***Introduction to Financial Accounting, 11e* (Horngren)**

**Chapter 1 Accounting: The Language of Business**

Learning Objective 1.1 Questions

1) The primary purpose of financial accounting is to

A) supply information for external users' decision making.

B) provide data for internal users' decision making.

C) produce data for income taxes.

D) create an audit report.

E) organize the data for management.

Answer: A

Diff: 1

Objective: L.O. 1-1

2) Footnotes are

A) included in the audit report.

B) an integral part of financial statement information.

C) an appendix to the letter from corporate management.

D) at the bottom of the report of the independent auditors.

E) explanatory information in the statement of management's responsibility for preparation of financial statements.

Answer: B

Diff: 2

Objective: L.O. 1-1

3) Accountants analyze and record

A) economic events.

B) costs.

C) revenues.

D) financial statements.

E) creditor statements.

Answer: A

Diff: 1

Objective: L.O. 1-1

4) Annual reports include all, but which of the following?

A) A letter from corporate management

B) Footnotes that explain many elements of the financial statements in more detail

C) The report of the independent registered public accounting firm (auditors)

D) Statements by both management and auditors on the company's internal controls

E) The company's handbook for new employees

Answer: E

Diff: 2

Objective: L.O. 1-1

5) The accountant at Forgum Corporation is asked to prepare the financial statements for the month of July. Which financial statement will he NOT prepare?

A) Balance sheet

B) Income statement

C) Statement of earnings and taxation

D) Statement of cash flows

E) Statement of stockholders' equity

Answer: C

Diff: 1

Objective: L.O. 1-1

6) Which of the following would be classified as external users of financial statements?

A) Creditors of the organization and the Internal Revenue Service

B) Stockholders and the CFO of the organization

C) Management of the organization and the audit firm

D) Management of the organization and SEC

E) Stockholders and middle managers of the organization

Answer: A

Diff: 2

Objective: L.O. 1-1

7) Which of the following individuals are most interested in management accounting information for Dotty Industries?

A) Bankers who loan money to Dotty Industries

B) The IRS, who Dotty Industries pays taxes to

C) Stockholders who buy stock in Dotty Industries

D) Management who work for Dotty Industries

E) Suppliers who sell goods to Dotty Industries

Answer: D

Diff: 2

Objective: L.O. 1-1

8) The governmental agency that regulates the stock market and the financial reporting of firms that trade in the market is the

A) Financial Accounting Standards Board.

B) Internal Revenue Service.

C) Public Company Accounting Oversight Board.

D) Securities and Exchange Commission.

E) Generally Accepted Accounting Board.

Answer: D

Diff: 1

Objective: L.O. 1-1

9) Accounting does not provide information that is useful in making decisions that have economic consequences.

Answer: FALSE

Diff: 2

Objective: L.O. 1-1

10) Because officials in federal, state, and local governments are not in the business of making a profit, they do not need an understanding of accounting.

Answer: FALSE

Diff: 2

Objective: L.O. 1-1

11) Financial accounting serves external decision makers, such as suppliers, banks, government agencies, and stockholders.

Answer: TRUE

Diff: 1

Objective: L.O. 1-1

12) Management accounting serves internal decision makers, such as top executives and department heads.

Answer: TRUE

Diff: 1

Objective: L.O. 1-1

13) Managerial accounting serves external users while financial accounting serves internal users.

Answer: FALSE

Diff: 2

Objective: L.O. 1-1

14) The annual report is a document prepared by the board of directors and distributed to current and potential investors.

Answer: FALSE

Diff: 1

Objective: L.O. 1-1

15) It is against SEC regulations to promote the corporation in the annual report.

Answer: FALSE

Diff: 1

Objective: L.O. 1-1

16) Describe the differences between financial accounting and management accounting.

Answer: Financial accounting focuses on the specific needs of decision makers external to the organization such as stockholders, suppliers, banks, and government agencies. Management accounting serves internal decision makers, such as top executives, department heads, college deans, hospital administrators, and people at other management levels within an organization. The two fields of accounting share many of the same procedures for analyzing and recording the effects of individual transactions.

Diff: 2

Objective: L.O. 1-1

Learning Objective 1.2 Questions

1) A liability that results from a purchase of goods or services on open account is referred to as a(n)

A) accounts receivable.

B) notes payable.

C) accounts payable.

D) notes receivable.

E) capital stock.

Answer: C

Diff: 1

Objective: L.O. 1-2

2) Which of the following statements is true?

A) Owners' equities are economic sacrifices after deducting liabilities.

B) Assets are expected to benefit no one.

C) Liabilities are future cash inflows.

D) Assets are always the sum of liabilities and owners' equities.

E) Owners' equities have priority over liabilities for assets upon liquidation.

Answer: D

Diff: 1

Objective: L.O. 1-2

3) The accounting equation can be stated as which of the following?

A) Assets - liabilities = owners' equity

B) Assets + liabilities = owners' equity

C) Liabilities + assets = owners' equity

D) Owners' equity + assets = liabilities

E) Liabilities - owners' equity = assets

Answer: A

Diff: 2

Objective: L.O. 1-2

4) Which of the following describes a liability?

A) Future economic benefit

B) Economic obligations to creditors

C) Paid-in capital

D) Investment by owners

E) Present value of customer future payments

Answer: B

Diff: 2

Objective: L.O. 1-2

5) Notes Payable are classified as

A) equity.

