

Beechy, Conrod & Farrell *Intermediate Accounting* Fifth Edition, Volume 1 – Test Bank

Chapter 1 – The Framework for Financial Reporting

1. The main purpose of financial accounting is to communicate useful financial information to decision-makers both inside and outside of the business organization.

Ans: True

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 5

2. Managers of an entity are considered to be internal decision- makers.

Ans: True

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 5

3. External users of a company's financial statements may have conflicting objectives.

Ans: True

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 5

4. Both private and publicly accountable companies must comply with IFRS beginning on January 1, 2011.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

5. Privately held, publicly accountable companies with a fiduciary responsibility must comply with IFRS.

Ans: True

Difficulty: Hard

Level of Learning: Knowledge

Topic: LO 7

6. Mutual fund companies, which may be privately held, are deemed to have a fiduciary responsibility and must therefore comply with IFRS.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

7. Canadian companies must always present their financial results in Canadian dollars.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 2

8. Canadian corporations are prohibited from using U.S. GAAP.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

9. A company's functional currency is the currency in which it conducts most of its business.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

10. A company's presentation currency should normally be its functional currency.

Ans: True
Difficulty: Hard
Level of Learning: Knowledge
Topic: LO 7

11. The disclosed basis of accounting (DBA) refers to the use of Non-GAAP accounting policies by private companies.

Ans: True
Difficulty: Medium

Level of Learning: Knowledge
Topic: LO 7

12. A wholly-owned subsidiary of a multinational corporation is essentially a private corporation.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 7

13. The accounting standards for private enterprises (ASPE) are essentially a scaled-down version of the CICA handbook, which is available to all small and medium sized enterprises with no fiduciary responsibility.

Ans: True
Difficulty: Hard
Level of Learning: Knowledge
Topic: LO 7

14. Accounting concepts, principles and standards are just as broad and general today as they were sixty years ago.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

15. The influence of tax rules when selecting appropriate accounting treatment for a transaction is particularly strong with public companies.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

16. Due to the excellent work of the ACSB, there are very few choices among alternative accounting policies today.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 3

17. At least half of the members of the AICPA must be other than professional accountants.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

18. Disclosure notes facilitate the evaluation of enterprise position and performance because they include information, which helps to explain qualitative aspects of earnings.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

19. A company whose net income is highly correlated to its operating cash flows is said to have a high quality of earnings.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

20. Maximization of net income is a common motivation of managers.

Ans: True

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 6

21. Developments in accounting standards have not addressed the problem of using accounting techniques to smooth earnings.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

22. The Federal Accounting Standards Board (FASB) is a branch of the CICA.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

23. The CICA Handbook is the most important primary source of GAAP.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 2

25. The various provincial securities commissions do not exert influence on the development of accounting standards.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 2

26. FASB and International Accounting Standards are secondary sources of GAAP.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 7

27. The CICA Handbook requires that income for tax purposes be equal to a company's accounting income at all times.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 2

28. The Accounting Standards Board (ACSB) is an independent group established to promulgate accounting standards for governmental units such as provincial and civic entities.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

29. The Canadian Institute of Chartered Accountants (CICA) initially created the Accounting and Auditing Research Committee, which was replaced by the Accounting Research Committee (ARC), which in turn was replaced by the Accounting Standards Board (AcSB).

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

30. The International Accounting Standards Board is responsible for the creation of International Financial Reporting Standards used by companies whose securities are traded on international markets.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

31. If cash flow prediction is a company's primary reporting objective, this would likely result in:
- A) Higher earnings
 - B) Lower earnings
 - C) Poor matching
 - D) Fewer accruals and deferrals

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

32. The organization created to develop accounting standards in Canada, the AICSB, is concerned about:
- A) reported cash flows.
 - B) reported earnings.
 - C) reported comparability of results.
 - D) reporting abuse.
 - E) all of these answers are correct.

Ans: E

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

33. Which of the following is published by the Financial Accounting Standards Board?
- A) Accounting Project Proposals
 - B) Accounting Exposure Drafts
 - C) Accounting Issues Papers
 - D) CICA Handbook Sections and Accounting Guidelines
 - E) Statements of Auditing Revisions

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

34. Generally accepted accounting principles currently are promulgated primarily by the:
- A) Canadian Academic Accounting Association (CAAA)
 - B) Canada Customs and Revenue Agency
 - C) Ontario Securities Commission (OSC)
 - D) Accounting Standards Board (AcSB)

Ans: D

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 7

35. Pronouncements of the Accounting Standards Board:

- A) are commonly known as "Accounting Research Studies."
- B) are enforced by the American Accounting Association.
- C) are similar in force and effect to those of the Accounting and Auditing Research Committee.
- D) are commonly known as "Opinions."
- E) must be followed for income tax purposes.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

36. The conceptual framework of accounting should have many positive effects as new accounting standards are developed. Which of the following is not one of those effects?

