



Following are multiple choice questions recently released by the AICPA. These questions were released by the AICPA with letter answers only. Our editorial board has provided the accompanying explanations.

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2006 AICPA Newly-Released Financial Questions

Which of the following should be disclosed in a summary of significant accounting policies?

- a. Basis of profit recognition on long-term construction contracts.
- b. Future minimum lease payments in the aggregate and for each of the five succeeding fiscal years.
- c. Depreciation expense.
- d. Composition of sales by segment.

ANSWER:

Choice "a" is correct. The summary of significant accounting policies should disclose policies. The only policy in this question is the "basis" of profit recognition on long-term construction contracts. The other disclosures are accounting details and would be disclosed in other footnotes, but not in the summary of significant accounting policies.

Choice "b" is incorrect. The future minimum lease payments should be disclosed, but not in the summary of significant accounting policies.

Choice "c" is incorrect. Depreciation expense should certainly be disclosed, but not in the summary of significant accounting policies.

Choice "d" is incorrect. The composition of sales by segment should be disclosed, but not in the summary of significant accounting policies.

2006 AICPA Newly-Released Financial Questions

A capital projects fund for a new city courthouse recorded a receivable of \$300,000 for a state grant and a \$450,000 transfer from the general fund. What amount should be reported as revenue by the capital projects fund?

- a. \$0
- b. \$300,000
- c. \$450,000
- d. \$750,000

ANSWER:

Choice "b" is correct. The state grant would be reported as revenue in the capital projects fund, and the transfer from the general fund would not (it would be recorded as an "other financing source" and not as revenue). Thus, revenue is \$300,000. The receivable associated with this capital project assumes revenues have been earned by either incurring eligible capital outlay expenditures or by satisfaction of other pertinent grant requirements prior to accruing the receivable.

Choice "a" is incorrect. Per the above explanation, the \$300,000 state grant is revenue, so this answer cannot be correct.

Choice "c" is incorrect. The \$450,000 transfer from the general fund is not revenue. It is classified as an "other financing source."

Choice "d" is incorrect. The \$450,000 transfer from the general fund is not revenue, so this answer, which combines the \$300,000 in revenue with the \$400,000 transfer, is incorrect.

2006 AICPA Newly-Released Financial Questions

Cart Co. purchased an office building and the land on which it is located for \$750,000 cash and an existing \$250,000 mortgage. For realty tax purposes, the property is assessed at \$960,000, 60% of which is allocated to the building. At what amount should Cart record the building?

- a. \$500,000
- b. \$576,000
- c. \$600,000
- d. \$960,000

ANSWER:

Choice "c" is correct. The \$1,000,000 total cost (\$750,000 cash + \$250,000 mortgage) should be allocated to the building and the land separately. There is no other information with which to perform this allocation other than the property tax assessment. So, 60% of the \$1,000,000, or \$600,000, is allocated to the building.

Choice "a" is incorrect. This answer is the \$750,000 cash price less the \$250,000 mortgage.

Choice "b" is incorrect. This answer is computed as 60% of the assessed value of \$960,000. The cost that should be allocated is the total purchase price of the land and building, **not** the assessed value.

Choice "d" is incorrect. This answer is the assessed value. Even if the assessed value were to be allocated, the full assessed value is not allocated to the building. The land has to be worth something.

2006 AICPA Newly-Released Financial Questions

A flash flood swept through Hat, Inc.'s warehouse on May 1. After the flood, Hat's accounting records showed the following:

Inventory, January 1	\$ 35,000
Purchases, January 1 through May 1	200,000
Sales, January 1 through May 1	250,000
Inventory not damaged by flood	30,000
Gross profit percentage on sales	40%

What amount of inventory was lost in the flood?

- a. \$55,000
- b. \$85,000
- c. \$120,000
- d. \$150,000

ANSWER:

Choice "a" is correct. The amount of inventory lost in the flood is calculated as follows:

Inventory = Beg inventory + Purchases – Sales reduced to a cost basis

Inventory = \$35,000 + \$200,000 – (\$250,000 × (1-.40)) = \$235,000 - \$150,000 = \$85,000

Inventory lost in the flood = \$85,000 - \$30,000 = \$55,000

Choice "b" is incorrect. This answer is the total inventory, **not** the amount of inventory lost in the flood.

Choice "c" is incorrect. This answer is the sales reduced to a cost basis minus the inventory not lost in the flood, not the amount of inventory lost in the flood.

Choice "d" is incorrect. This answer is the sales reduced to a cost basis, **not** the amount of inventory lost in the flood.

2006 AICPA Newly-Released Financial Questions

Which of the following financial instruments is **not** considered a derivative financial instrument?

- a. Interest-rate swaps.
- b. Currency futures.
- c. Stock-index options.
- d. Bank certificates of deposit.

ANSWER:

Choice "d" is correct. A bank certificate of deposit is **not** a derivative financial instrument. Derivatives include futures, forwards, options, and swaps.

Choice "a" is incorrect. Interest rate swaps (or currency swaps) are derivative financial instruments.

Choice "b" is incorrect. Currency futures (or any other futures or forwards) are derivative financial instruments.

Choice "c" is incorrect. Stock-index options (or any other options) are derivative financial instruments.

2006 AICPA Newly-Released Financial Questions

Dex Co. has entered into a joint venture with an affiliate to secure access to additional inventory. Under the joint venture agreement, Dex will purchase the output of the venture at prices negotiated on an arms-length basis. Which of the following is(are) required to be disclosed about the related party transaction?

- I. The amount due to the affiliate at the balance sheet date.
 - II. The dollar amount of the purchases during the year.
- a. I only.
 - b. II only.
 - c. Both I and II.
 - d. Neither I nor II.

ANSWER:

Choice "c" is correct. For a related party transaction, **both** the amount due to the affiliate and the dollar amount of the purchases during the year must be disclosed. In disclosure questions, if you are not sure, disclose the most rather than the least.

Choice "a" is incorrect. For a related party transaction, **both** the amount due to the affiliate and the dollar amount of the purchases during the year must be disclosed.

Choice "b" is incorrect. For the related party transaction, **both** the amount due to the affiliate and the dollar amount of the purchases during the year must be disclosed.

Choice "d" is incorrect. For the related party transaction, **both** the amount due to the affiliate and the dollar amount of the purchases during the year must be disclosed.

2006 AICPA Newly-Released Financial Questions

Arpco, Inc., a for-profit provider of healthcare services, recently purchased two smaller companies and is researching accounting issues arising from the two business combinations. Which of the following accounting pronouncements are the most authoritative?

- a. AICPA Statements of Position.
- b. AICPA Industry and Audit Guides.
- c. FASB Statements of Financial Accounting Concepts.
- d. FASB Statements of Financial Accounting Standards.

ANSWER:

Choice "d" is correct. Since Arpco is a for-profit provider of healthcare services, it is covered under normal GAAP. Thus, the most authoritative pronouncements are the FASB Statements of Financial Accounting Standards (SFAS).

Choice "a" is incorrect. AICPA Statements of Position are not the most authoritative pronouncement for almost anything (other than for some issues that only they cover). They are normally "merely" the opinion of the AICPA.

Choice "b" is incorrect. AICPA Industry and Audit Guides are not the most authoritative pronouncement for almost anything (other than for some issues that only they cover).

Choice "c" is incorrect. FASB Statements of Financial Accounting Concepts are not authoritative pronouncements except where they have been incorporated by reference into an SFAS. They are the basis on which SFAS can be constructed.