B) assets.

C) owner investments.

D) liabilities.

E) expenses.

Answer: D

Diff: 2

Objective: L.O. 1-2

6) Income taxes owed to the federal government would be classified as a(n)

A) liability on the balance sheet.

B) asset on the balance sheet.

C) liability on the statement of cash flows.

D) equity on the balance sheet.

E) They would not appear on a financial statement.

Answer: A

Diff: 2

Objective: L.O. 1-2

7) An example of stockholders' equity is

A) accounts payable.

B) accounts receivable.

C) capital stock.

D) marketable securities.

E) cash and cash equivalents.

Answer: C

Diff: 1

Objective: L.O. 1-2

8) Statement of financial position is another name for the balance sheet.

Answer: TRUE

Diff: 1

Objective: L.O. 1-2

9) Assets and owners' equity are presented on the right side of the balance sheet.

Answer: FALSE

Diff: 1

Objective: L.O. 1-2

10) The balance sheet equation is assets = liabilities - owner's equity.

Answer: FALSE

Diff: 1

Objective: L.O. 1-2

11) Liabilities are economic obligations of the organization to outsiders, or claims against its assets by outsiders.

Answer: TRUE

Diff: 2

Objective: L.O. 1-2

12) Accountants use the terms notes payable or notes receivable to describe the existence of promissory notes.

Answer: TRUE

Diff: 1

Objective: L.O. 1-2

13) Examples of assets include cash, inventory, and capital stock.

Answer: FALSE

Diff: 1

Objective: L.O. 1-2

14) Inventory is goods held by a company for the purpose of sale to customers, and is considered a liability on the balance sheet.

Answer: FALSE

Diff: 2

Objective: L.O. 1-2

15) A balance sheet is dated for a period of time, such as "for the year ended December 31, 20X2."

Answer: FALSE

Diff: 1

Objective: L.O. 1-2

16) Owners' equity is the residual interest in the organization's assets after deducting liabilities.

Answer: TRUE

Diff: 1

Objective: L.O. 1-2

17) Long-term debt $ 190

Cash (1)

Total stockholders' equity (2)

Total liabilities (3)

Accounts receivable 450

Common stock 75

Inventory 375

Accounts payable 575

Property, plant, and equipment 525

Additional stockholders' equity 650

Other assets 200

Other liabilities (4)

Total assets 2,000

Using the balance sheet equation as a starting point, determine the missing amounts: (1), (2), (3), and (4) above.

Answer:

(1) $2,000 - $450 - $375 - $525 - $200 = $450

(2) $75 + $650 = $725

(3) $2,000 - $725 = $1275

(4) $1,275 - $575 - $190 = $510

Diff: 2

Objective: L.O. 1-2

18) What is the purpose of a balance sheet?

Answer: A balance sheet shows the financial position of an entity at a point in time. The accounting equation is represented in the balance sheet. The balance sheet reports a company's assets, liabilities and owners' equity.

Diff: 2

Objective: L.O. 1-2

Learning Objective 1.3 Questions

1) An entity

A) is a separate economic unit.

B) allows a section of an organization to be a separate economic unit.

C) helps accountants relate events to a defined area of accounting.

D) All of the above

E) None of the above

Answer: D

Diff: 2

Objective: L.O. 1-3

2) If liabilities increase by $10,000 during a given period and stockholders' equity decreases by $6,000 during the same period, assets must have

A) increased by $16,000.

B) increased by $4,000.

C) decreased by $4,000.

D) decreased by $16,000.

E) This cannot be determined with the given information.

Answer: B

Diff: 3

Objective: L.O. 1-3

3) A transaction

A) affects the financial position of an entity.

B) maintains the equality of the balance sheet equation.

C) affects the cash position of an entity.

D) will always change values on the income statement.

E) both A and B

Answer: E

Diff: 2

Objective: L.O. 1-3

4) Surround Sound, LLC owned land originally costing $33,000. A real estate agent appraised the land and stated that it is now worth $38,000. Surround Sound, LLC should

A) increase the land account by $5,000 and increase the capital stock account by $5,000.

B) increase the land account by $5,000 and increase the cash account by $5,000.

C) increase the land account by $5,000 and increase the paid-in capital in excess of par account by $5,000.

D) There is no effect from the increase in the value of the land on the accounts of Surround Sound, LLC.

E) increase the land account and the investment account.

Answer: D

Diff: 2

Objective: L.O. 1-3

5) Which of the following statements is false?

A) If you increase an asset account, you may increase a liability account.

B) If you increase an asset account, you may decrease an asset account.

C) If you decrease an asset account, you may increase an owners' equity account.

D) If you decrease an asset account, you may decrease an owners' equity account.

E) If you increase an asset account, you may increase an owners' equity account.

Answer: C

Diff: 2

Objective: L.O. 1-3

6) Mexland Company, acquired land costing $25,000. Mexland Company paid $10,000 in cash and issued a short-term note for the balance. The effect of this transaction on Mexland Company, would be to

A) increase the land account by $25,000, decrease the cash account by $10,000, and decrease the balance in the notes payable account by $15,000.

B) increase the land account by $25,000, decrease the cash account by $10,000, and decrease the balance in the notes receivable account by $15,000.