- A) Financial statements among companies and industries should be more consistent and comparable.
- B) Standard setting should be more consistent with an overall statement of the objectives and concepts of financial reporting.
- C) Users' understanding and confidence in financial statements should increase.
- D) Management should have greater latitude in choosing among accounting alternatives.
- E) Accountants should be better able to assess the validity of different accounting alternatives for similar and dissimilar transactions and events.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

37. External decision-makers include all of the following except:

- A) managers.
- B) owners.
- C) creditors.
- D) financial press.

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

38. The users toward which financial statements are directed:
- A) are very sophisticated and experienced in using financial information.
 - B) are independent Public Accountants.
 - C) have degrees in accounting and finance.
 - D) have a reasonable understanding of business and economic activities.
 - E) are Chartered Financial Analysts.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

39. General-purpose financial statements report financial information relevant to:
- A) investors only.
 - B) creditors only.
 - C) government users only.
 - D) investors, creditors and government users.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

40. Users of financial statements can generally be broken down into which of the following two categories:
- A) Internal and external users.
 - B) Government and investors.
 - C) Creditors and Investors.
 - D) External users and preparers.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

41. What is the purpose of financial statements?

- A) to disclose the market value of the firm's assets and liabilities.
- B) to determine compliance with tax laws.
- C) to identify shareholders.
- D) to help users make decisions.

Ans: D

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 2

42. Choose the correct statement about audits of corporations:

- A) Outside auditors are paid by the government for auditing the financial statements of corporations.
- B) Revenue Canada performs audits of corporations' financial statements.
- C) Public corporations (those whose stock are traded on exchanges) are subject to annual audit as to their compliance with GAAP.
- D) It is the employees of the firm being audited who perform the annual audit of the financial statements of that firm.

Ans: C

Difficulty: Hard

Level of Learning: Knowledge

Topic: LO 7

43. Which of the following areas within the accounting field has as its main purpose serving the information needs of parties outside the reporting firm?

- A) Financial accounting.
- B) Tax accounting.
- C) Managerial accounting.
- D) Auditing.

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

44. The stewardship function refers to
- A) Disclosing management's use of funds and other financial information to absentee shareholders
 - B) A company's corporate citizenship track record
 - C) The collection of information for planning the future of the entity, implementing those plans, and for controlling daily operations.
 - D) The collection of information to help present and potential investors and creditors and other users in assessing the amounts, timing and uncertainty of prospective cash receipts.

Ans: A

Difficulty: Hard

Level of Learning: Knowledge

Topic: LO 5

45. The primary responsibility of an independent auditor who is a professional accountant is to:
- A) verify the accuracy of the amounts determined by the client.
 - B) assess whether the management is honest.
 - C) evaluate the "fair presentation" of the company's financial reports.
 - D) prepare current financial reports for the client.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

46. Professional accountants need a wide range of knowledge and skills. Which of the following is not an example of such knowledge or skills?
- A) an ability to calculate and analyze data, and a facility with numbers.
 - B) knowledge of many disciplines such as finance, economics, management, marketing and statistics.
 - C) an ability to communicate in a concise and understandable manner.
 - D) skills derived from prior management experience.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

47. Which of the following statements regarding cash flows is not accurate?
- A) Before the present cash flow statement standard became effective, companies had a choice of whether to report cash flow from operating activities or working capital from operating activities.
 - B) Studies have shown that a cash flows report is more relevant to investor decisions than a working capital report.
 - C) The reported cash flow from operating activities has been found useful in evaluating a firm's ability to make interest payments and repay debt.
 - D) Information about past cash flows is useful in predicting an entity's future cash flows.
 - E) Information about the balances of current liabilities, long-term debt and stockholders' equity can be found in the statement of cash flows.

Ans: E

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

48. The stewardship function is reflected by:
- A) Minimizing interperiod allocations
 - B) Performance evaluation
 - C) Full disclosure
 - D) Both (A) and (B) are correct.
 - E) Both (A) and (C) are correct.

Ans: E

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

49. Which of the following is NOT a primary motivator for maximizing net income?
- A) Compliance with debt covenants.
 - B) To positively influence users' assessment of management performance.
 - C) To enhance managers' performance-based compensation.
 - D) To minimize the company's income tax liability.

Ans: D

Difficulty: Hard

Level of Learning: Knowledge

Topic: LO 5

50. Generally accepted accounting principles are:

- A) optional procedures for recording economic events
- B) mandatory rules applied to both financial and management accounting
- C) the rules of accounting, prescribed exclusively by Federal regulatory agencies
- D) standards of accounting, a material departure from which may result in a qualified opinion issued by an auditor

Ans: D

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 2

51. Generally accepted accounting principles

- A) include specific rules, practices and procedures.
- B) include broad principles and conventions of general applications including underlying concepts
- C) standards of accounting, a material departure from which may result in a qualified opinion issued by an auditor.
- D) all of these answers are correct.