2006 AICPA Newly-Released Financial Questions

Which of the following should be disclosed for each reportable operating segment of an enterprise?

	<u>Profit or loss</u>	<u>Total assets</u>
a.	Yes	Yes
b.	Yes	No
c.	No	Yes
d.	No	No

ANSWER:

Choice "a" is correct. For each reportable segment of an enterprise, **both** profit or loss and total assets should be disclosed. In disclosure questions, if you are not sure, disclose the most rather than the least.

Choice "b" is incorrect. For each reportable segment of an enterprise, **both** profit or loss and total assets should be disclosed.

Choice "c" is incorrect. For each reportable segment of an enterprise, **both** profit or loss and total assets should be disclosed.

Choice "d" is incorrect. For each reportable segment of an enterprise, **both** profit or loss and total assets should be disclosed.

2006 AICPA Newly-Released Financial Questions

According to the FASB conceptual framework, the quality of information that helps users increase the likelihood of correctly forecasting the outcome of past or present events is called:

- a. Feedback value.
- b. Predictive value.
- c. Representational faithfulness.
- d. Reliability.

ANSWER:

Choice "b" is correct. The quality of information that helps users increase the likelihood of correctly forecasting the outcome of past or present events is called predictive value. Forecasting is predicting.

Choice "a" is incorrect. The quality of information that helps users increase the likelihood of correctly forecasting the outcome of past or present events is called predictive value, **not** feedback value. Feedback value enables decision makers to confirm prior expectations or to adjust or correct the decisions made previously.

Choice "c" is incorrect. The quality of information that helps users increase the likelihood of correctly forecasting the outcome of past or present events is called predictive value, **not** representational faithfulness. Representational faithfulness is the agreement between financial reporting and the resources or events represented.

Choice "d" is incorrect. The quality of information that helps users increase the likelihood of correctly forecasting the outcome of past or present events is called predictive value, **not** reliability. Reliability is the combination of neutrality, representational faithfulness, and verifiability.

2006 AICPA Newly-Released Financial Questions

During the year, Private College received the following:

An unrestricted \$50,000 pledge to be paid the following year.

A \$25,000 cash gift restricted for scholarships.

A notice from a recent graduate that the college is named as a beneficiary of \$10,000 in that graduate's will.

What amount of contribution revenue should Private College report in its statement of activities?

- a. \$25,000
- b. \$35,000
- c. \$75,000
- d. \$85,000

ANSWER:

Choice "c" is correct. Total contribution revenue is \$75,000. The \$50,000 unrestricted pledge is reported as contribution revenue on the statement of activities, even though it is to be paid (and collected) in the following year. The \$25,000 cash gift is reported as contribution revenue on the statement of activities, even though it is restricted (it is recorded as restricted revenue). The "notice" from a recent graduate that the college is named as a beneficiary is not definite enough for the recording of revenue (the recent graduate may live a long time and may change his or her will at any time). Total contribution revenue is thus \$75,000.

Choice "a" is incorrect. The \$50,000 unrestricted pledge is reported as contribution revenue on the statement of activities, not just the \$25,000 cash gift.

Choice "b" is incorrect. The \$25,000 restricted gift is an element of recognized contribution revenue on the statement of activities, but the \$10,000 "notice" is not.

Choice "d" is incorrect. The \$10,000 "notice" is not reported as contribution revenue on the statement of activities, although the other two amounts related to actual receipts or receivables are recognized.

When debt is issued at a discount, interest expense over the term of debt equals the cash interest paid:

- a. Minus discount.
- b. Minus discount minus par value.
- c. Plus discount.
- d. Plus discount plus par value.

ANSWER:

Choice "c" is correct. When debt is issued at a discount, interest expense over the term of the debt equals the cash interest paid plus amortization of the discount. The Journal Entry for the amortization of the discount is as follows:

Dr Interest expense
Cr Amortization of bond discount
Cr Cash (or interest payable)

An easy way to remember whether to add or to subtract is that the discount is a reduction (Dr) of the bond's face value or par amount (Cr). Since the discount is a Debit, the way to reduce (amortize) it is to Credit it.

Choice "a" is incorrect. When debt is issued at a discount, interest expense over the term of the debt equals the cash interest paid plus, **not** minus, amortization of the discount.

Choice "b" is incorrect. When debt is issued at a discount, interest expense over the term of the debt equals the cash interest paid plus amortization of the discount. The par value should definitely not be subtracted.

Choice "d" is incorrect. When debt is issued at a discount, interest expense over the term of the debt equals the cash interest paid plus amortization of the discount. The par value should definitely not be added.

2006 AICPA Newly-Released Financial Questions

On December 30, Devlin Co. sold goods to Jensen Co. for \$10,000, under an arrangement in which (1) Jensen has an unlimited right of return and (2) Jensen's obligation to pay Devlin is contingent upon Jensen's reselling the goods. Past experience has shown that Jensen ordinarily resells 60% of goods and returns the other 40%. What amount should Devlin include in sales revenue for this transaction on its December 31 income statement?

- a. \$10,000
- b. \$6,000
- c. \$4,000
- d. \$0

ANSWER:

Choice "d" is correct. When there is an unlimited right of return, nothing should be recorded as sales revenue unless four conditions are satisfied. These conditions are the following:

- The sales price is substantially fixed (it seems like it is in this question).
- The buyer assumes all risk of loss (no information).
- The buyer has paid some form of consideration (no information).
- The amount of returns can be reasonably estimated (which they can in this question).

Since all four conditions have not been satisfied, revenue should not be recognized until they are or until something is actually sold.

Choice "a" is incorrect. No revenue should be recognized because all four conditions have not been satisfied.

Choice "b" is incorrect. No revenue should be recognized because all four conditions have not been satisfied.

Choice "c" is incorrect. No revenue should be recognized because all four conditions have not been satisfied.

Which of the following is a required financial statement for an investment trust fund?

- a. Statement of revenues, expenditures, and changes in fiduciary net assets.
- b. Statement of activities.
- c. Statement of revenues, expenses, and changes in fiduciary net assets.
- d. Statement of changes in fiduciary net assets.

ANSWER:

Choice "d" is correct. For an investment trust fund, the required financial statements are a statement of fiduciary net assets (balance sheet) and a statement of changes in fiduciary net assets (income statement). Of the choices available, the statement of changes in fiduciary net assets is required.

Choice "a" is incorrect. There is no statement of revenues, expenditures, and changes in fiduciary net assets for an investment trust fund. Investment trust funds use the accrual method and not the modified accrual method; thus, there are no expenditures.

Choice "b" is incorrect. There is no statement of activities for an investment trust fund. The closest is the statement of changes in fiduciary net assets.

Choice "c" is incorrect. There is no statement of revenues, expenses, and changes in fiduciary net assets. The closest is the statement of changes in fiduciary net assets.

Payne Co. prepares its statement of cash flows using the indirect method. Payne's unamortized bond discount account decreased by \$25,000 during the year. How should Payne report the change in unamortized bond discount in its statement of cash flows?

- a. As a financing cash inflow.
- b. As a financing cash outflow.
- c. As an addition to net income in the operating activities section.
- d. As a subtraction from net income in the operating activities section.

ANSWER:

Choice "c" is correct. Amortization of bond discount is an income-related item; thus, it is almost automatically an operating activity, not a financing activity. That knocks out two of the answers. Because the amortization of the discount was originally subtracted to get to net income in the first place, it is added back to net income for an indirect method statement of cash flows.