C) increase the land account by $25,000, decrease the cash account by $10,000, and increase the balance in the notes receivable account by $15,000.

D) increase the land account by $10,000 and decrease the cash account by $10,000.

E) increase the land account by $25,000, decrease the cash account by $10,000, and increase the balance in the notes payable account by $15,000.

Answer: E

Diff: 2

Objective: L.O. 1-3

7) Assets amount to $35,000 at the beginning of the period and $40,000 at the end of the period. Liabilities amount to $10,000 at the beginning of the period and $20,000 at the end of the period. What is the amount of the change and the direction of the change in owners' equity for the period?

A) Increase of $15,000

B) Decrease of $10,000

C) Increase of $5,000

D) Increase of $10,000

E) Decrease of $5,000

Answer: E

Diff: 2

Objective: L.O. 1-3

8) Smith's Medical Supplies sold unused land at cost, which was $15,000. The buyer paid $6,000 in cash, with the balance to be paid on a note due in 6 months. The effect on Smith's Medical Supplies is to

A) decrease the land account by $15,000, increase the cash account by $6,000, and increase the balance in the notes payable account by $9,000.

B) decrease the land account by $15,000, increase the cash account by $6,000, and increase the balance in the notes receivable account by $9,000.

C) decrease the land account by $15,000, increase the cash account by $6,000, and decrease the balance in the notes receivable by $9,000.

D) decrease the land account by $6,000 and increase the cash account by $6,000.

E) decrease the land account by $15,000, increase the cash account by $6,000, and decrease the balance in the notes payable account by $9,000.

Answer: B

Diff: 2

Objective: L.O. 1-3

9) Mailers Manufacturing, acquired equipment for $19,000. Mailers Manufacturing, paid $6,000 in cash, with the balance due on a note. The effect of this transaction on Mailers Manufacturing, would be to

A) increase the equipment account by $19,000, decrease the cash account by $6,000 and increase the notes payable account by $13,000.

B) increase the equipment account by $19,000, decrease the cash account by $6,000, and decrease the notes receivable by $13,000.

C) increase the equipment account by $6,000, and decrease the cash account by $6,000.

D) increase the equipment account by $6,000, decrease the cash account by $6,000, and increase the notes payable account by $13,000.

E) increase the equipment account by $19,000, and increase the notes payable account by $6,000.

Answer: A

Diff: 2

Objective: L.O. 1-3

10) Zeus Greek Foods purchased a $21,000 van for use in the business. The company made a $15,000 cash down payment, and signed a note for the balance. The effect of this transaction on Zeus Greek Foods would be to

A) increase the van account by $21,000, decrease the cash account by $15,000, and decrease the notes receivable account by $6,000.

B) increase the van account by $21,000, decrease the cash account by $15,000, and decrease the notes payable account by $6,000.

C) increase the van account by $15,000 and decrease the cash account by $15,000.

D) increase the van account by $21,000, decrease the cash account by $15,000, and increase the notes payable account by $6,000.

E) decrease the van account by $15,000 and increase the cash account by $15,000.

Answer: D

Diff: 2

Objective: L.O. 1-3

11) Payton Corporation, acquired some office equipment, including a desk costing $900. The owner of the business next door said that he had been searching for a desk just like that one, so Payton Corporation, sold the desk to its business neighbor at cost, receiving $400 in cash, with the remainder to be paid in 30 days. The effect of this transaction on Payton Corporation, would be to

A) increase the cash account by $400, increase the capital account by $500, and decrease the equipment account by $900.

B) increase the cash account by $400, increase the accounts payable account by $500, and decrease the equipment account by $900.

C) increase the cash account by $400, decrease the accounts payable account by $500, and decrease the equipment account by $900.

D) increase the cash account by $400, increase the accounts receivable account by $500, and decrease the equipment account by $900.

E) increase the cash account by $400, decrease the accounts receivable account by $500, and decrease the equipment account by $900.

Answer: D

Diff: 2

Objective: L.O. 1-3

12) Home Theater Advantage sells audio equipment. Home Theater Advantage acquired 50 speakers from a manufacturer at a cost of $200 per speaker and purchased the speakers on account. The effect of this transaction on Home Theater Advantage would be to

A) increase inventory by $10,000 and increase capital by $10,000.

B) increase inventory by $10,000 and decrease capital by $10,000.

C) increase inventory by $10,000 and decrease cash by $10,000.

D) increase inventory by $10,000 and increase accounts payable by $10,000.

E) increase inventory by $10,000 and decrease accounts payable by $10,000.

Answer: D

Diff: 2

Objective: L.O. 1-3

13) Iacofano Pizza Place acquired equipment costing $11,000 on account. The effect of this transaction on Iacofano Pizza Place would be to

A) increase equipment by $11,000 and decrease capital by $11,000.

B) increase equipment by $11,000 and increase capital by $11,000.

C) increase equipment by $11,000 and increase accounts payable by $11,000.

D) increase equipment by $11,000 and decrease accounts payable by $11,000.

E) No transaction is recorded since no cash has been paid.

Answer: C

Diff: 2

Objective: L.O. 1-3

14) Manziel Inc. is a sole proprietorship owned by Chris Herold. Chris acquired $9,000 worth of equipment for use in his store. He will pay for the equipment in 30 days. The effect of this transaction on Manziel would be to

A) increase the equipment account by $9,000 and increase the accounts payable account by $9,000.