Ans: D

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 2

52. Which of the following are major factors in the rapidly changing financial reporting environment in Canada?

- A) increased demand for accountants and the impact of technology.
- B) globalization and the use of computer networks.
- C) the growing number of institutional investors and the knowledge based economy.
- D) none of these answers is correct.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

53. An organization that has *not* published financial accounting standards is the
- A) the Institute of Chartered Accountants.
 - B) the Certified Management Accountants of Canada.
 - C) the International Accounting Standards Committee.
 - D) the Emerging Issues Committee

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

54. The role of the Accounting Standards Board (ACSB) in the formulation of accounting principles in Canada can be best described as
- A) primary
 - B) secondary
 - C) sometimes primary and sometimes secondary
 - D) non-existent

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

55. The body that has the responsibility to set generally accepted accounting principles in Canada is the
- A) FASB
 - B) IASC
 - C) AcSB
 - D) OSC

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

56. Which of the following financial statements are required for companies adhering to IFRS but NOT ASPE (private entity GAAP)?

- A) Statement of Comprehensive income.
- B) Statement of Changes in Equity.
- C) Statement of Cash Flows.
- D) Statement of Retained Earnings.
- E) Both A & B are correct.

Ans: E

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

57. The essential characteristic(s) of accounting is (are)

- A) communication of financial information to interested persons.
- B) communication of financial information about economic entities.
- C) identification, measurement, and communication of financial information.
- D) all of these.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 1

58. During the coming years, we should expect the AICSB to

- A) extend differential reporting options available to private companies.
- B) harmonize Canadian GAAP to international standards.
- C) continue to provide accounting standards for private companies.
- D) all of these.

Ans: D

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 2

59. Which of the following is NOT a primary source of GAAP?

- A) Accounting sections of the CICA Handbook.
- B) FASB accounting standards.
- C) Accounting Guidelines issued by the AICSB.
- D) Abstracts of Issues discussed by the EIC (Emerging Issues Committee).

Ans: B

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 2

60. Secondary sources of GAAP should be evaluated on

- A) acceptance of the source by industry professionals.
- B) the specificity of the source.
- C) the continued relevance of the source.
- D) both the specificity of the source & the continued relevance of the source.
- E) none of these answers is correct.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

61. Which of the following statements is correct?

- A) There is no hierarchy with respect to primary sources of GAAP.
- B) There is no hierarchy with respect to secondary sources of GAAP.
- C) Both primary and secondary sources of GAAP have established hierarchies.
- D) Neither primary nor secondary sources of GAAP have established hierarchies.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

62. The disclosed basis of accounting refers to

- A) the use of non-GAAP policies by private companies.
- B) the use of non-GAAP policies by any company.
- C) the use of International Financial Reporting Standards.
- D) the practice of disclosing all pertinent accounting policies in a company's annual report.

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

63. Private placements refer to:

- A) funds not disclosed by private companies.
- B) debt or equity securities issued to individuals or organizations without being listed with a securities commission.
- C) shares that form part of a control block.
- D) all of these answers are correct.

Ans: B

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 5

64) Which of the following statement(s) is(are) correct?

- A) Companies that use the disclosed basis of accounting are in effect using differential reporting,
- B) Companies that use the disclosed basis of accounting are NOT allowed to use differential reporting,
- C) When used, the disclosed basis of accounting must comply with GAAP.
- D) both “companies that use the disclosed basis of accounting are NOT allowed to use differential reporting” and “when used, the disclosed basis of accounting must comply with GAAP” are correct.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 2

65. Lenders and creditors are most concerned with a company's

- A) profitability.
- B) adherence to covenants.
- C) solvency.
- D) cash flows.

Ans: D

Difficulty: Easy

Level of Learning: Knowledge

Topic: LO 5

66. Discuss in general the due process procedure the AcSB follows in developing accounting standards. Who are the groups which typically have opposing views when it comes to accounting standards, and why?

Ans: After identifying an issue of interest, the AcSB writes a project proposal which defines the terms of reference, the need and scope of the issue, and those affected. A task force is made up to monitor the issue to its conclusion. An issues paper may be prepared to help the AcSB members to appreciate the problems. A statement of principles is usually prepared to outline the basic response to the issues raised. Input is then sought on a private and confidential basis to fine-tune the issues. After AcSB approval, an exposure draft is developed and circulated to all interested parties and input is requested. Revisions may result in a re-exposure draft being circulated again for further public input. Finally, a 2/3 vote by the AcSB is required to approve a new section of the CICA Handbook.

The two groups with frequently opposing views are the preparers (reporting companies) and the investment community. Reporting companies base their arguments for or against a standard on how their interests might be affected by a new standard. The investment community typically wants expanded disclosure to enable the best possible decisions concerning resource allocation, and favours neutral reporting. The AcSB prefers neutral financial accounting principles to principles which would have a goal of influencing particular types of economic activity or government regulation.