Choice "a" is incorrect. Amortization of bond discount is not a financing activity at all and certainly not a financing cash inflow.

Choice "b" is incorrect. Amortization of bond discount is not a financing activity at all and certainly not a financing cash outflow.

Choice "d" is incorrect. Because the amortization of the discount was originally subtracted to get to net income in the first place, it is added back to, **not** subtracted from, net income for an indirect method statement of cash flows.

2006 AICPA Newly-Released Financial Questions

A voluntary health and welfare organization received a \$700,000 permanent endowment during the year. The donor stipulated that the income and investment appreciation be used to maintain its senior center. The endowment fund reported a net investment appreciation of \$80,000 and investment income of \$50,000. The organization spent \$60,000 to maintain its senior center during the year. What amount of change in temporarily restricted net assets should the organization report?

- a. \$50,000
- b. \$70,000
- c. \$130,000
- d. \$770,000

ANSWER:

Choice "b" is correct. In this question, the donor stipulated that the income (\$50,000) and the investment appreciation (\$80,000) be used in maintain the senior center. Both the income and the investment appreciation represent increases in temporarily restricted net assets (total of \$130,000). The actual \$60,000 spent represents a decrease in temporarily restricted net assets. Thus, the total change is a \$70,000 increase.

Choice "a" is incorrect. The change in temporarily restricted net assets is **not** only the investment income.

Choice "c" is incorrect. The change in temporarily restricted net assets is **not** just the income and investment appreciation. The \$60,000 must be taken into account also.

Choice "d" is incorrect. The \$700,000 endowment is a permanently restricted net asset, **not** a temporarily restricted net asset.

2006 AICPA Newly-Released Financial Questions

Koby Co. entered into a capital lease with a vendor for equipment on January 2 for seven years. The equipment has no guaranteed residual value. The lease required Koby to pay \$500,000 annually on January 2, beginning with the current year. The present value of an annuity due for seven years was 5.35 at the inception of the lease. What amount should Koby capitalize as leased equipment?

- a. \$500,000
- b. \$825,000
- c. \$2,675,000
- d. \$3,500,000

ANSWER:

Choice "c" is correct. The amount to be capitalized for a capital lease is the present value of the minimum lease payments. In this question, the minimum lease payments are \$500,000 and the present value factor is 5.35. The present value of the minimum lease payments is thus $\$500,000 \times 5.35$, or \$2,675,000.

Choice "a" is incorrect. The amount to capitalize for a capital lease is certainly not the \$500,000 amount of the payment.

Choice "b" is incorrect. This is the difference between the total payments of \$3,500,000 and the present value of those payments of \$2,675,000.

Choice "d" is incorrect. The amount to capitalize for a capital lease is not the total value of the minimum lease payments ($\$500,000 \times 7 = \$3,500,000$). It is the present value of the minimum lease payments and must include the present value factor in the computation.

2006 AICPA Newly-Released Financial Questions

Godart Co. issued \$4,500,000 notes payable as a scrip dividend that matured in five years. At maturity, each shareholder of Godart's three million shares will receive payment of the note principal plus interest. The annual interest rate was 10%. What amount should be paid to the stockholders at the end of the fifth year?

- a. \$450,000
- b. \$2,250,000
- c. \$4,500,000
- d. \$6,750,000

ANSWER:

Note: For purposes of this question, to clarify the question, we are assuming that what the examiners mean is that each shareholder will receive his/her "portion" of the note receivable plus interest; however, the interpretation does not really make any difference because the question is what amount should be paid to the stockholders (in total). Further, there is nothing about a note that automatically says the interest on the note has to be simple interest. Many notes are short-term (less than a year), and the issue thus never arises.

Choice "d" is correct. The annual interest rate on the notes is 10% assumed to be non-compounding (the question does not say that, or indicate it in any way, but it is the only way to get the answer that the examiners have provided). Simple interest each year is \$450,000 ($\$4,500,000 \times .10$), and 5 years of this interest is \$2,250,000. The note principal plus interest is thus \$4,500,000 plus \$2,250,000, or \$6,750,000.

Choice "a" is incorrect. \$450,000 is only one year's worth of interest, and the time period in this question is five years. This answer also ignores the principal. The stockholders would really be unhappy.

Choice "b" is incorrect. This answer ignores the interest and includes just the principal in the payment to the stockholders. The question says that the shareholders will receive principal PLUS interest.

Choice "c" is incorrect. This answer ignores the principal and just includes the interest in the payment to the stockholders. The question says that the shareholders will receive principal PLUS interest.

2006 AICPA Newly-Released Financial Questions

Standard Co. spent \$10,000,000 on its new software package that is to be used only for internal use. The amount spent is for costs after the application development stage. The economic life of the product is expected to be three years. The equipment on which the package is to be used is being depreciated over five years. What amount of expense should Standard report on its income statement for the first full year?

- a. \$0
- b. \$2,000,000
- c. \$3,333,333
- d. \$10,000,000

ANSWER:

Choice "c" is correct. For software developed internally, costs incurred in the preliminary project state (application development stage) are expensed. In this question, the costs AFTER the preliminary project stage are capitalized and depreciated over the economic life of the product (3 years). Depreciation expense is thus \$3,333,333. The 5-year life of the equipment on which the package will be used is a distracter.

Choice "a" is incorrect. In this question, the \$10,000,000 of cost is after the application development stage. This cost will be capitalized and depreciated. Thus, depreciation expense is other than \$0.

Choice "b" is incorrect. In this question, the software is depreciated over 3 years, not 5 years. The 5-year life of the equipment on which the package will be used is a distracter.

Choice "d" is incorrect. The full \$10,000,000 cost would not be expensed in the first year unless the costs were incurred during the preliminary project stage. In this question, the cost was incurred AFTER the preliminary project stage.

Which of the following conditions must exist in order for an impairment loss to be recognized?

- I. The carrying amount of the long-lived asset is less than its fair value.
 - II. The carrying amount of the long-lived asset is not recoverable.
- a. I only.
 - b. II only.
 - c. Both I and II.
 - d. Neither I nor II.

ANSWER:

Choice "b" is correct. A long-lived asset is impaired if the carrying amount of the asset is less than its fair value and if that carrying amount is not recoverable (the fair value would be recoverable, but the difference would not be). That means that both of the conditions must exist. An impairment loss would then be recognized for the amount of the difference.

Choice "a" is incorrect. Both of the conditions must exist for an impairment loss to be recognized.

Choice "c" is incorrect. Both of the conditions must exist for an impairment loss to be recognized.

Choice "d" is incorrect. Both of the conditions must exist for an impairment loss to be recognized.

2006 AICPA Newly-Released Financial Questions

Which of the following should be disclosed in a company's financial statements related to deferred taxes?

- I. The types and amounts of existing temporary differences.
 - II. The types and amounts of existing permanent differences.
 - III. The nature and amount of each type of operating loss and tax credit carryforward.
- a. I and II only.
 - b. I and III only.
 - c. II and III only.
 - d. I, II, and III.

ANSWER:

Choice "b" is correct. The normal rule for disclosure is to disclose "everything," the more the better. However, every rule has an exception. In this question, one of the options is permanent differences. There are no deferred taxes for permanent differences. So the types and amounts of existing permanent differences do not have to be disclosed. The types and amounts of temporary differences and the nature and types of operating loss and tax credit carryforwards, however, should be disclosed.

Choice "a" is incorrect. The types and amounts of existing permanent differences are not required disclosures.