B) increase the equipment account by $9,000 and decrease the accounts payable account by $9,000.

C) increase the equipment account by $9,000 and increase the capital account by $9,000.

D) This would not change any account because the equipment has not been paid for.

E) This would not change any account because this transaction does not affect Manziel Inc.

Answer: A

Diff: 2

Objective: L.O. 1-3

15) Jakey Technologies has 1,000 folders in inventory that cost $2.00 each. The company's supplier announced that, effective immediately, all future folders will cost $2.20 each. Jakey Technologies should

A) increase the inventory account by $200 and increase the capital account by $200.

B) increase the inventory account by $200 and decrease the capital account by $200.

C) increase the inventory account by $200 and increase the accounts payable account by $200.

D) increase the inventory account by $200 and decrease the accounts payable account by $200.

E) There is no effect from the price change on the accounts of Jakey Technologies.

Answer: E

Diff: 2

Objective: L.O. 1-3

16) Sounds Good Entertainment acquired office equipment valued at $4,000 and office supplies valued at $600 by paying cash of $1,300 with the balance on account. The effect of this transaction on Sounds Good Entertainment would be to

A) increase the cash account by $1,300, increase the accounts payable account by $3,300, and increase the office equipment account by $4,600.

B) increase the office equipment account by $4,600, decrease the cash account by $1,300, and decrease the accounts payable account by $3,300.

C) decrease the cash account by $1,300, increase the accounts payable account by $3,300, increase the office equipment account by $4,000, and increase the office supplies by $600.

D) increase the cash account by $1,300, increase the capital account by $3,300, decrease the equipment account by $4,000, and increase the office supplies account by $600.

E) increase the office supplies account by $600, decrease the office equipment account by $4,000, increase the accounts payable account by $4,000, and decrease the cash account by $600.

Answer: C

Diff: 2

Objective: L.O. 1-3

17) Kitty Clips acquired $2,800 worth of merchandise inventory on account. Upon inspection, the company discovered that $400 worth of the merchandise inventory was defective. Kitty Clips returned the defective merchandise inventory and received full credit. The effect of the return transaction on Kitty Clips would be to

A) decrease the merchandise inventory account by $400 and increase the accounts payable account by $400.

B) decrease the merchandise inventory account by $400 and decrease the accounts payable account by $400.

C) decrease the merchandise inventory account by $400 and increase the accounts receivable account by $400.

D) decrease the merchandise inventory account by $400 and decrease the accounts receivable account by $400.

E) Because the merchandise inventory was never used, Kitty Clips would not record the return of the merchandise inventory.

Answer: B

Diff: 2

Objective: L.O. 1-3

18) Stockholders' equity at the beginning and end of the period amounts to $16,000 and $19,000, respectively. Assets at the beginning and end of the period amount to $26,000 and $21,000, respectively. Liabilities at the beginning of the period were $10,000. Liabilities at the end of the period amount to

A) $8,000.

B) $6,000.

C) $2,000.

D) $5,000.

E) $3,000.

Answer: C

Diff: 2

Objective: L.O. 1-3

19) What effect does the purchase of store equipment on account have on the balance sheet equation?

A) Assets increase and liabilities decrease

B) Assets increase and liabilities increase

C) Assets decrease and liabilities decrease

D) Assets decrease and liabilities increase

E) There is no effect on the accounting equation.

Answer: B

Diff: 2

Objective: L.O. 1-3

20) What accounts are affected by an initial investment of cash by an owner into his business?

A) Cash and Owner payable

B) Cash and Long-term debt payable

C) Owner payable and Accounts payable

D) Cash and Capital

E) Cash and Retained earnings

Answer: D

Diff: 2

Objective: L.O. 1-3

21) An owner's investment into a business will increase assets and decrease liabilities.

Answer: FALSE

Diff: 2

Objective: L.O. 1-3

22) An account is a summary record of the changes in a particular asset, liability, or owners' equity.

Answer: TRUE

Diff: 1

Objective: L.O. 1-3

23) A transaction affects the financial position of an entity and can be reliably recorded in terms of money.

Answer: TRUE

Diff: 2

Objective: L.O. 1-3

24) A transaction does not require counterbalancing entries so that the total assets are equal to the total liabilities plus owner's equity.

Answer: FALSE

Diff: 2

Objective: L.O. 1-3

25) A loan from a financial institution will increase assets and increase liabilities.

Answer: TRUE

Diff: 2

Objective: L.O. 1-3

26) The purchase of inventory on credit will increase liabilities and equity.

Answer: FALSE

Diff: 2

Objective: L.O. 1-3

27) Buying on credit creates an account receivable.

Answer: FALSE

Diff: 1

Objective: L.O. 1-3

28) A creditor is one to whom money is owed.

Answer: TRUE

Diff: 2

Objective: L.O. 1-3

29) A payment to a creditor will decrease assets and increase liabilities.

Answer: FALSE

Diff: 2

Objective: L.O. 1-3

30) If assets increase $80,000 during a period and liabilities decrease $40,000, then owners' equity must have decreased $40,000.

Answer: FALSE

Diff: 2

Objective: L.O. 1-3

31) Analyze the following transactions in the balance sheet equation using the following worksheet.

