Question #1 of 30

Question ID: 1573508

An analyst has gathered the following information about a company:

Balance Sheet	
Assets	
Cash	100
Accounts Receivable	750
Marketable Securities	300
Inventory	850
Property, Plant & Equip	900
Accumulated Depreciation	(150)
Total Assets	2750
Liabilities and Equity	
Accounts Payable	300
Short-Term Debt	130
Long-Term Debt	700
Common Stock	1000
Retained Earnings	620
Total Liab. and Stockholder's equity	2750

Income Statement	
Sales	1500
COGS	1100
Gross Profit	400
SG&A	150
Operating Profit	250
Interest Expense	25
Taxes	75
Net Income	150

What is the quick ratio?

A) 0.62.

B) 1.53.

C) 2.67.

Explanation

Quick ratio = [100(cash) + 750(AR) + 300(marketable securities)] / [300(AP) + 130(short-term debt)] = (1,150 / 430) = 2.67

(Module 31.1, LOS 31.e)

Question #2 of 30

Question ID: 1573506

Selected balance sheet data for Parker Company are as follows:

Current assets	3,000
Long-lived assets	7,000
Total assets	10,000
Current liabilities	2,000
Long-term liabilities	4,000
Total liabilities	6,000
Shareholders' equity	4,000

On a common-size balance sheet, Parker's current liabilities would be stated as:

A) 33%.

B) 67%.

C) 20%.

Explanation

On a common-size balance sheet, each line item is stated as a percentage of total assets: 2,000 / 10,000 = 20%.

(Module 31.1, LOS 31.e)

Question #3 of 30

Question ID: 1577943

Under U.S. GAAP, the balance sheet value of a debt security classified as held-to-maturity is its:

A) historical cost.

B) amortized cost.

C) fair value.

Explanation

Under U.S. GAAP, held-to-maturity securities are carried on the balance sheet at their amortized cost.

(Module 31.1, LOS 31.c)

Question #4 of 30

Question ID: 1577944

A U.S. GAAP reporting firm invests some of its cash in equity securities that have quoted market prices. The firm may classify these securities as:

A) trading securities only.

B) available-for-sale securities only.

C) trading securities, unless it elects at the time of purchase to classify them as available-for-sale.

Explanation

U.S. GAAP requires equity securities to be classified as trading securities. IFRS offers firms an irrevocable choice at the time of purchase to account for equity securities as measured at fair value through other comprehensive income.

(Module 31.1, LOS 31.c)

Question #5 of 30

Question ID: 1573502

In Country Norlatia, revenue is recognized in the income statement when a sale is made. Which of the following tax treatments would *most likely* result in a deferred tax liability?

A) Revenue is taxable when a sale is made.

B) Revenue is not taxable.

C) Revenue is taxable when the cash is received from the customer.

Explanation

There may be a temporary timing difference between when a sale is made and when cash is received. If the customer does not pay immediately, the revenue has been recognized in the income statement before it becomes taxable. This will be taxable at a later date and, as a result, a deferred tax liability will be created. If revenue was taxable when a sale is made, there would be no difference between accounting and tax treatment. If revenue was not taxable, this would be a permanent difference. Deferred taxes are only used for temporary timing differences.

(Module 31.1, LOS 31.d)

Question #6 of 30

Question ID: 1573499

The U.S. GAAP treatment of trading securities is the same as the IFRS treatment of securities measured at:

A) amortized cost.

B) fair value through profit and loss.

C) fair value through other comprehensive income.

Explanation

Trading securities are measured at fair value through profit and loss under both U.S. GAAP and IFRS. Any unrealized gain/loss is recognized in the income statement, along with any interest/dividend income and realized gains/losses.

(Module 31.1, LOS 31.c)

Question #7 of 30

Question ID: 1577945

Under IFRS, which types of financial assets may a firm elect to carry at fair value through profit and loss?

A) Any financial asset.

B) Debt instruments only.

C) Equity or debt securities, but not derivatives.

Explanation

Under IFRS, firms can make an irrevocable choice to carry any financial asset at fair value through profit and loss.