Choice "c" is incorrect. The types and amounts of existing permanent differences are not required disclosures.

Choice "d" is incorrect. The types and amounts of existing permanent differences are not required disclosures.

Note that II (permanent differences) is in all three wrong answers.

2006 AICPA Newly-Released Financial Questions

Nomar Co. shipped inventory on consignment to Seabright Co. that cost \$20,000. Seabright paid \$500 for advertising that was reimbursable from Nomar. At the end of the year, 70% of the inventory was sold for \$30,000. The agreement states that a commission of 20% will be provided to Seabright for all sales. What amount of net inventory on consignment remains on the balance sheet for the first year for Nomar?

- a. \$0
- b. \$6,000
- c. \$6,500
- d. \$20,000

ANSWER:

Choice "b" is correct. The cost of consigned inventory includes the cost of the inventory and any costs needed to get the inventory in place for sale. In this question, that is \$20,000. Because the \$500 is paid for advertising, and not for something like freight, it is not included in the cost of the inventory. At the end of the year, 30% of the inventory will remain unsold. 30% of the original inventory ($30\% \times \$20,000 = \$6,000$) remains on the balance sheet.

Choice "a" is incorrect. Consigned inventory remains on the balance sheet of the consignor (Nomar).

Choice "c" is incorrect. This answer includes the \$500 advertising in the cost of the inventory. The cost of advertising should not be included.

Choice "d" is incorrect. This answer includes the full original amount of the inventory. Some of it has been sold.

2006 AICPA Newly-Released Financial Questions

During the current year, a voluntary health and welfare organization receives \$300,000 in unrestricted pledges. Of this amount, \$100,000 has been designated by donors for use next year to support operations. If 15% of the unrestricted pledges are expected to be uncollectible, what amount of unrestricted support should the organization recognize in its current-year financial statements?

- a. \$300,000
- b. \$270,000
- c. \$200,000
- d. \$170,000

ANSWER:

Choice "d" is correct. The unrestricted support, net of expected uncollectibles, recognized in the current year financial statements is \$170,000. Although \$300,000 was pledged, 15% are anticipated to be uncollectible and \$100,000 is effectively temporarily restricted by the time restriction limiting the use of the funds to the following year. The \$200,000 (\$300,000 - \$100,000) of unrestricted current year pledges, reduced by \$30,000 (15% of \$200,000) is \$170,000 (\$200,000 - \$30,000).

Choice "a" is incorrect. This answer incorrectly includes the entire amount pledged and ignores the \$30,000 estimate of uncollectibility.

Choice "b" is incorrect. This answer incorrectly includes the entire amount pledged for current year recognition as unrestricted but does subtract the \$30,000 estimate of uncollectibility.

Choice "c" is incorrect. This answer includes only the unrestricted pledges but does subtract the estimate of uncollectibility.

2006 AICPA Newly-Released Financial Questions

Which of the following must be included in a company's summary of significant accounting policies in the notes to the financial statements?

- a. Description of current year equity transactions.
- b. Summary of long-term debt outstanding.
- c. Schedule of fixed assets.
- d. Revenue recognition policies.

ANSWER:

Choice "d" is correct. The summary of significant accounting policies should include "policies." The only policy in the choices listed is the revenue recognition policies.

Choice "a" is incorrect. A description of current year equity transactions is not a policy. It should be disclosed somewhere in the footnotes but not in the summary of significant accounting policies.

Choice "b" is incorrect. A summary of long-term debt outstanding is not a policy. It should be disclosed somewhere in the footnotes but not in the summary of significant accounting policies.

Choice "c" is incorrect. A schedule of fixed assets is not a policy. It should be disclosed somewhere in the footnotes but not in the summary of significant accounting policies.

2006 AICPA Newly-Released Financial Questions

Mellow Co. depreciated a \$12,000 asset over five years, using the straight-line method with no salvage value. At the beginning of the fifth year, it was determined that the asset will last another four years. What amount should Mellow report as depreciation expense for year 5?

- a. \$600
- b. \$900
- c. \$1,500
- d. \$2,400

ANSWER:

Choice "a" is correct. Over the first 4 years, the asset would be depreciated down to \$2,400. Once it was determined that the asset would last for another 4 years, \$600 would be depreciated each year of that 4-year period. This change is a change in accounting estimate (the estimate being the life of the asset). Changes in accounting estimate are accounted for in the current year and future years if the change affects both.

Choice "b" is incorrect. This answer is the difference between the depreciation expense IF depreciation expense had been retroactively restated ($\$24,000 / 8 = \$1,500$) and the correct depreciation expense. Retroactive restatement is not appropriate for changes in accounting estimate.

Choice "c" is incorrect. This answer is the depreciation expense IF depreciation had been retroactively restated ($\$24,000 / 8 = \$1,500$). Retroactive restatement is not appropriate for changes in accounting estimate.

Choice "d" is incorrect. This answer is the undepreciated amount at the beginning of the fifth year or the amount of the depreciation expense for each of the first 4 years. Either way, it certainly is not going to be the depreciation expense for that year because the remaining cost will be depreciated over the remaining period.

2006 AICPA Newly-Released Financial Questions

Cantor Co. purchased a coal mine for \$2,000,000. It cost \$500,000 to prepare the coal mine for extraction of the coal. It was estimated that 750,000 tons of coal would be extracted from the mine during its useful life. Cantor planned to sell the property for \$100,000 at the end of its useful life. During the current year, 15,000 tons of coal were extracted and sold. What would be Cantor's depletion amount per ton for the current year?

- a. \$2.50
- b. \$2.60
- c. \$3.20
- d. \$3.30

ANSWER:

Choice "c" is correct. In this question, the total cost of the mine is the purchase price (\$2,000,000) plus the preparation (\$500,000), net of the anticipated sales price at the end of its useful life (\$100,000). The total cost is thus \$2,400,000 ($\$2,000,000 + \$500,000 - \$100,000 = \$2,400,000$). That total cost is divided by the estimated 750,000 tons of coal, for a per unit depletion amount of \$3.20. Note that the depletion amount per unit would be the same for every year unless additional expenditures were incurred.

Note that the 15,000 tons produced and sold is irrelevant because the question is asking for the depletion per ton. Often, the questions indicate that a certain number of units is produced and that a different amount is sold and ask about the depreciation expense for the period. In those questions, it is the number of units sold that count.

Choice "a" is incorrect, per the above calculation.

Choice "b" is incorrect, per the above calculation.

Choice "d" is incorrect. This answer ignores the anticipated sales price at the end of its useful life. This amount is effectively a salvage value and should be subtracted in the numerator of the depletion formula.

Assuming no outstanding encumbrances at year end, closing entries for which of the following situations would increase the unreserved fund balance at year end?

- a. Actual revenues were **less** than estimated revenues.
- b. Estimated revenues exceed actual appropriations.
- c. Actual expenditures exceed appropriations.
- d. Appropriations exceed actual expenditures.

ANSWER:

RULE: Unreserved fund balance represents the amount of current resources carried forward into the following year that will be available for appropriations. Assuming there are no encumbrances, the relationships between estimated and actual amounts has a determinable relationship with final fund balance amounts. The Budgetary Comparison Schedule illustrated for Progressive Township in your text shows that the "Final" budgeted fund balance at the beginning of the year is equal to the "Actual" fund balance at the beginning of the year. The examiners question effectively asks when the relationships between budgeted and actual results create an actual fund balance greater than expected.