Difficulty: Hard
Level of Learning: Application
Topic: LO 2

67. What is GAAP, how is it currently defined, and what is the outcome of the due process?

Ans: GAAP is the set of rules, procedures, policies and customs, which govern measurement, recognition and disclosure in financial statements. Currently, the bulk of GAAP is defined as those pronouncements promulgated by the Accounting and Auditing Research Committee, Accounting Research Committee, and Accounting Standards Board, which have not been superseded by later pronouncements. Primarily, these consist of the Accounting recommendations in the Handbook and when a matter is not covered by a Recommendation, other accounting principles that either:

- (a) are generally accepted by virtue of their use in similar circumstances by a significant number of entities in Canada; or
- (b) are consistent with the Recommendations in the Handbook and are developed through the exercise of professional judgement, including consultation with other informed accountants where appropriate, and the application of the concepts. In exercising professional judgement, established principles for analogous situations dealt with in the Handbook would be taken into account and reference would be made to:
 - (i) other relevant matters dealt with in the Handbook;
 - (ii) practice in similar circumstances;
 - (iii) Accounting Guidelines;
 - (iv) Abstracts of Issues Discussed by the CICA Emerging Issues Committee
 - (v) International Accounting Standards published by the International Accounting Standards Committee;
 - (vi) standards published by bodies authorised to establish financial accounting standards in other jurisdictions;
 - (vii) CICA research studies; and
 - (viii) other sources of accounting literature such as textbooks and journals.

The relative importance of these various sources is a matter of professional judgement in the circumstances. (CICA Handbook, Section 1000)

Difficulty: Hard
Level of Learning: Application
Topic: LO 2

68. Discuss the reasons why a corporation would have the motive or the tendency to adopt the same accounting practices for financial reporting purposes as for tax reporting.

Ans: The term used to for adopting the same accounting practices for financial reporting purposes as for tax reporting is book-tax conformity. Many accountants feel that disclosure of variations between tax and book reporting on the tax return is a "red flag" for Revenue Canada and invites a tax audit. Examples would include the deferral of revenues and the acceleration of expense recognition. Revenue Canada generally takes a dim view of a corporation's recognizing revenue in the income statement while deferring recognition for tax purposes.

Difficulty: Hard
Level of Learning: Application
Topic: LO 5

69. The International Accounting Standards Committee (IASC), established in 1973 has the objective to promote the worldwide harmonization of accounting principles. Is this harmonization necessary to allow movement of capital between countries?

Ans: Although there is pressure from securities regulators and public accountants to harmonize worldwide accounting standards, there is little evidence to suggest that such harmonization is needed in order to facilitate the international movement of capital.

Difficulty: Medium
Level of Learning: Application
Topic: LO 2

70. Why is the response time more rapid for the Financial Standards Board (FASB) in the U.S. who issue Statements of Financial Accounting Standards (SFAS) than the CICA AcSB who take as much as two years to bring new Handbook Recommendations to fruition.

Ans: FASB has a full-time paid Board of seven members that is supplemented by a full-time professional staff of about 30. The AcSB is made up of members who serve on a volunteer basis.

Difficulty: Medium
Level of Learning: Application
Topic: LO 7

71. Compared to financial accounting, what are the major concerns of managerial accounting?

Ans: Management accounting is concerned with preparing and analyzing information for the exclusive use of management for decision-making, planning, employee motivation, and internal performance evaluation. The level of detail is much greater and the basis of accountability may differ from that presented in the organization's financial statements.

Difficulty: Medium
Level of Learning: Application
Topic: LO 1

72. The CICA Board of Directors chooses at least eight of the voting members of the AcSB (including the chairperson), while the other groups are invited to appoint one member each. Name the other groups.

Ans: Canadian Council of Financial Analysis
Financial Executives Institute of Canada
Canadian Academic Accounting Association
Certified General Accountants' Association of Canada
Society of Management Accountants of Canada

Difficulty: Medium
Level of Learning: Application
Topic: LO 2

73. Creditors and analysts who attempt to assess and predict future cash flows tend to prefer earnings measures that are supported by operating cash flows taken from the Cash Flow Statement. What comparisons do they use in assessing the entity's strength in respect of operating cash flows?

Ans: Creditors and analysts often use the reported cash flow from operations to calculate cash flow per share. They compare the operating cash flow per share with the earnings per share and conclude that if there is a higher degree of correspondence between the two measures, the company has high quality earnings. If there is a wide disparity between the two, then the company is said to have low quality earnings.

Difficulty: Medium
Level of Learning: Application
Topic: LO 5

74. Give examples of provisions, known as maintenance tests or covenants which are often contained in debt contracts or agreements.

Ans: a) maximum debt: equity ratio
b) a maximum percentage of dividend pay-out
c) a minimum times-interest-earned ratio
d) a minimum level of shareholders' equity

Difficulty: Medium
Level of Learning: Application
Topic: LO 5

75. Instead of maximizing reported earnings, management may wish to minimize reported earnings an ongoing endeavour. Besides income tax minimization, what are some of the reasons why management would want to minimize earnings?

Ans: a) to avoid public embarrassment by reducing a high level of reported earnings.
b) to avoid attracting competitors into a very lucrative business.
c) to discourage hostile take-over bids.
d) to avoid the scrutiny of regulators or politicians; or
e) to discourage large wage claims (or to justify initiatives for wage reductions and cutbacks).

Difficulty: Medium
Level of Learning: Application
Topic: LO 5

76. Briefly explain how the CRA (Revenue Canada) differs from most GAAP based policies in terms of revenue recognition

Ans: Most GAAP-based policies recognize revenues as they are earned. In general, CRA takes the view that revenues are to be taxed when they are collected, while expenses are deductible for tax purposes when paid. Essentially, CRA works on the 'cash basis' while most GAAP policies are "accrual" based.

