FINANCIAL-ACCOUNTING-AND-REPORTING Q&As

Certified Public Accountant (Financial Accounting & Reporting)

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QUESTION 1

According to the FASB conceptual framework, the objectives of financial reporting for business enterprises are based on:

A. The need for conservatism.

B. Reporting on management\\'s stewardship.

C. Generally accepted accounting principles.

D. The needs of the users of the information.

Correct Answer: D

Choice "d" is correct. The FASB conceptual framework states that the objectives of financial reporting stem from the informational needs of the external users of the information. SFAC 1 para. 28 Choice "a" is incorrect. Conservatism is an underlying concept for financial accounting but is not the basis for the objectives. SFAC 2 para. 91-97 Choice "b" is incorrect. Information concerning management\\'s stewardship is only one aspect of the information financial statements are intended to provide. SFAC 1 para. 50 Choice "c" is incorrect. Generally accepted accounting principles (GAAP) are derived from and based on the objectives of financial reporting, not the other way around.

QUESTION 2

APB Opinion No. 28, Interim Financial Reporting, concluded that interim financial reporting should be viewed primarily in which of the following ways?

A. As useful only if activity is spread evenly throughout the year.

B. As if the interim period were an annual accounting period.

C. As reporting for an integral part of an annual period.

D. As reporting under a comprehensive basis of accounting other than GAAP.

Correct Answer: C

Choice "c" is correct. Interim financial reporting should be viewed as reporting for an integral part of an

annual period.

Choices "a", "b", and "d" are incorrect, per the above rule.

QUESTION 3

On January 2, 1993, Quo, Inc. hired Reed to be its controller. During the year, Reed, working closely with

Quo\\'s president and outside accountants, made changes in accounting policies, corrected several errors

dating from 1992 and before, and instituted new accounting policies.

Quo\\'s 1993 financial statements will be presented in comparative form with its 1992 financial statements.

This question represents one of Quo\\'s transactions. List B represents the general accounting treatment

required for these transactions. These treatments are:

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Cumulative effect approach - Include the cumulative effect of the adjustment resulting from the accounting change or error correction in the 1993 financial statements, and do not restate the 1992 financial statements.

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Retroactive or retrospective restatement approach - Restate the 1992 financial statements and adjust 1992 beginning retained earnings if the error or change affects a period prior to 1992.

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Prospective approach - Report 1993 and future financial statements on the new basis but do not restate 1992 financial statements.

Item to Be Answered Quo manufactures heavy equipment to customer specifications on a contract basis. On the basis that it is preferable, accounting for these long-term contracts was switched from the completed-contract method to the percentage-of-completion method.

List B (Select one)

A. Cumulative effect approach.

B. Retroactive or retrospective restatement approach.

C. Prospective approach.

Correct Answer: B

Choice "B" is correct. Changes in accounting principle are handled "retrospectively." Beginning retained earnings of the earliest year presented is adjusted for the cumulative effect of the change and all prior year financial statements are restated.

QUESTION 4

Which of the following information should be included in Melay, Inc.\\'s 1992 summary of significant accounting policies?

A. Property, plant, and equipment is recorded at cost with depreciation computed principally by the straight-line method.

B. During 1992, the Delay component was sold.

C. Business segment 1992 sales are Alay $1M, Belay $2M, and Celay $3M.

D. Future common share dividends are expected to approximate 60% of earnings.

Correct Answer: A

Choice "a" is correct. Computing depreciation principally by the straight-line method is a GAAP method of depreciation that should be described in the "summary of significant accounting policies." Choice "b" is incorrect. Disclosing the sale of a component of a business is required (and is covered in the lecture on "discontinued operations" in the F1 class) but is not a "significant accounting policy." Choice "c" is incorrect. Disclosing "sales" of segments is required, but is not a "significant accounting policy." Choice "d" is incorrect. "Estimates of future common share dividends" are not appropriate disclosures for the financial statements. They might be appropriate for the "presidents letter to shareholders."

QUESTION 5

How should the effect of a change in accounting principle that is inseparable from the effect of a change in accounting estimate be reported?

A. As a component of income from continuing operations.

B. By restating the financial statements of all prior periods presented.

C. As a correction of an error.

D. By footnote disclosure only.

Correct Answer: A

Choice "a" is correct. When the effect of a change in accounting principle is inseparable from the effect of a change in accounting estimate, the reporting treatment for the overall effect is as a change in estimate. Thus, the effect is reported prospectively as a component of income from continuing operations. Under SFAS No. 154, this type of change is now called a change in accounting estimate affected by a change in accounting principle. Choice "b" is incorrect. Restatement of all prior periods is the retroactive accounting treatment that is applied to the correction of an error and the retrospective accounting treatment given to changes in accounting principle. However, a change in accounting principle that is inseparable from the effect of a change in accounting estimate is now treated as a change in accounting estimate. Choice "c" is incorrect. Correction of an error is given retroactive treatment as a prior period adjustment to retained earnings with restatement of prior periods. This is not the treatment appropriate for the effect of a change in accounting principle that is inseparable from the effect of a change in accounting estimate. Choice "d" is incorrect. While footnote disclosure is always appropriate for an accounting change, such disclosure alone is never the appropriate accounting treatment.