Choice "d" is correct. Appropriations (estimated expenditures) in excess of actual expenditures would increase the unreserved fund balance. Not all of the original budget (appropriations) was spent, and the excess was returned to fund balance.

Choice "a" is incorrect. Actual revenues less than estimated revenues would indicate that the unreserved fund balance would decrease. There was effectively a revenue shortfall, and it had to come out of fund balance.

Choice "b" is incorrect. The relationship between estimated revenues exceeding actual appropriations is a comparison of budgeted amounts that does not give sufficient information to draw any conclusion with regard to the impact on unreserved fund balance. The "actual" appropriations is a distracter.

Choice "c" is incorrect. Actual expenditures in excess of appropriations would decrease the unreserved fund balance. More money was spent than was anticipated.

2006 AICPA Newly-Released Financial Questions

Which of the following is correct concerning financial statement disclosure of accounting policies?

- a. Disclosures should be limited to principles and methods peculiar to the industry in which the company operates.
- b. Disclosure of accounting policies is an integral part of the financial statements.
- c. The format and location of accounting policy disclosures are fixed by generally accepted accounting principles.
- d. Disclosures should duplicate details disclosed elsewhere in the financial statements.

ANSWER:

Choice "b" is correct. Disclosure of accounting policies (and all other disclosure also) is an integral part of the financial statements.

Choice "a" is incorrect. For disclosure of accounting policies, disclosure should **not** be limited to principles and methods peculiar to the industry in which the company operates. All material accounting policies should be disclosed.

Choice "c" is incorrect. For disclosure of accounting policies, the format and location of accounting policies are **not** fixed by GAAP. Accounting policy disclosures are normally Note 1, but that is a (reasonable and very general) practice and not a "rule." It does make sense to disclose the "why" before the "what."

Choice "d" is incorrect. Disclosure of accounting policies should **not** duplicate details disclosed elsewhere in the financial statements.

An employer's obligation for postretirement health benefits that are expected to be fully provided to or for an employee must be fully accrued by the date the:

- a. Benefits are paid.
- b. Benefits are utilized.
- c. Employee retires.
- d. Employee is fully eligible for benefits.

ANSWER:

Choice "d" is correct. An employer's obligation for postretirement health benefits that are expected to be fully provided to or for an employee must be fully accrued by the date the employee is fully eligible for benefits.

Choice "a" is incorrect. An employer's obligation for postretirement health benefits that are expected to be fully provided to or for an employee must be fully accrued by the date the employee is fully eligible for benefits, **not** the date the benefits are paid.

Choice "b" is incorrect. An employer's obligation for postretirement health benefits that are expected to be fully provided to or for an employee must be fully accrued by the date the employee is fully eligible for benefits, **not** the date the benefits are utilized.

Choice "c" is incorrect. An employer's obligation for postretirement health benefits that are expected to be fully provided to or for an employee must be fully accrued by the date the employee is fully eligible for benefits, **not** the date the employee retires.

2006 AICPA Newly-Released Financial Questions

On September 30, World Co. borrowed \$1,000,000 on a 9% note payable. World paid the first of four quarterly payments of \$264,200 when due on December 30. In its income statement for the year, what amount should World report as interest expense?

- a. \$0
- b. \$14,200
- c. \$22,500
- d. \$30,000

ANSWER:

Choice "c" is correct. In this question, World borrowed the \$1,000,000 on September 30. That means 3 months of interest had accrued in the current year. The interest is $\$1,000,000 \times .09 \times 3/12 = \$22,500$. The payment of \$264,200 will reduce the principal for the next quarterly interest payment due on March 31.

Choice "a" is incorrect. There would certainly be some interest expense for the fourth quarter of the year. So, \$0 cannot be correct. \$0 can sometimes be a correct answer (when, for example, a condition or a rule does not even apply), but it is not correct for this question.

Choice "b" is incorrect. The \$14,200 is exactly 60% of the correct answer, but there do not seem to be any amounts in the question that can be combined to obtain that amount. It might be just made up. It is often difficult, especially in simple questions, for the examiners to create three good wrong answers. This gives you a better chance of answering the question correctly!

Choice "d" is incorrect. This answer is computed by $\$1,000,000 \times .09 \times 1/3 = \$30,000$. There are 3 months in the interest payment period, but that does not mean that the originally calculated interest expense is just divided by 3.

Which of the following factors determines whether an identified segment of an enterprise should be reported in the enterprise's financial statements under SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*?

- I. The segment's assets constitute more than 10% of the combined assets of all operating segments.
 - II. The segment's liabilities constitute more than 10% of the combined liabilities of all operating segments.
- a. I only.
 - b. II only.
 - c. Both I and II.
 - d. Neither I nor II.

ANSWER:

Choice "a" is correct. For segment reporting, if an identified segment's assets constitute more than 10% of the combined assets of all operating segments, the segment should be reported. The same rule does not apply for the segment's liabilities. The candidate does have to remember the 10% and also the 10% of "what."

Choice "b" is incorrect. For segment reporting, if an identified segment's assets constitute more than 10% of the combined assets of all operating segments, the segment should be reported. The same rule does not apply for the segment's liabilities.

Choice "c" is incorrect. For segment reporting, if an identified segment's assets constitute more than 10% of the combined assets of all operating segments, the segment should be reported. The same rule does not apply for the segment's liabilities, so the correct answer cannot be "Both."

Choice "d" is incorrect. For segment reporting, if an identified segment's assets constitute more than 10% of the combined assets of all operating segments, the segment should be reported. The correct answer cannot be "Neither."

Which of the following is a research and development cost?

- a. Development or improvement of techniques and processes.
- b. Offshore oil exploration that is the primary activity of a company.
- c. Research and development performed under contract for others.
- d. Market research related to a major product for the company.

ANSWER:

Choice "a" is correct. Development or improvement of techniques and processes is a research and development (R&D) cost.

Choice "b" is incorrect. Offshore oil "exploration" costs (assumed to be geological and geophysical expenses) that is the primary activity of a company is not an R&D cost. These costs would be expensed (as cost of services sold) by a company whose primary activity is the incurring of such geological and geophysical costs. If these "exploration" costs are not assumed to be geological and geophysical expenses, they would be the drilling of exploratory wells looking for commercial oil & gas deposits; in that event, they would be capitalized and then amortized. Either way, the costs are not an R&D cost.

Choice "c" is incorrect. Research and development performed under contract for others is not an R&D cost. The purchaser buying the research and development will be able to expense its expenditures as R&D costs.

Choice "d" is incorrect. Market research, even though the term contains the word research, is not an R&D cost.

2006 AICPA Newly-Released Financial Questions

Which of the following items is included in the financing activities section of the statement of cash flows?

- a. Cash effects of transactions involving making and collecting loans.
- b. Cash effects of acquiring and disposing of investments and property, plant, and equipment.
- c. Cash effects of transactions obtaining resources from owners and providing them with a return on their investment.
- d. Cash effects of transactions that enter into the determination of net income.

ANSWER:

Choice "c" is correct. Financing activities include the cash effects of transactions obtaining resources from owners and providing them with a return on their investment.

Choice "a" is incorrect. The cash effects of transactions involving making and collecting loans are included in investing activities, **not** financing activities.

Choice "b" is incorrect. The cash effects of acquiring and disposing of investments and property, plant, and equipment are included in investing activities, **not** financing activities.

Choice "d" is incorrect. The cash effects of transactions that enter into the determination of net income are included in operating activities, **not** financing activities.