(Module 31.1, LOS 31.c)

Question #8 of 30

Question ID: 1577940

Balance sheet goodwill is *most* accurately described as the:

A) amount by which the purchase price of an acquired firm exceeds its identifiable net assets.

B) intangible value a firm creates in excess of its identifiable net assets.

C) value derived from the expected future performance of a firm.

Explanation

Accounting goodwill is the amount by which the purchase price of an acquired firm is greater than the fair value of its identifiable net assets. Internally generated goodwill is not recognized on a firm's balance sheet. Value from the expected future performance of a firm is referred to as "economic goodwill" to distinguish it from accounting goodwill.

(Module 31.1, LOS 31.b)

Question #9 of 30

Question ID: 1573498

James Alexander, Inc., paid par of $220,000 for 5% coupon bonds in Charles Michael, Inc. By the end of the accounting period, the fair value of the bonds was $212,000. The firm plans to hold these bonds for a few years but sell them before maturity. What will be the *most likely* impact on net income at the end of the first year?

A) Net income will be unaffected.

B) Net income will decrease.

C) Net income will increase.

Explanation

These bonds will be classified as fair value through other comprehensive income, or available-for-sale securities under U.S. GAAP. Any interest income will increase net income. The bonds will be recognized at fair value ($212,000) at the end of the year, and the unrealized loss of $8,000 will be recognized in other comprehensive income.

(Module 31.1, LOS 31.c)

Question #10 of 30

Question ID: 1573492

Which of the following scenarios would *most likely* result in the greatest goodwill recognized on the balance sheet?

A) Building up Brand Y internally, with estimated goodwill of $95,000.

B) Acquiring Firm X for $500,000, with goodwill calculated at $90,000.

C) Purchasing Company Z for $700,000, where the fair value of the net identifiable assets is $800,000.

Explanation

Only acquiring Firm X will result in goodwill being recorded on the balance sheet. Internally generated goodwill is expensed on the income statement. The purchase of Company Z resulted in a gain from a bargain purchase of $100,000 as the amount paid was less than the fair value of net identifiable assets. This gain will be recognized as income on the income statement.

(Module 31.1, LOS 31.b)

Question #11 of 30

Question ID: 1573507

A segment of a common-size balance sheet for Olsen Company in its most recent year shows the following data:

Common stock	1%
Additional paid-in capital	19%
Preferred stock	15%

How should an analyst most appropriately interpret these data?

A) Shareholders' equity is 35% of total assets.

B) Preferred stock is 15% of shareholders' equity.

C) Proceeds from the issuance of common stock are 20% of total assets.

Explanation

Common-size balance sheets express each balance sheet item as a percentage of total assets. Contributed capital from issuing common shares may be included in common stock (at par value) or additional paid-in capital (for proceeds in excess of par value). Shareholders' equity is unlikely to consist only of common and preferred stock, as it also includes components such as retained earnings and accumulated other comprehensive income.

(Module 31.1, LOS 31.e)

Question #12 of 30

Question ID: 1573495

If a firm wishes to manipulate its net income upward in the year it purchases another company, which of the following would *most likely* make this possible?

A) Overvaluing goodwill and overvaluing the acquired identifiable assets.

B) Overvaluing goodwill and undervaluing the acquired identifiable assets.

C) Undervaluing goodwill and overvaluing the acquired identifiable assets.

Explanation

Goodwill is not amortized, so it will not impact the income statement (unless subject to impairment). By allocating more of the acquisition price to goodwill and less to the acquired identifiable assets, the firm will charge less depreciation on the identifiable assets—and, as a result, increase net income. In future years, overvaluing goodwill could cause a higher chance of impairment if revalued appropriately. Overvaluing the identifiable assets will lead to higher depreciation and lower net income. Overvaluing both will cause the balance sheet to no longer balance.