1. Initial investment of $300,000 by the owner

2. Acquire equipment for $25,000 cash

3. Acquire inventory for $6,000 on credit

4. Obtain loan of $15,000 from the bank

5. Returned $600 of inventory to supplier

6. Payment to creditor for amount of inventory purchase less amount returned

 Note Accounts

Transaction Cash Inventory Equipment Payable Payable Capital

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| 1 |  |  |  |  |  |  |
| 2 |  |  |  |  |  |  |
| 3 |  |  |  |  |  |  |
| 4 |  |  |  |  |  |  |
| 5 |  |  |  |  |  |  |
| 6 |  |  |  |  |  |  |

Answer:

 Note Accounts

Transaction Cash Inventory Equipment Payable Payable Capital

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| 1 | +300,00 |  |  |  |  | +300,000 |
| 2 | -25,000 |  | +25,000 |  |  |  |
| 3 |  | +6,000 |  |  | +6,000 |  |
| 4 | +15,000 |  |  | +15,000 |  |  |
| 5 |  | -600 |  |  | -600 |  |
| 6 | -5,400 |  |  |  | -5,400 |  |

Diff: 3

Objective: L.O. 1-3

32) Given below are the daily balances in the accounts of Travel Tips, Inc.. Assuming only one transaction occurred each day, explain the nature of each transaction from June 1 to June 10.

 Accounts Owner,

 Cash Receivable Inventory Equipment Payable Capital

Bal. $6,000 $3,000 $8,000 $7,000 $4,000 $20,000

June 1 6,000 3,000 8,700 7,000 4,700 20,000

June 2 6,600 2,400 8,700 7,000 4,700 20,000

June 3 5,800 2,400 8,700 7,000 3,900 20,000

June 4 6,900 2,400 8,700 7,000 3,900 21,100

June 5 5,600 2,400 8,700 9,600 5,200 21,100

June 6 5,600 2,400 8,200 9,600 4,700 21,100

June 7 6,100 3,700 8,200 7,800 4,700 21,100

June 8 4,000 3,700 8,200 7,800 4,700 19,000

June 9 3,200 3,700 9,000 7,800 4,700 19,000

June 10 3,200 3,700 9,000 9,500 4,700 20,700

Answer:

June 1: Acquired $700 of inventory on credit.

June 2: Received $600 from credit customers.

June 3: Paid $800 in accounts payable.

June 4: Owners invested an additional $1,100 in cash.

June 5: Acquired equipment costing $2,600, paying $1,300 in cash with the remaining $1,300 on account.

June 6: Returned inventory costing $500 and received a reduction in its accounts payable.

June 7: Sold equipment costing $1,800, receiving $500 in cash with the remaining $1,300 owed toTravel Tips

June 8: Owners withdrew $2,100 from Travel Tips company.

June 9: Bought $800 of inventory, paying cash.

June 10: Owners invested equipment in the business valued at $1,700.

Diff: 2

Objective: L.O. 1-3

33) Use the following balance sheet equation format to show the effect of the following transactions. Write the signs (+, -) for increases and decreases in components of the equation for each transaction.

|  |  |  |  |
| --- | --- | --- | --- |
|  | Total assets | Total liabilities | Owners' equity |
| A |  |  |  |
| B |  |  |  |
| C |  |  |  |
| D |  |  |  |
| E |  |  |  |
| F |  |  |  |
| G |  |  |  |

A. The owner invests cash in the company.

B. The company borrows money from a bank, issuing a promissory note payable.

C. The company acquires equipment by paying cash for the total amount.

D. The company acquires inventory from the manufacturer on credit.

E. The company returns part of the inventory purchased in part D.

F. The company sells equipment acquired in part C to a competitor on open account at cost.

G. The company pays the amount due on the inventory purchase in part D.

Answer:

|  |  |  |  |
| --- | --- | --- | --- |
|  | Total assets | Total liabilities | Owners' equity |
| A | + |  | + |
| B | + | + |  |
| C | +, - |  |  |
| D | + | + |  |
| E | - | - |  |
| F | +, - |  |  |
| G | - | - |  |

Diff: 2

Objective: L.O. 1-3

Learning Objective 1.4 Questions

1) Twinkle Toes Dance Company

December 31, 20X9

|  |  |  |  |
| --- | --- | --- | --- |
|  Cash | $10,000 | Accounts payable | $5,600 |
| Accounts receivable | 4,000 | Notes payable | 17,000 |
| Inventory | 8,000 | Common stock | 5,000 |
| Equipment | 14,800 | Retained earnings | 9,200 |
| Total Assets | $36,800 | Total liabilities and shareholders equity | $36,800 |

What is the name of the financial statement above?

A) Income Statement

B) Balance Sheet

C) Statement of Cash Flows

D) Statement of Changes in Shareholders Equity

E) Statement of Retained Earnings

Answer: B

Diff: 2

Objective: L.O. 1-4

2) Following is an alphabetical list of the assets, liabilities, and stock owners' equity accounts of Apex Marketing Solutions. Prepare a balance sheet dated December 31, 20X9.