North Co. entered into a franchise agreement with South Co. for an initial fee of \$50,000. North received \$10,000 at the agreement's signing. The remaining balance was to be paid at a rate of \$10,000 per year, beginning the following year. North's services per the agreement were not complete in the current year. Operating activities will commence next year. What amount should North report as franchise revenue in the current year?

- a. \$0
- b. \$10,000
- c. \$20,000
- d. \$50,000

ANSWER:

Choice "a" is correct. Franchise fee revenue of \$0 should be recognized in the current year because North's services per the franchise agreement were not complete in the current year. The \$10,000 is the first payment of the \$50,000 initial franchise fee that was to be paid in installments. From a franchisor's (North Co.) standpoint, initial franchise fees are not revenue until all material conditions of the sale have been "substantially performed." The services were stated in the question to not be complete.

Choice "b" is incorrect. Franchise fee revenue of \$0, **not** the \$10,000 that was received on the agreement's signing, should be recognized in the current year because North's services per the franchise agreement were not complete in the current year.

Choice "c" is incorrect. Franchise fee revenue of \$0, **not** the \$10,000 that was received on the agreement's signing and presumably the \$10,000 that was to be paid at the beginning of the next year, should be recognized in the current year because North's services per the franchise agreement were not complete in the current year.

Choice "d" is incorrect. Franchise fee revenue of \$0, **not** the full \$50,000 initial franchise fee, should be recognized in the current year because North's services per the franchise agreement were not complete in the current year.

2006 AICPA Newly-Released Financial Questions

Whether recognized or unrecognized in an entity's financial statements, disclosure of the fair values of the entity's financial instruments is required when:

	<u><i>It is practicable to estimate those values</i></u>	<u><i>Aggregated fair values are material to the entity</i></u>
a.	No	No
b.	No	Yes
c.	Yes	No
d.	Yes	Yes

ANSWER:

Choice "d" is correct. Disclosure of the fair values of an entity's financial instruments is required when it is practicable to estimate those values and when the aggregate fair values are material (materiality is always an issue in disclosure, so the only real criteria here is practicability).

Choice "a" is incorrect. Disclosure of the fair values of an entity's financial instruments is required when it is practicable to estimate those values and when the aggregate fair values are material.

Choice "b" is incorrect. Disclosure of the fair values of an entity's financial instruments is required when it is practicable to estimate those values and when the aggregate fair values are material.

Choice "c" is incorrect. Disclosure of the fair values of an entity's financial instruments is required when it is practicable to estimate those values and when the aggregate fair values are material.

2006 AICPA Newly-Released Financial Questions

Green Co. incurred leasehold improvement costs for its leased property. The estimated useful life of the improvements was 15 years. The remaining term of the nonrenewable lease was 20 years. These costs should be:

- a. Expensed as incurred.
- b. Capitalized and depreciated over 20 years.
- c. Capitalized and expensed in the year in which the lease expires.
- d. Capitalized and depreciated over 15 years.

ANSWER:

Choice "d" is correct. Leasehold improvements are capitalized and then amortized over the lesser of the life of the improvements or the remaining term of the lease (in this question, the amortization period is lesser of 15 or 20). The leasehold improvement costs should thus be expensed over a period of 15 years. This rule makes sense because the party making the leasehold improvements will benefit from the improvements for either the life of the improvements or the term of the lease if the term of the lease is shorter than the life of the improvements (in which case, somebody else will benefit from the improvements for the remaining life of the improvements).

Choice "a" is incorrect. Leasehold improvements are capitalized and amortized, **not** expensed as incurred.

Choice "b" is incorrect. Leasehold improvements are capitalized and then amortized over the lesser of the life of the improvements or the remaining term of the lease, which in this question is 15, **not** 20, years.

Choice "c" is incorrect. Leasehold improvements are capitalized and then amortized over the lesser of the life of the improvements or the remaining term of the lease, **not** expensed in the year in which the lease expires.

2006 AICPA Newly-Released Financial Questions

On January 1 of the current year, Lean Co. made an investment of \$10,000. The following is the present value of \$1.00 discounted at a 10% interest rate:

<u>Periods</u>	<u>Present value of \$1.00 Discounted at 10%</u>
1	.909
2	.826
3	.751

What amount of cash will Lean accumulate in two years?

- a. \$12,000
- b. \$12,107
- c. \$16,250
- d. \$27,002

ANSWER:

Choice "b" is correct. The problem with this question is that there is a discount rate but not an interest rate available. The normal present value formula can be expressed as:

Present value = Future amount x present value factor

\$10,000 = Future amount x .826 (the present value factor is the discount rate for 2 years)

Future amount = \$10,000 / .826 = \$12,107

Choice "a" is incorrect. If the interest rate, rather than the discount rate, was 10% and the interest was not compounded, the \$10,000 would accumulate to \$12,000 (\$1,000 of interest each year). However, that calculation does not coincide with the facts of the question (the discount rate is 10% and the interest is compounded).

Choice "c" is incorrect. If Lean had invested \$10,000 at a rate around 10%, it is not expected that the investment could accumulate to anything like \$16,250. \$10,000 invested at 10% would only amount to slightly more than \$12,000.

Choice "d" is incorrect, per the above calculation and explanation.

2006 AICPA Newly-Released Financial Questions

Yellow Co. spent \$12,000,000 during the current year developing its new software package. Of this amount, \$4,000,000 was spent before it was at the application development stage and the package was only to be used internally. The package was completed during the year and is expected to have a four-year useful life. Yellow has a policy of taking a full-year's amortization in the first year. After the development stage, \$50,000 was spent on training employees to use the program. What amount should Yellow report as an expense for the current year?

- a. \$1,600,000
- b. \$2,000,000
- c. \$6,012,500
- d. \$6,050,000

ANSWER:

Choice "d" is correct. The \$4,000,000 that was spent before the application development stage (during the preliminary project state) would certainly be expensed. The \$50,000 for training employees would certainly be expensed (costs for training and maintenance are expensed). The total so far is \$4,050,000. The package was completed during the year and a full year's worth of amortization is taken ($\$8,000,000 / 4 = \$2,000,000$). The total then is \$6,050,000.

Choice "a" is incorrect. This answer appears to be amortization of the \$4,000,000 that was spent before the application development stage and nothing else. That would mean that everything else was capitalized. If everything else were capitalized, what about amortization on those capitalized amounts? It is hard to imagine that they would just "stay out there" forever.

Choice "b" is incorrect. This answer appears to be amortization of the \$8,000,000 ($\$8,000,000 / 4 = \$2,000,000$). That would mean that everything else was capitalized. If everything else were capitalized, what about amortization on those capitalized amounts?

Choice "c" is incorrect. This answer includes amortization ($\$50,000 / 4 = \$12,500$) of the training expenditures. Training should be expensed when incurred. The rest of the answer (\$6,000,000) is the same as the correct answer.

2006 AICPA Newly-Released Financial Questions

Miller Co. discovered that in the prior year, it failed to report \$40,000 of depreciation related to a newly constructed building. The depreciation was computed correctly for tax purposes. The tax rate for the current year was 40%. What was the impact of the error on Miller's financial statements for the prior year?

- a. Understatement of accumulated depreciation of \$24,000.
- b. Understatement of accumulated depreciation of \$40,000.
- c. Understatement of depreciation expense of \$24,000.
- d. Understatement of net income of \$24,000.