(Module 31.1, LOS 31.b)

Question #13 of 30

Question ID: 1573509

Given the following income statement and balance sheet for a company:

Balance Sheet		
Assets	*Year 2003*	*Year 2004*
Cash	500	450
Accounts Receivable	600	660
Inventory	500	550
Total CA	1600	1660
Plant, prop. equip	1000	1250
Total Assets	2600	2910
Liabilities		
Accounts Payable	500	550
Long term debt	700	1002
Total liabilities	1200	1552

Equity		
Common Stock	400	538
Retained Earnings	1000	820
Total Liabilities & Equity	2600	2910

Income Statement	
Sales	3000
Cost of Goods Sold	(1000)
Gross Profit	2000
SG&A	(500)
Interest Expense	(151)
EBT	1349
Taxes (30%)	(405)
Net Income	944

What is the current ratio for 2004?

A) 0.331.

B) 2.018.

C) 3.018.

Explanation

Current ratio = (CA / CL) = (1,660 / 550) = 3.018

(Module 31.1, LOS 31.e)

Question #14 of 30

Question ID: 1573496

Interest income from a financial asset is recorded on the income statement if the underlying financial asset is recognized as:

A) trading only.

B) held to maturity, trading, or available for sale.

C) trading or available for sale.

Explanation

Interest/dividend income and realized gains/losses are recognized on the income statement for all three classifications of financial assets. The different accounting treatments relate to unrealized gains/losses and the value on the balance sheet (fair value for trading and available for sale; amortized cost for held to maturity).

(Module 31.1, LOS 31.c)

Question #15 of 30

Question ID: 1573497

Anne is trying to classify some financial assets under IFRS and states the following:

Statement 1:	Unlisted equity securities are always measured at amortized cost.
Statement 2:	Listed equity securities are always measured at fair value through profit and loss.

Which of these statements is *most likely* correct?

A) Statement 2 only.

B) Neither Statement 1 nor Statement 2.

C) Statement 1 only.

Explanation

Unlisted equity securities are measured at amortized cost if the fair value cannot be determined reliably. The default classification for listed equity securities under IFRS is fair value through profit and loss, but the firm can choose at the time of purchase to measure at fair value through other comprehensive income.

(Module 31.1, LOS 31.c)

Question #16 of 30

Question ID: 1573510

The following data is from Delta's common size financial statement:

Earnings after taxes	18%
Equity	40%
Current assets	60%
Current liabilities	30%
Sales	$300
Total assets	$1,400

What is Delta's total-liabilities-to-equity ratio?

A) 1.0.

B) 1.5.

C) 2.0.

Explanation

If equity = 40% of assets, total liabilities = 60% of assets, thus 60 / 40 = 1.5.

(Module 31.1, LOS 31.e)

Question #17 of 30

Question ID: 1573489

Which of the following is classified as an identifiable intangible asset?

A) Goodwill.

B) A security investment.

C) A trademark.

Explanation

Identifiable intangible assets are nonmonetary assets that lack physical substance, which can be acquired separately. Goodwill cannot be acquired separately; therefore, it is an unidentifiable intangible asset. Securities are considered tangible rather than intangible assets.

(Module 31.1, LOS 31.a)

Question #18 of 30

Question ID: 1573500

A firm holds the following:

1. Derivative assets
2. Debt securities to be sold in the immediate future
3. Debt securities to be held until maturity

How many of these can be measured at fair value through profit or loss (FVTPL)?

A) Two under both U.S. GAAP and IFRS.

B) Two under IFRS, and all three under U.S. GAAP.

C) Two under U.S. GAAP, and all three under IFRS.

Explanation

The derivative assets and trading securities will be held at FVTPL under both IFRS and U.S. GAAP. The debt securities being held to maturity will be measured at amortized cost under U.S. GAAP. These will commonly be measured at amortized cost under IFRS, but firms can make an irrevocable choice to carry any financial assets at FVTPL—and could, therefore, measure all three at FVTPL under IFRS.

(Module 31.1, LOS 31.c)

Question #19 of 30

Question ID: 1577939

A company purchases an intangible asset for which an active market exists. The company may present the intangible asset's value using the revaluation model if it reports its financial statements under:

A) neither IFRS nor U.S. GAAP.

B) either IFRS or U.S. GAAP.

C) IFRS, but not U.S. GAAP.

Explanation

If an active market exists for a purchased intangible asset, IFRS permits companies to report its value using the revaluation model. U.S. GAAP requires the cost model for purchased intangible assets.