Accounts payable $ 2,000

Accounts receivable 31,400

Capital stock 25,500

Cash 18,000

Inventory 9,600

Notes payable 14,900

Paid-in capital in excess of par 16,600

Answer: Apex Marketing Solution

 Balance Sheet

 December 31, 20X9

Assets Liabilities and Owners' Equity

 Liabilities:

Cash $18,000 Accounts payable $ 2,000

Accounts receivable 31,400 Notes payable 14,900

Inventory 9,600 Total liabilities $16,900

 Owners' equity:

 Capital stock 25,500

 Paid-in capital in excess of par 16,600

 Total owners' equity 42,100

Total assets $59,000 Total liabilities and owners' equity $59,000

Diff: 2

Objective: L.O. 1-4

3) Presented below are the balances, listed in alphabetical order, of Ferb Products, at December 1,

20X9:

Accounts Payable $ 8,100

Accounts Receivable 4,000

Cash 7,300

Land 15,300

Machinery 31,600

Merchandise Inventory 12,200

Long-term Debt Payable 20,700

Note Payable 2,200

Paid-in Capital 39,400

Following are the transactions for Ferb Products for the month of December 20X9:

a. Borrowed an additional $1,300 in notes payable.

b. Collected $1,900 from credit customers.

c. Paid $2,600 of the amount owed on account.

d.The owners contributed $12,000 cash in exchange for capital.

Required:

1. Prepare an analysis of the transactions on the balance sheet equation.

2. Prepare a balance sheet as of December 31, 20X9, considering the beginning balances and incorporating the effects of the December, 20X9 transactions.

Answer:

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  Cash | Accounts Receivable | Merch. Inventory | Land | Machinery | AccountsPayable | Notes Payable | LT DebtPayable | Paid-in Capital |
| $7,300 | $4,000 | $12,200 | $15,300 | $31,600 | $8,100 | $2,200 | $20,700 | $39,400 |
| +1,300 |  |  |  |  |  | +$1,300 |  |  |
| +1,900 |  -1,900 |  |  |  |  |  |  |  |
| -2,600 |  |  |  |  | -2,600 |  |  |  |
| +12,000 |  |  |  |  |  |  |  | +12,000 |
| $19,900 | $2,100 | $12,200 | $15,300 | $31,600 | $5,500 | $3,500 | $20,700 | $51,400 |

Ferb Products

Balance Sheet

December 31, 20X9

Assets Liabilities and Owners' Equity

 Liabilities:

Cash $ 19,900 Accounts Payable $ 5,500

Accounts Receivable 2,100 Notes Payable 3,500

Merchandise Inventory 12,200 Long-term Debt Payable 20,700

Land 15,300 Total Liabilities 29,700

Machinery 31,600 Owners' Equity:

Total Assets 81,100 Paid-in Capital 51,400

 Total Liab. and Owners' Equity $81,100

Diff: 3

Objective: L.O. 1-3, 1-4

4) Shelly Wagner began a sole proprietorship named Wagner Company on June 1, 20X9. Following are the transactions, which occurred during the first 10 days of June, 20X9.

June 1 Shelly invested $6,600 cash in Wagner Company

June 2 Wagner Company acquired equipment costing $3,900. One-third of the balance was paid in cash with the balance as a note.

June 4 Wagner Company acquired inventory costing $2,200, half of which was paid in cash.

June 5 Wagner Company acquired $200 in supplies on open account.

June 7 Shelly's daughter, Sydney, purchased $600 of equipment, at cost and on open account from Wagner Company

June 9 Wagner Company returned $100 of defective inventory and received a full credit.

June 10 Wagner Company received $200 from Sydney, Shelly's daughter, in partial settlement of her account.

Required:

1. Prepare an analysis of the transactions on the balance sheet equation.

2. Prepare a balance sheet for Wagner Company as of June 10, 20X9.

Answer:

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | Cash | Accounts Receivable | Inventory | Supplies | Equipment | Accounts Payable | Notes Payable | Wagner, Capital |
| June 1 | +$6,600 |  |  |  |  |  |  | +$6,600 |
| June 2 | -1,300 |  |  |  | +3,900 |  | +$2,600 |  |
| June 4 | -1,100 |  | +2,200 |  |  | +1,100 |  |  |
| June 5 |  |  |  | +200 |  | +200 |  |  |
| June 7 |  | +600 |  |  | -600 |  |  |  |
| June 9 |  |  | -100 |  |  | -100 |  |  |
| June 10 | +200 | -200 |  |  |  |  |  |  |
|  | $4,400 | $400 | $2,100 | $200 | $3,300 | $1,200 | $2,600 | $6,600 |

Wagner Company

Balance Sheet

June 10, 20X9

Assets Liabilities and Owner's Equity

 Liabilities:

Cash $ 4,400 Accounts Payable $ 1,200

Accounts Receivable 400 Notes Payable 2,600

Inventory 2,100 Total Liabilities 3,800

Supplies 200 Owner's Equity:

Equipment 3,300 Shelly Wagner, Capital 6,600

Total Assets $10,400 Total Liab. and Owner's Equity $10,400

Diff: 3

Objective: L.O. 1-3, 1-4

5) Abigail and Amanda started the ACL Partnership on September 1, 20X9. Given the following transactions, prepare a balance sheet for the partnership as of September 10, 20X9.

Sept. 1 The ACL Partnership was formed as Abigail invested $9,000 in cash and Amanda invested $4,100 worth of supplies and $4,700 in cash.

Sept. 2 ACL acquired $3,600 in inventory, paying cash.

Sept. 4 ACL acquired equipment costing $23,900, making a $3,500 cash down payment, with the balance due on a note.