ANSWER:

Choice "b" is correct. An understatement (failure to report) of depreciation (expense) would certainly understate accumulated depreciation by the same amount, gross of tax. [Note that three of the answers listed are net of tax and that only one of them is gross of tax. Since there can be only one correct answer, an initial thought would be that the "odd man out" answer, the net of tax answer, is probably correct.]

Choice "a" is incorrect. An understatement of depreciation (expense) would certainly understate accumulated depreciation by the same amount, gross, **not** net, of tax.

Choice "c" is incorrect. An understatement of depreciation (expense) would certainly understate depreciation expense gross, **not** net, of tax.

Choice "d" is incorrect. An understatement of depreciation (expense) would overstate, **not** understate, net income by the same amount, gross, **not** net, of tax.

2006 AICPA Newly-Released Financial Questions

At June 30, Almond Co.'s cash balance was \$10,012 before adjustments, while its ending bank statement balance was \$10,772. Check number 101 was issued June 2 in the amount of \$95, but was erroneously recorded in Almond's general ledger balance as \$59. The check was correctly listed in the bank statement at \$95. The bank statement also included a credit memo for interest earned in the amount of \$35, and a debit memo for monthly service charges in the amount of \$50. What was Almond's adjusted cash balance at June 30?

- a. \$9,598
- b. \$9,961
- c. \$10,048
- d. \$10,462

ANSWER:

Choice "b" is correct. Almond's adjusted cash balance is computed as follows:

Adjusted cash balance = Unadjusted cash balance +/- bank errors + credit memos – service charges

$$\text{Adjusted cash balance} = \$10,012 - (\$95 - \$59) + \$35 - \$50 = \$9,961$$

Choice "a" is incorrect, per the above calculation.

Choice "c" is incorrect, per the above calculation. The difference between this answer and the correct answer is \$87, and it was likely calculated as $\$10,012 + (\$95 - \$59)$.

Choice "d" is incorrect, per the above calculation.

2006 AICPA Newly-Released Financial Questions

Trans Co. uses a periodic inventory system. The following are inventory transactions for the month of January:

1/1	Beginning inventory	10,000 units at \$3
1/5	Purchase	5,000 units at \$4
1/15	Purchase	5,000 units at \$5
1/20	Sales at \$10 per unit	10,000 units

Trans uses the average pricing method to determine the value of its inventory. What amount should Trans report as cost of goods sold on its income statement for the month of January?

- a. \$30,000
- b. \$37,500
- c. \$40,000
- d. \$100,000

ANSWER:

Choice "b" is correct. Regardless of the type of inventory costing method, the first step would be to calculate the number of units in the ending inventory and/or cost of goods sold. In this question, there are 20,000 units available for sale and thus 10,000 units (20,000 total purchases – 10,000 ending inventory) in cost of goods sold. The (weighted) average purchase price of the units available for sale is $((10,000 \times \$3) + (5,000 \times \$4) + (5,000 \times \$5) / (10,000 + 5,000 + 5,000) = \3.75 . Thus the cost of goods sold is $10,000 \times \$3.75 = \$37,500$.

Choice "a" is incorrect. In a (weighted) average pricing inventory costing system, the cost of goods sold would not be at the price of the beginning inventory, or \$3 in this question, even though there were 10,000 units sold and 10,000 units in the beginning inventory.

Choice "c" is incorrect. In a (weighted) average pricing inventory costing system, the cost of goods sold would not be costed at the price of the first purchase, or \$4 in this question.

Choice "d" is incorrect. In a (weighted) average pricing inventory costing system, the cost of goods sold would not be costed at the selling price of the goods, or \$10 in this question.

Note that this question does not use good terminology. The question asks about the "value" of the inventory. It should ask about the "cost" of the inventory. The value of the inventory is whatever the inventory could be sold for in the market.

2006 AICPA Newly-Released Financial Questions

Porter Co. began its business last year and issued 10,000 shares of common stock at \$3 per share. The par value of the stock is \$1 per share. During January of the current year, Porter bought back 500 shares at \$6 per share, which were reported by Porter as treasury stock. The treasury stock shares were reissued later in the current year at \$10 per share. Porter used the cost method to account for its equity transactions. What amount should Porter report as paid-in capital related to its treasury stock transactions on its balance sheet for the current year?

- a. \$1,500
- b. \$2,000
- c. \$4,500
- d. \$20,000

ANSWER:

Choice "b" is correct. Using the cost method, the treasury stock transactions include the reissuance of the treasury shares at \$10 per share (\$4 per share to APIC x 500 shares), or \$2,000. The additional paid-in capital from the original issuance of the stock is not paid-in capital related to the treasury stock and is not included.

Choice "a" is incorrect. This answer apparently includes the 500 shares at \$3 per share, which is the amount of additional paid-in capital generated on the original issuance of the stock. Additional paid-in capital from the original issuance of the stock is not included.

Choice "c" is incorrect. This answer apparently includes the 500 shares at \$9 per share, which is the difference between the price at which the treasury shares were reissued (\$10 reissuance price - \$1 par value = \$9 x 500 = \$4,500).

Choice "d" is incorrect. This answer apparently includes the 10,000 shares originally issued at the additional paid-in capital amount that was generated in the original issuance (\$3 issuance price - \$1 per share = \$2 x 10,000 = \$20,000).

2006 AICPA Newly-Released Financial Questions

New England Co. had net cash provided by operating activities of \$351,000; net cash used by investing activities of \$420,000; and cash provided by financing activities of \$250,000. New England's cash balance was \$27,000 on January 1. During the year, there was a sale of land that resulted in a gain of \$25,000 and proceeds of \$40,000 were received from the sale. What was New England's cash balance at the end of the year?

- a. \$27,000
- b. \$40,000
- c. \$208,000
- d. \$248,000

ANSWER:

Choice "c" is correct. New England's cash balance at the end of the year includes the cash balance at the beginning of the year, the net cash provided by operating activities, the net cash used by investing activities, and the net cash provided by financing activities ($\$27,000 + \$351,000 - \$420,000 + \$250,000 = \$208,000$). The sale of the land was included in the cash from the investing activities and does not have to be considered separately. When working this type of question, be sure to distinguish between the net cash used and the net cash provided.

Choice "a" is incorrect. The cash balance at the end of the year certainly includes more than just the cash balance at the beginning of the year.

Choice "b" is incorrect. The cash balance at the end of the year certainly includes more than just the proceeds from the land.

Choice "d" is incorrect. The proceeds from the sale of the land are already included in the net cash from investing activities. It does not have to be considered separately and does not have to be added.

2006 AICPA Newly-Released Financial Questions

Which of the following assets of a nongovernmental not-for-profit charitable organization must be depreciated?

- a. A freezer costing \$150,000 for storing food for the soup kitchen.
- b. Building costs of \$500,000 for construction in progress for senior citizen housing.
- c. Land valued at \$1 million being used as the site of the new senior citizen home.
- d. A bulk purchase of \$20,000 of linens for its nursing home.

ANSWER:

Choice "a" is correct. A nongovernmental not-for-profit charitable organization is accounted for using the accrual method, so normal accrual accounting is used. A freezer would be considered a fixed asset and would be depreciated.

Choice "b" is incorrect. Construction in progress is not depreciated, regardless of the type of organization.

Choice "c" is incorrect. Land is not depreciated, regardless of the type of organization.

Choice "d" is incorrect. Linens for a nursing home would not be considered a fixed asset and thus would not be depreciated. Linens would be considered a consumable (supplies).