(Module 31.1, LOS 31.a)

Question #20 of 30

Question ID: 1577942

Under U.S. GAAP, unrealized gains and losses on trading securities are:

A) not recognized in the financial statements.

B) recognized in other comprehensive income.

C) recognized in the income statement.

Explanation

Under U.S. GAAP, unrealized gains and losses on trading securities are recognized in the income statement.

(Module 31.1, LOS 31.c)

Question #21 of 30

Question ID: 1573490

Adler, Inc., purchases an identifiable intangible asset on January 1, 20X7, for $100k. The firm's policy is to amortize similar intangible assets on a straight-line basis over five years, based on their useful life. The fair value of the intangible asset on December 13, 20X7, is $83,000. The asset will be recorded on the balance sheet at December 13, 20X7, under U.S. GAAP at:

A) $80,000.

B) $83,000.

C) $100,000.

Explanation

Under U.S. GAAP, intangible assets must be held under the cost model. The revaluation model is not allowed; therefore, the asset cannot be revalued to $83,000, unlike under IFRS. Some intangibles that have indefinite lives, such as goodwill, are not amortized and remain at cost, with annual impairment reviews. This asset has a useful life of five years and will be amortized by $20,000 ($100,000 / 5) for the year, giving a balance sheet value of $80,000 at December 13, 20X7.

(Module 31.1, LOS 31.a)

Question #22 of 30

Question ID: 1573491

Heath Ltd., a pharmaceutical firm, has been working on a new vaccine. At the beginning of the year, the firm incurred £780,000 in initial testing costs, which proved that the vaccine is technically feasible. The firm now plans to commence production and has secured a contract with the government for sales. It expects to spend £95,000 in training costs, £530,000 in materials and direct labor, and £260,000 in production overhead. Under IFRS, how much should be expensed?

A) £1,135,000.

B) £780,000.

C) £875,000.

Explanation

Total expenses = £780,000 initial testing costs + £95,000 training costs = £875,000.

Under IFRS, any costs incurred during the research phase should be expensed (the initial £780,000). Costs incurred during development are capitalized. Heath Ltd. moved from research to development at the point where the vaccine was proven technically feasible, a market exists for the product (the contract with the government), and it has the intention and resources to complete and sell the vaccine. Training costs are always expensed, regardless of whether they are incurred during research or development. The development costs for materials, direct labor, and production overhead will be capitalized. Note that if the firm incurred any costs for administrative overhead, these would also be expensed.

(Module 31.1, LOS 31.a)

Question #23 of 30

Question ID: 1577946

Typically, companies report non-current liabilities on the balance sheet at:

A) issuance price.

B) amortized cost.

C) fair value.

Explanation

Non-current liabilities are usually carried at amortized cost, which is the issue price minus any principal payments, plus any amortized discount or minus any amortized premium.

(Module 31.1, LOS 31.d)

Question #24 of 30

Question ID: 1573494

When comparing firms, which of the following is the *most accurate* approach to adjusting goodwill to enable analysis?

A) Remove goodwill from the balance sheet and remove any income statement impact.

B) Remove goodwill from the balance sheet only, as goodwill does not impact the income statement.

C) No adjustments should be made to either the balance sheet or income statement.

Explanation

Goodwill is subjective and should be removed from the balance sheet for analytical purposes. Even though goodwill is not amortized, it can impact the income statement if it is impaired, or if a gain from a bargain purchase has occurred. Any income statement impact should also be removed.

(Module 31.1, LOS 31.b)

Question #25 of 30

Question ID: 1573504

Balance sheet data for two comparable firms are presented below:

	Amplus, Inc.	Brevis, Inc.
Cash and equivalents	3,800	500
Accounts receivable	2,400	700
Inventories	5,800	1,100
Current assets	12,000	2,300
Land	400	100
Property, plant and equipment	24,600	6,400
Noncurrent assets	25,000	6,500
Total assets	**37,000**	**8,800**
Accounts payable	1,800	400
Unearned revenue	600	100
Current liabilities	2,400	500
Long-term borrowing	9,600	3,300
Total liabilities	12,000	3,800
Common stock	1,500	300
Retained earnings	23,500	4,700
Total equity	25,000	5,000
Total liabilities and equity	**37,000**	**8,800**

Based on common-size analysis of the two firms' balance sheets, Amplus Company:

A) has a greater investment in working capital than Brevis Company.