Sept. 5 ACL returned $300 worth of defective inventory and received a refund.

Sept. 7 ACL acquired inventory costing $800 on open account.

Sept. 8 ACL sold equipment costing $1,700 at cost. A close friend, purchased the equipment on account.

Sept. 9 ACL paid $400 associated with the inventory acquired on September 7.

Sept. 10 ACL received $400 from the friend who acquired equipment on September 8.

Required:

1. Prepare an analysis of the transactions on the balance sheet equation.

2. Prepare a balance sheet as of September 10, 20X9 for ACL Partnership.

Answer:

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | Cash | Accts.Receiv | Inventory | Supplies | Equip. | Accts. Payable | Notes Payable | Abigail, Capital | Amanda, Capital |
| Sept. 1 | +$9,000 |  |  |  |  |  |  | +$9,000 |  |
|  | +4,700 |  |  | +4,100 |  |  |  |  | +8,800 |
| Sept. 2 | -3,600 |  | +3,600 |  |  |  |  |  |  |
| Sept. 4 | -3,500 |  |  |  | +23,900 |  | +20,400 |  |  |
| Sept. 5 | +300 |  | -300 |  |  |  |  |  |  |
| Sept. 7 |  |  | +800 |  |  | +800 |  |  |  |
| Sept. 8 |  | +1,700 |  |  | -1,700 |  |  |  |  |
| Sept. 9 | -400 |  |  |  |  | -400 |  |  |  |
| Sept 10 | +400 | -400 |  |  |  |  |  |  |  |
|  | $6,900 | $1,300 | $4,100 | $4,100 | $22,200 | $400 | $20,400 | $9,000 | $8,800 |

The ACL Partnership

Balance Sheet

September 10, 20X9

Assets Liabilities and Owners' Equity

 Liabilities:

Cash $ 6,900 Accounts Payable $ 400

Accounts Receivable 1,300 Notes Payable 20,400

Inventory 4,100 Total Liabilities $20,800

Supplies 4,100 Owners' Equity:

Equipment 22,200 Abigail, Capital 9,000

 Amanda, Capital 8,800

 Total Partners' Capital 17,800

Total Assets $38,600 Total Liabilities and Owners' Equity $38,600

Diff: 3

Objective: L.O. 1-3, 1-4

6) The accountant for Tibbo Industries is required to prepare monthly financial statements. Upon opening the file with the previous month's balance sheets, the accountant notices that they have been prepared incorrectly. Prepare a corrected November balance sheet based on the information below.

Balance Sheet for

Tibbo Industries

Prepared on

November 29, 2009

Assets Liabilities and Owners' Equity

Merchandise inventory 8,000 Office supplies 500

Accounts payable 4,500 Long term debt 18,000

Cash 9,000 Owners equity 50,500

Owners' equity 50,500 Prepaid expenses 5,000

Property and equipment 50,500

Answer: Assets

Cash $ 9,000

Merchandise Inventory 8,000

Prepaid expenses 5,000

Office supplies 500

Property and equipment 50,500

Total assets $73,000

Liabilities and Owners' Equity

Liabilities:

Accounts payable $ 4,500

Long term debt 18,000

Total Liabilities 22,500

Owners' equity 50,500

Total Liabilities and Owners' Equity $73,000

Diff: 3

Objective: L.O. 1-4

Learning Objective 1.5 Questions

1) Which of the following statements is false?

A) If a sole proprietorship fails, the creditors can obtain repayment from the personal assets of the single owner.

B) If a partnership fails, the creditors can obtain repayment from the personal assets of the partners.

C) If a corporation fails, the creditors can obtain repayment from the personal assets of the stockholders.

D) A change in ownership among the partners results in the termination of the partnership.

E) Income taxes are not levied against sole proprietorships and partnerships.

Answer: C

Diff: 2

Objective: L.O. 1-5

2) Which of the following statements is false?

A) Most states require stock certificates to have some dollar amount printed on them.

B) Additional paid-in capital is part of total liabilities on the balance sheet.

C) The ultimate responsibility for management of a company is delegated by stockholders to professional managers.

D) Typically, stock is sold for an amount above par value.

E) An advantage of the corporate form of organization is the separation of ownership and management.

Answer: B

Diff: 2

Objective: L.O. 1-5

3) Which of the following forms of business organizations protect the personal assets of the owners from creditors of the business?

A) Partnerships

B) Corporations

C) Proprietorships

D) Partnerships and corporations

E) Partnerships and proprietorships

Answer: B

Diff: 1

Objective: L.O. 1-5

4) Which of the following statements is false?

A) Corporations are business organizations created under federal law.

B) One of the most notable characteristics of a corporation is the limited liability of the owners.

C) An advantage of corporations over other business entities is the ease of transfer of ownership.

D) The laws governing corporations vary from state to state.

E) Individuals can sell stock to each other without corporate involvement.

Answer: A

Diff: 2

Objective: L.O. 1-5

5) A corporation is an organization

A) with owners assuming personal liability for business losses.

B) that joins two or more people together as co-owners.

C) that is an "artificial being" created by individual state laws.

D) that gives stockholders control of everyday management decisions.

E) that does not sell stock to raise capital.

Answer: C

Diff: 1

Objective: L.O. 1-5

6) The form of organization that has limited liability for the owners is a(n)

A) corporation.

B) partnership.