Which of the following would be reported as program revenues on a local government's government-wide statement of activities?

- a. Charges for services.
- b. Taxes levied for a specific function.
- c. Proceeds from the sale of a capital asset used for a specific function.
- d. Interest revenues.

ANSWER:

Choice "a" is correct. For a local government's government-wide statement of activities, charges for services are reported as program revenue. Program revenue is revenue directly associated with a program or function. Remember the categories of program revenue and recall that the government can "SOC" away these revenues:

- S** Charges (for services)
- O** Operating grants and contributions
- C** Capital grants and contributions

Choice "b" is incorrect. Taxes are not program revenue. Even though the taxes are levied for the specific function, taxes are not revenue. The words "levied for a specific function" were included to attempt to confuse.

Choice "c" is incorrect. Proceeds from the sale of a capital asset used for a specific function are not program revenue. Again, the words "used fro a specific function" were included to confuse.

Choice "d" is incorrect. Interest revenue is not program revenue.

2006 AICPA Newly-Released Financial Questions

A nongovernmental not-for-profit organization borrowed \$5,000, which it used to purchase a truck. In which section of the organization's statement of cash flows should the transaction be reported?

- a. In cash inflow and cash outflow from investing activities.
- b. In cash inflow and cash outflow from financing activities.
- c. In cash inflow from financing activities and cash outflow from investing activities.
- d. In cash inflow from operating activities and cash outflow from investing activities.

ANSWER:

Choice "c" is correct. For a nongovernmental not-for-profit organization, the borrowing would be a cash inflow from financing activities, and the purchase of the truck would be a cash outflow from investing activities. For a nongovernmental not-for-profit organization, the commercial format for the statement of cash flows is followed.

Choice "a" is incorrect. The cash inflow for the borrowing is a financing activity, **not** an investing activity.

Choice "b" is incorrect. The cash outflow for the purchase of the truck is an investing activity, **not** a financing activity.

Choice "d" is incorrect. The cash inflow for the borrowing is a financing activity, **not** an operating activity.

2006 AICPA Newly-Released Financial Questions

Janna Association, a nongovernmental not-for-profit organization, received a cash gift with the stipulation that the principal be held for at least 20 years. How should the cash gift be recorded?

- a. A temporarily restricted asset.
- b. A permanently restricted asset.
- c. An unrestricted asset.
- d. A temporary liability.

ANSWER:

Choice "a" is correct. For a nongovernmental non-for-profit organization, a cash gift (with a stipulation that the principal be held for at least 20 years) should be recorded as a temporarily (a 20-year spending restriction would be temporary because it can ultimately be satisfied) restricted asset.

Choice "b" is incorrect. The cash gift would be recorded as a temporarily, **not** permanently, restricted net asset.

Choice "c" is incorrect. The cash gift would be recorded as a temporarily restricted, **not** an unrestricted, asset.

Choice "d" is incorrect. The cash gift would be recorded as a temporarily restricted net asset, **not** a temporary liability. The term temporary liability is a distracter.

Which of the following assumptions means that money is the common denominator of economic activity and provides an appropriate basis for accounting measurement and analysis?

- a. Going concern.
- b. Periodicity.
- c. Monetary unit.
- d. Economic entity.

ANSWER:

Choice "c" is correct. The monetary unit assumption means that money is the common denominator for economic activity and provides an appropriate basis for accounting measurements and analysis.

Choice "a" is incorrect. The going concern assumption has nothing to do with money per se. The going concern assumption presumes that an entity will continue to operate in the foreseeable future.

Choice "b" is incorrect. The periodicity has nothing to do with money per se. The periodicity assumption is that economic activity can be divided into meaningful time periods.

Choice "d" is incorrect. The economic entity assumption has nothing to do with money per se. The economic entity assumption is that economic activity can be accounted for when considering an identifiable set of activities.

2006 AICPA Newly-Released Financial Questions

Which of the following statements best describes an operating procedure for issuing a new Financial Accounting Standards Board (FASB) statement?

- a. The emerging issues task force must approve a discussion memorandum before it is disseminated to the public.
- b. The exposure draft is modified per public opinion before issuing the discussion memorandum.
- c. A new statement is issued only after a majority vote by the members of the FASB.
- d. A new FASB statement can be rescinded by a majority vote of the AICPA membership.

ANSWER:

Choice "c" is correct. A new statement from the FASB is issued only after a majority vote of the members of the FASB.

Choice "a" is incorrect. There is no necessity for the EITF to approve a discussion memorandum (presumably the question means a discussion memorandum of the FASB statement itself and not an EITF statement) before it is disseminated to the public.

Choice "b" is incorrect. There is no necessity for an exposure draft to be modified per public opinion before issuing the discussion memorandum (a question can be raised here as to "what" discussion memorandum). Exposure drafts are quite/most often modified before they are issued as FASB statements, but they do not have to be. Whether they are or are not modified is a function of whether the FASB thinks they should be modified, partly due to the public comments that have been received.

Choice "d" is incorrect. There is no way to rescind a new FASB statement, although, in reality, a FASB statement can be rescinded by the issuance of a new statement on the same subject. However, even if there was a way to rescind a new FASB statement, it would not be by a majority vote of the AICPA membership, but by a majority vote of the members of the FASB.

2006 AICPA Newly-Released Financial Questions

What is the present value of all future retirement payments attributed by the pension benefit formula to employee services rendered prior to that date only?

- a. Service cost.
- b. Interest cost.
- c. Projected benefit obligation.
- d. Accumulated benefit obligation.

ANSWER:

Choice "d" is correct. The accumulated benefit obligation is the present value of future retirement payments attributed to the pension benefit formula to employee services rendered prior to a date, based on current and past compensation levels.

Choice "a" is incorrect. Service cost is the present value of all pension benefits earned by company employees in the current year.

Choice "b" is incorrect. Interest cost is the interest on the projected benefit obligation.

Choice "c" is incorrect. The projected benefit obligation is the present value of future retirement payments attributed to the pension benefit formula to employee services rendered prior to a date, based on current and past and (an assumption about) future compensation levels. The only difference between the accumulated benefit obligation and the projected benefit obligation is the assumption of future compensation levels. The projected benefit obligation is used for most pension calculations; the accumulated benefit obligation is used only to compute the minimum liability (fair value of plan assets less the accumulated benefit obligation).

Which of the following is a criterion for a lease to be classified as a capital lease in the books of a lessee?

- a. The lease contains a bargain purchase option.
- b. The lease does **not** transfer ownership of the property to the lessee.
- c. The lease term is equal to 65% or more of the estimated useful life of the leased property.
- d. The present value of the minimum lease payments is 70% or more of the fair market value of the leased property.

ANSWER:

Choice "a" is correct. One of the four criteria (OWNS) for a lease to be classified as a capital lease on the books of a lessee is the existence of a bargain purchase option.

Choice "b" is incorrect. One of the four criteria (OWNS) for a lease to be classified as a capital lease on the books of a lessee is that the lease does transfer ownership of the leased property to the lessee at the end of the lease.

Choice "c" is incorrect. One of the four criteria (OWNS) for a lease to be classified as a capital lease on the books of a lessee is that the lease term is equal to 75%, **not** 65%, or more of the estimated useful life of the leased property.

Choice "d" is incorrect. One of the four criteria (OWNS) for a lease to be classified as a capital lease on the books of a lessee is that the present value of the minimum lease payments is 90%, **not** 70%, or more of the fair value of the leased property.