Difficulty: Medium
Level of Learning: Application
Topic: LO 5

77. Do you think that most companies in the oil sector would adopt expanded disclosure policies or simply adhere to minimum compliance requirements? Explain.

Ans: Students answers are sure to vary here, and for this reason this would be a good question for class-discussion purposes. While many responses may be valid, it can be argued that oil companies would be under enormous pressure to disclose as much information about their activities as possible. Rightly or wrongly, oil companies are often thought to be exploiting the environment for their own benefit. Moreover, many consumers still believe that they are being "gouged" by these companies. As a result, companies in the oil sector are not viewed favourably by many people. As a result of these negative perceptions, these companies would feel pressured to provide expanded disclosures in their annual reports, to show that they are good corporate citizens.

Difficulty: Medium
Level of Learning: Application
Topic: LO 5

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Chapter 2 – Accounting Judgments

1. Recognition requires the measurement of an item for inclusion in the financial statements.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 5

2. The use of historical cost, rather than liquidation value, is supported by the continuity assumption.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 5

3. Legally, as well as for accounting statement purposes, a corporation is treated as a separate entity apart from its stockholders, whereas a partnership is treated as one entity including the owners.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 3

4. The time period concept dictates that the reporting period or fiscal period of an entity must be for 12 months.

Ans: False
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 3

5. Under the productive capacity capital maintenance approach, a profit is assumed to have been earned only if enough financial capital has been recovered by the end of the year to enable the business to operate at the same level as at the beginning of the year.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 5

6. Information is reliable when it is in agreement with the actual underlying transactions and events, the agreement is capable of independent verification and the information is reasonably free from error and bias.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 4

7. The going concern principal does not apply if a company is expected to be liquidated in the next 24 months.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 3

8. Relevance is of primary importance in financial reporting, whereas comparability is of secondary importance.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 3

9. Inter-period comparability is significantly enhanced when two similar companies use the same accounting methods during a single reporting period.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 1

10. Information is neutral when it is free from bias that would lead users towards making decisions that are influenced by the way the information is measured or presented.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 5

11. When capital assets such as land, building and equipment are acquired, they should be recorded in the accounts in conformity with the cost principle.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

12. The conservatism principle no longer applies under IFRS as it has been replaced by prudence.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

13. Accounting should provide information that is useful in assessing the "value" of an entity; however, accounting information does not necessarily report the actual "value" of the entity.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

14. At times, reliability must be sacrificed in order to enhance the relevance of accounting information.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 1

15. To Recording periodic amortization on assets such as buildings or machinery is an application of the matching principle.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 1

16. The primary medium used by a business to communicate accounting information is its periodic financial statements.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

17. The matching concept is the name applied to the process of associating expenses with revenues.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

18. An example of the full disclosure principle would be a firm signing a major contract in November to construct custom machinery for a client. Work in the current year is nil, yet the notes to the firm's financial statements discuss the nature and dollar amount of the contract.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

19. The information contained in financial statements should be understandable to persons who have a reasonable understanding of business and economic conditions and are willing to study the information with reasonable diligence.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

20. One of the objectives of financial reporting is to help users assess the amounts, timing and uncertainty of prospective cash flows of the enterprise.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

21. The continuity assumption holds that the entity will continue in business for the foreseeable future but it does not mean that it will be a going concern forever.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

22. Revenue is recognized when service is rendered and collection is probable.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

23. Conservatism is one of the underlying assumptions in accounting.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

24. Under IFRS, a change in accounting policy must result in information that is more relevant and reliable.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 6

25. The revenue recognition principle requires the cash basis of accounting because revenue should not be recorded until the earnings process is complete.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 6

26. In order to recognize sales revenue, collection of cash from the buyer is not necessary; however, collection must be reasonably assured.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

27. Revenues from the performance of service cannot be recognized until all of the service has been performed.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

28. Warranty expense on goods sold should be recognized in the period of the sale, even though the costs to fulfill warranty claims will not be incurred until two or three years later.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 6

29. The full disclosure principle asserts that the financial reports of a business enterprise should disclose all reliable information relating to its economic affairs.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

30. Both ASPE and IFRS allow for voluntary changes in accounting policy.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

31. Relevance and reliability are fundamental qualities under IFRS and ASPE.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 3

32. The separate entity assumption applies only to legally separate entities such as corporations; it does not apply to proprietorships or other unincorporated businesses.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 3

33. Managers must put aside their own motivations if they are to act ethically and in the best interest of all stakeholders.

