?

A. Lisa may engage in the management of the limited partnership without losing her limited liability.

B. Jen may transfer her interest and make Karen a new limited partner without the approval of the other partners.

C. Jen may withdraw from the limited partnership without giving notice to the partnership.

D. Lisa has a right to vote on the transferring of interest to and admission of Karen as a limited partner.

Correct Answer: D

Explanation:

Choice "d" is correct. Limited partners have the right to vote on the transfer of interest and admission of a new partner. Admission of a new partner requires unanimous consent.

Choice "a" is incorrect. A limited partner who acts as a general partner loses her limited liability status to those she acted as a general partner towards.

Choice "b" is incorrect. Partners can freely transfer their interests in profits and losses to third parties, but the third party cannot become a limited partner without the unanimous consent of the other partners.

Choice "c" is incorrect. Limited partners must give 6 months notice of withdrawal in absence of an agreement to the contrary.

QUESTION 4

Kane, CPA, concludes that there is substantial doubt about ABC Co.\\'s ability to continue as a going concern for a reasonable period of time. If ABC\\'s financial statements adequately disclose its financial difficulties, Kane\\'s auditor\\'s report is required to include an explanatory paragraph that specifically uses the phrase(s):

	"Possible discontinuance of operations"	*"Reasonable period of time, not to exceed one year"*
A.	Yes	Yes
B.	Yes	No
C.	No	Yes
D.	No	No

A. Option A

B. Option B

C. Option C

D. Option D

Correct Answer: D

Explanation: Choice "d" is correct. If, after considering identified conditions and events and management\\'s plans, the auditor concludes that substantial doubt about the entity\\'s ability to continue as a going concern for a reasonable period of time remains, the audit report should include an explanatory paragraph (following the opinion paragraph) to reflect that conclusion. This conclusion should be expressed through the use of the phrase "substantial doubt about its (the entity\\'s) ability to continue as a going concern" [or similar wording that includes the terms "substantial doubt" and "going concern"]. The "reasonable period...not to exceed one year" is inherent in the definition of going concern and is not explicitly stated in the audit report. The phrase "possible discontinuation of operations" may be included in the going concern disclosure but is not specifically required. Choices "a", "b", and "c" are incorrect, as per the above explanation.

QUESTION 5

If, in a competitive market, a price ceiling is imposed establishing a maximum price below the market equilibrium price, this price ceiling would result in:

A. Shortages because the quantity demanded would exceed the quantity supplied.

B. No effect on the quantity supplied or demanded.

C. Surpluses because the quantity supplied would exceed the quantity demanded.

D. Surpluses because the supply curve would shift to the right.

Correct Answer: A

Explanation:

Choice "a" is correct. Setting a ceiling price below the price dictated by the market (as established by the equilibrium price) would create excess demand and a shortage.

Choices "b", "c", and "d" are incorrect, per above Explanation.