B) is more financially leveraged than Brevis Company.

C) uses relatively more fixed assets then Brevis Company.

Explanation

Common-size balance sheets for the two firms are as follows:

	Amplus, Inc.	Brevis, Inc.
Cash and equivalents	10.3%	5.7%
Accounts receivable	6.5%	8.0%
Inventories	15.7%	12.5%
Current assets	32.4%	26.1%
Land	1.1%	1.1%
Property, plant and equipment	66.5%	72.7%
Noncurrent assets	67.6%	73.9%
Total assets	100.0%	100.0%
Accounts payable	4.9%	4.5%
Unearned revenue	1.6%	1.1%
Current liabilities	6.5%	5.7%
Long-term borrowing	25.9%	37.5%
Total liabilities	32.4%	43.2%
Common stock	4.1%	3.4%
Retained earnings	63.5%	53.4%
Total equity	67.6%	56.8%
Total liabilities and equity	100.0%	100.0%

Working capital (current assets minus current liabilities) is 32.4% – 6.5% = 25.9% of assets for Amplus and 26.1% – 5.7% = 20.4% of assets for Brevis. Fixed assets (property, plant, and equipment) are relatively larger for Brevis than for Amplus. Based on long-term borrowing and total liabilities, Brevis is significantly more leveraged than Amplus.

(Module 31.1, LOS 31.e)

Question #26 of 30

Question ID: 1577941

Under U.S. GAAP, unrealized gains and losses on available-for-sale securities are:

A) recognized in the income statement.

B) not recognized in the financial statements.

C) recognized in other comprehensive income.

Explanation

Under U.S. GAAP, unrealized gains and losses on available-for-sale securities are recognized in other comprehensive income.

(Module 31.1, LOS 31.c)

Question #27 of 30

Question ID: 1573493

Which of the following is *most accurate* regarding accounting goodwill?

A) The carrying value considers both the past acquisition cost and the future expected performance. ✓

B) The carrying value considers only the past acquisition cost. ✗

C) The carrying value considers only the future expected performance. ✗

Explanation

While the initial recognition of purchased goodwill is based on the acquisition cost compared to the net identifiable assets obtained, goodwill must be tested for impairment at least annually. One key indicator of impairment would be where the expected future excess returns to be earned from the acquired business have fallen compared to when initially purchased. Therefore, the carrying value considers both the past and the future.

Economic goodwill only looks at the expected future performance of the firm and does not appear in the financial statements.

(Module 31.1, LOS 31.b)

Question #28 of 30

Question ID: 1573501

The amortization of a bond issued at a premium will *most likely* result in:

A) an increase in net income. ✓

B) a decrease in net income. ✗

C) no impact on net income. ✗

Explanation

The bond will be initially recorded at its issue price on the balance sheet. This will be amortized and gradually reduce to par over the life of the bond. This amortization will reduce the liability and be recognized as a gain in the income statement, thereby increasing net income.

(Module 31.1, LOS 31.d)

Question #29 of 30

Question ID: 1573503

Which of the following financial liabilities will *most likely* be held at fair value on the balance sheet?

A) Derivatives.

B) Bonds.

C) Bank loans.

Explanation

Derivatives can be financial assets or liabilities and are recognized at fair value on the balance sheet. Bank loans will most likely be issued at face value and reported on the balance sheet at the same amount. If a bond is issued at a premium or discount to par, it will be held at amortized cost.

(Module 31.1, LOS 31.d)

Question #30 of 30

Question ID: 1573505

Common size balance sheets express all balance sheet items as a percentage of:

A) equity.

B) sales.

C) assets.

Explanation

Common size balance sheets express all balance sheet items as a percentage of assets. Common size income statements express all income statement items as a percentage of sales.

(Module 31.1, LOS 31.e)