Ans: True
Difficulty: Easy
Level of Learning: Knowledge
Topic: LO 2

34. Comparability is an enhancing quality under IFRS and ASPE.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 4

35. The cost-benefit trade-off is a persuasive constraint under both IFRS and ASPE.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 4

36. As of 2011, public companies in Canada must adhere to IFRS.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 5

37. Private entities in Canada are forbidden from using IFRS.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 5

38. Materiality is a component of representational faithfulness under IFRS.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 4

39. Conservatism was removed from the IFRS Conceptual framework since it is not neutral and may introduce bias.

Ans: True
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 4

40. Full disclosure is one of the underlying assumptions in accounting.

Ans: False
Difficulty: Medium
Level of Learning: Knowledge
Topic: LO 3

41. Verifiability focuses on the correct application of a basis of measurement rather than its appropriateness.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

42. Under IFRS and ASPE, assets and liabilities must both arise from past events.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

43. The quality of information that gives assurance that it is reasonably free of error and bias and is a faithful representation is relevance.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

44. All relevant and reliable information must be presented in the financial statements regardless of the total cost of developing the information.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

45. Comparability is sometimes sacrificed for conservatism.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

46. If accounting information is timely and has predictive and feedback value, then it can be characterized as qualitative.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

47. Financial information does not demonstrate consistency when a company changes its estimate of the salvage value of capital assets.

Ans: True

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

48. In classifying the elements of financial statements, the primary distinction between revenues and gains is the materiality of the amounts involved.

Ans: False

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 7

49. The going concern or continuity assumption is critical to financial accounting. The assumption

- A) Is always maintained for all firms for all years
- B) Supports the use of historical cost valuation for assets rather than market values
- C) Means that a corporation has a definite ending date
- D) Requires that we immediately expense prepaid accounts because they do not represent a future cash inflow

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

50. The objective of financial reporting is:

- A) To provide the market value of a firm at a point in time
- B) To provide the total market value of its common stock
- C) To provide information useful for decision making by investors and creditors
- D) To require all companies to comply with GAAP

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

51. A company reports only its total accounts receivable balance in its balance sheet, as opposed to a complete listing of its individual customer balances. This is an example of:

- A) Cost/benefit
- B) Materiality
- C) Reliability
- D) Conservatism

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

52. A firm's accounting policy is to immediately expense the cost of metal wastebaskets it purchases for use by its employees at their desks. The total cost of wastebaskets in any year is \$1,000 and the firm has \$6 billion in total assets. The firm expects the wastebaskets to last indefinitely. The firm

- A) Is violating GAAP
- B) Is invoking the materiality constraint
- C) Is invoking the conservatism constraint
- D) Is violating the relevance principle
- E) None of these answers is correct.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

53. The sales manager of a firm has the use of a blue company-owned automobile to use to visit potential customers. The sales manager also owns her own identical car except that it is red. The manager paid for the red car with funds earned from her employment as sales manager. The firm will report the cost of the blue auto in its balance sheet, but not the red auto. This is an example of:
- A) Reliability
 - B) Matching
 - C) Separate entity
 - D) Going concern
 - E) None of these answers is correct

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

54. Preparation of financial statements with adequate notes is primarily based on the:
- A) separate entity assumption.
 - B) full-disclosure principle.
 - C) cost principle.
 - D) cost/benefit constraint.
 - E) reliability quality.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

55. Which of the following accounting concepts best justifies the use of accruals and deferrals?
- A) Cost/benefit constraint
 - B) Unit-of-measure assumption
 - C) Continuity assumption
 - D) Materiality constraint

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

56. Accounting traditionally has been influenced by conservatism because of the:

- A) probability of undetected errors in the financial statements.
- B) difficulty in measuring net income on the accrual basis.
- C) inherent uncertainties of many accounting measurements.
- D) difficulty in making certain calculations.
- E) large number of transactions recorded in any one period.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

57. The continuity assumption is the basis for the rule that:

- A) the income statement should not include material gains and losses that are both unusual and infrequent.
- B) treasury stock should not be reported in the balance sheet as an asset.
- C) the cost of installing a machine should not be included in the recorded cost of the machine, but rather expensed immediately.
- D) the cost of operational assets should be allocated to expense systematically and rationally over their useful lives.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

58. S Corporation offered to issue 5,000 shares of its no par value common shares to another company in exchange for a building at a time when there were 1,000,000 shares already outstanding and were selling for \$4.00 per share at the time. The owner of the building had the opportunity to sell it to a competing buyer for \$26,000. However, because the seller wanted the S Corporation shares, S's offer was accepted. At what amount should the building be reported in S's financial statements?

- A) \$26,000
- B) \$10,000
- C) \$20,000
- D) \$16,000

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

59. A trust company will loan up to \$500,000 to preferred customers. The company charges 10% interest based on the amount of the collateral. However, due to the fact that they admired one of their clients, they loaned him \$200,000 and charged only 6% interest. The amount of revenue that should be recognized by the trust company in conformity with the revenue recognition principle is:
- A) \$50,000
 - B) \$30,000
 - C) \$20,000
 - D) \$12,000

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

60. C Corporation exchanged 20,000 shares of its nonconvertible preferred shares for land owned by B Corporation. A competing buyer previously had offered \$150,000 cash for the land. Because of tax consequences, the cash offer was not accepted and the lot was exchanged for the shares. C Corporation previously had sold only 100 shares of its preferred shares at \$9 per share several months ago. Based on the cost principle, at what amount should the land be reported on C's financial statements?
- A) \$180,000
 - B) \$165,000
 - C) \$150,000
 - D) \$160,000

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

61. The list price of a new van was \$30,000 at a local car dealership. However, a customer convinced the dealer to sell the van for \$25,000 (the van had cost the dealer \$20,000). The amount of revenue that would be recognized by the dealer as a result of the sale is:
- A) \$30,000
 - B) \$25,000
 - C) \$10,000
 - D) \$ 5,000

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

62. An appliance company received a bill for \$6,000 from a contractor for services rendered. The contractor was building a new home and wanted payment in the form of new appliances. The appliance company settled the bill by giving the contractor appliances, which usually sold for \$5,000. The amount of revenue that should be recognized by the appliance company is:
- A) \$6,000
 - B) \$5,000
 - C) \$5,500
 - D) \$1,000
 - E) Not determinable.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

63. Accounting information is considered to be relevant when it
- A) can be depended on to represent the economic conditions and events that it is intended to represent.
 - B) is capable of making a difference to a decision-maker.
 - C) is understandable by reasonably informed users of accounting information.
 - D) is verifiable and neutral.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

64. The quality of information that gives assurance that it is reasonably free of error and bias and is a faithful representation is
- A) relevance.
 - B) reliability.
 - C) verifiability.
 - D) neutrality.
 - E) none of these answers is correct.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

65. Timeliness is an ingredient of the qualitative criteria of

	Relevance	Reliability
1	Yes	Yes
2	No	Yes
3	Yes	No
4	No	No

- A) Choice 1
- B) Choice 2
- C) Choice 3
- D) Choice 4

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

66. Verifiability is an ingredient of the qualitative criteria of

	Relevance	Reliability
1	Yes	No
2	Yes	Yes
3	No	No
4	No	Yes

- A) Choice 1
- B) Choice 2
- C) Choice 3
- D) Choice 4

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

67. Neutrality is an ingredient of the qualitative criteria of

	Relevance	Reliability
1	Yes	Yes
2	No	Yes
3	Yes	No
4	No	No

- A) Choice 1
- B) Choice 2
- C) Choice 3
- D) Choice 4

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

68. Predictive value is an ingredient of the qualitative criteria of

	Relevance	Reliability
1	Yes	No
2	Yes	Yes
3	No	No
4	No	Yes

- A) Choice 1
- B) Choice 2
- C) Choice 3
- D) Choice 4

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

69. Representational faithfulness is an ingredient of the qualitative criteria of

	Reliability	Relevance
1	Yes	Yes
2	No	Yes
3	Yes	No
4	No	No

- A) Choice 1
- B) Choice 2
- C) Choice 3
- D) Choice 4

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

70. A primary objective of financial reporting is to:

- A) assist investors in predicting prospective cash flows.
- B) assist investors in analyzing the economy.
- C) assist suppliers in determining an appropriate discount to offer a particular company.
- D) enable banks to determine an appropriate interest rate for their commercial loans.

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

71. Which of the following is an incorrect statement?

- A) Theory can be defined as a coherent set of hypothetical, conceptual, and pragmatic principles forming a general frame of reference for a field of inquiry.
- B) Accounting theory in Canada was developed primarily in response to government regulations.
- C) Concepts are components of theory.
- D) Financial statement elements form part of the conceptual framework of accounting.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

72. Accounting concepts are not derived from:

- A) Inductive reasoning.
- B) Experience.
- C) Pragmatism.
- D) Laws of nature.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

73. If, in year 1, a company used LIFO; year 2, FIFO; and in year 3, moving average cost for inventory valuation, which of the following assumptions, constraints, or principles would be violated:

- A) cost.
- B) time period.
- C) matching.
- D) consistency.
- E) materiality.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

74. Which of the following qualities does the cost principle primarily support?

- A) Predictive value
- B) Conservatism
- C) Verifiability
- D) Timeliness

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

75. The inclusion of notes and supporting schedules in the financial statements reflect application of the:
- A) time period assumption.
 - B) industry peculiarities constraint.
 - C) relevance quality.
 - D) full-disclosure principle.
 - E) comparability characteristic.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

76. Certain costs of doing business are capitalized when incurred and then amortized over subsequent accounting periods to:
- A) aid management in decision-making.
 - B) match the costs incurred with revenues earned.
 - C) conform to the conservatism constraint.
 - D) conform to the comparability characteristic.
 - E) reduce the income tax.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 5

77. Adjusting entries are needed because an entity:
- A) has earned revenue during the period by selling products from its central operations.
 - B) has expenses.
 - C) uses the accrual basis of accounting.
 - D) uses the cash basis of accounting rather than the accrual basis.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 1

78. A large international corporation immediately expenses the \$50 cost of a small item of office equipment. This is an example of:
- A) reliability.
 - B) conservatism.
 - C) materiality.
 - D) an accounting error.
 - E) none of these answers is correct.

Ans: C

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

79. When an \$30 asset with a six-year estimated useful life is recorded as an expense at the date of purchase, this is an application of the:
- A) matching principle.
 - B) cost principle.
 - C) unit-of-measure assumption.
 - D) materiality constraint.
 - E) none of these answers is correct.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3-4

80. Which of the following distinguishes the personal transactions of business owners from business transactions?
- A) Unit-of-measure assumption
 - B) Full-disclosure principle
 - C) Materiality constraint
 - D) Separate entity assumption

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

81. A corporation needed a new warehouse; a contractor quoted a \$250,000 price to construct it. The corporation believed that it could build the warehouse for \$215,000 and decided to use company employees to construct the warehouse. The final construction cost incurred by the corporation was \$240,000 but the asset was recorded at \$250,000. This is in violation of the:
- A) cost principle.
 - B) time period assumption.
 - C) matching principle.
 - D) revenue recognition principle.
 - E) none of these answers is correct.

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

82. Which of the following is the incorrect basis for recognizing the expense indicated?
- A) Sales commissions expense on the basis of relationship with sales.
 - B) Administrative salaries expense recognized as incurred.
 - C) Amortization expense on the basis of time.
 - D) Cost of goods sold expense on a subjective or arbitrary basis.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 6

83. When a corporation buys a portion of its own common shares, the recording must conform to the:
- A) matching principle.
 - B) cost principle.
 - C) revenue recognition principle.
 - D) accrual principle.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 6

84. A corporation reports the sale of some of its shares to a shareholder in its financial statements, and the shareholder reports the same transaction as an investment. Therefore,
- A) the revenue recognition principle has been violated.
 - B) the separate entity assumption has been violated.
 - C) the double entry accounting concept has been violated.
 - D) no accounting concept has been violated.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

85. The separate entity assumption:
- A) requires periodic income measurement.
 - B) is applicable to both incorporated and unincorporated businesses.
 - C) is not applicable to an unincorporated business.
 - D) recognizes the legal nature of a business organization.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

86. An accounting error may be all of the following except:
- A) A mistake.
 - B) An inaccurate estimate made in good faith.
 - C) intentional.
 - D) unintentional.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 6

87. Under which of the following will revenues and expenses most likely be reported in the period they are earned or incurred?
- A) Cash basis accounting
 - B) A combination of accrual and cash basis accounting
 - C) Single entry accounting
 - D) Accrual basis accounting

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

88. Estimating bad debt expense for the period is based primarily on the:

- A) cost principle.
- B) conservatism constraint.
- C) full-disclosure principle.
- D) revenue recognition principle.
- E) matching principle.

Ans: E

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

89. A corporation made the following entries:

A	Prepaid insurance	900	
	Cash		900
B	Depreciation expense	10,000	
	Accumulated depreciation.		10,000
C	Wages payable.	3,000	
	Cash.		3,000
D	Inventory of Merchandise.	4,000	
	Accounts payable.		4,000

Which entry must have been made as a direct result of the matching principle?

- A) A
- B) B
- C) C
- D) D

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

90. The assumption that dollars will buy the same quantity of goods and services today as they would have five years ago is the:
- A) revenue recognition principle.
 - B) time period assumption.
 - C) separate entity assumption.
 - D) unit-of-measure assumption.
 - E) continuity assumption.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3

91. Revenues and expenses often are recognized in income statement accounts even though no cash has been received or paid. This is primarily a result of applying the:
- A) full-disclosure principle.
 - B) continuity assumption.
 - C) revenue recognition principle.
 - D) accrual basis of accounting.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

92. The underlying assumptions of accounting include all of the following except:
- A) unit-of-measure.
 - B) separate entity.
 - C) time period.
 - D) continuity.
 - E) conservatism.

Ans: E

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

93. The measurement conventions of accounting include all of the following except:

- A) continuity.
- B) full-disclosure.
- C) historical cost.
- D) matching.
- E) revenue recognition.

Ans: A

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

94. The implementation constraints include all of the following except:

- A) materiality.
- B) conservatism.
- C) cost/benefit.
- D) separate entity.
- E) industry peculiarities.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

95. The underlying concept that the value of accounting information must exceed the expenditures incurred to provide it is called the:

- A) substance over form.
- B) cost/benefit implementation constraint.
- C) conservatism.
- D) full-disclosure principle.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 3-4

96. The materiality constraint:

- A) is only relevant when preparing annual financial statements as opposed to quarterly statements.
- B) is applicable only for low-cost items that cost less than, say, \$500.
- C) is the only defence for gross negligence by an independent accountant.
- D) does not necessarily imply that an immaterial amount can be ignored for accounting purposes.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

97. The use of deferrals and accruals is a direct result of the:

- A) unit-of-measure assumption.
- B) time period assumption.
- C) cost/benefit constraint.
- D) separate entity assumption.
- E) revenue recognition principle.

Ans: B

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4

98. An item is not material if:

- A) The accounting equation ($A = L + OE$) does not include the item.
- B) It decreases the qualitative usefulness of the financial statements, but not the quantitative usefulness.
- C) Its cost is less than \$25.
- D) Its omission will not influence the judgement of a reasonable person.

Ans: D

Difficulty: Medium

Level of Learning: Knowledge

Topic: LO 4