C) proprietorship.

D) cartel.

E) Sarbanes group.

Answer: A

Diff: 1

Objective: L.O. 1-5

7) Which is a disadvantage of a corporation?

A) Limited liability for owners

B) Easy transfer of ownership

C) Ease in raising ownership capital from potential stockholders

D) Management's consumption of perquisites

E) Continuity of existence

Answer: D

Diff: 1

Objective: L.O. 1-5

8) A sole proprietorship is an accounting entity, even though it has only a single owner.

Answer: TRUE

Diff: 1

Objective: L.O. 1-5

9) The owners of a corporation have limited liability.

Answer: TRUE

Diff: 1

Objective: L.O. 1-5

10) Corporations are the most important form of business ownership because they conduct the vast majority of business.

Answer: TRUE

Diff: 2

Objective: L.O. 1-5

11) The effects of the form of ownership of a business entity on income taxes may vary significantly.

Answer: TRUE

Diff: 2

Objective: L.O. 1-5

12) Privately held corporations can be owned by family members, but they still sell stock publicly.

Answer: FALSE

Diff: 2

Objective: L.O. 1-5

13) Describe the three forms of business entities and state how they differ.

Answer: A proprietorship has a single owner whereas a partnership has two or more individuals together as co-owners. In both of these forms of organization, the owners are individually liable for the debts of the business. A corporation is a business owned by stockholders, who generally do not have a part in the day-to-day operations of the business. The stockholders of a corporation are not legally liable for the debts of the business and it is easier to sell out of a corporation than a proprietorship or partnership. Corporations can raise capital easier than proprietorships and partnerships. Corporations also have the advantage of continuity of existence.

Diff: 2

Objective: L.O. 1-5

14) Match each of the following terms with the appropriate definition. Use each term only once.

A. Sole proprietorship

B. Partnership

C. Corporation

D. For-profit company

E. Not-for-profit company

\_\_\_\_\_\_\_\_ 1. A company with the goal of maximizing the owners' wealth

\_\_\_\_\_\_\_\_ 2. An organization that exists to provide goods and services to a target group at a reduced cost or no cost

\_\_\_\_\_\_\_\_ 3. A company owned by two or more individuals

\_\_\_\_\_\_\_\_ 4. This type of organization is taxed twice; first as a business and second when shareholders receive dividends

\_\_\_\_\_\_\_\_ 5. A company with one owner

Answer: D, E, B, C, A

Diff: 2

Objective: L.O. 1-5

Learning Objective 1.6 Questions

1) Kristine Parsons owns 2,000 shares of $1.00 par value capital stock of Garments 4 You. Kristine sold 100 of these shares to Beverly Plito for $200. The effect of this transaction on the accounts of Garments 4 You would be to

A) increase the capital stock account by $1,800 and increase the cash account by $1,800.

B) increase the capital stock account by $200, increase the paid-in capital in excess of par account by $2,000, and increase the cash account by $1,800.

C) decrease the capital stock account by $1,800 and increase the paid-in capital in excess of par account by $1,800.

D) increase the capital stock account by $1,800 and decrease the paid-in capital in excess of par account by $1,800.

E) There is no effect from this transaction on the accounts of Garments 4 You.

Answer: E

Diff: 2

Objective: L.O. 1-6

2) Wendy Walia owns 500 shares of Rhodes Water Company. The capital stock of Rhodes Water Company has a par value of $3 per share. Wendy Walia sells her 500 shares of Rhodes Water stock to Steve Matelski for $10 per share. The effect of this transaction on Rhodes Water Company would be to

A) increase the cash account by $5,000 and increase the capital stock account by $5,000.

B) increase the cash account by $5,000, increase the capital stock account by $1,500, and increase the paid-in capital in excess of par account by $3,500.

C) increase the cash account by $5,000 and decrease the capital stock account by $5,000.

D) increase the cash account by $5,000, decrease the capital stock account by $1,500, and decrease the paid-in capital in excess of par account by $3,500.

E) Rhodes Water Company would not record this transaction but would note the change in ownership.

Answer: E

Diff: 2

Objective: L.O. 1-6

3) Michael Hudson owns 400 shares of Surefoot Enterprises. The capital stock of Surefoot Enterprises has a par value of $8 per share. Michael Hudson sells his 400 shares of Surefoot Enterprises stock to Brian Haas for $15 per share. The effect of this transaction on Surefoot Enterprises, would be to

A) increase the cash account by $6,000 and increase the capital stock account by $6,000.

B) increase the cash account by $6,000 and decrease the capital stock account by $6,000.

C) increase the cash account by $6,000, increase the capital stock account by $3,200, and increase the paid-in capital in excess of par account by $2,800.

D) Surefoot Enterprises would not record this transaction but would note the change in ownership.

E) Surefoot Enterprises records this transaction but would not note the change in ownership.

Answer: D

Diff: 2

Objective: L.O. 1-6

4) Firelog Company began business on July 1, 20X8, by selling 1,000 shares of $1 par value capital stock at $20 per share. The effect of this transaction on Firelog Company would be to

A) increase the capital stock at par account by $20,000 and increase the cash account by $20,000.

B) increase the capital stock at par by $20,000 and decrease the cash account by $20,000.

C) decrease the capital stock at par by $20,000 and increase the cash account by $20,000.

D) increase the capital stock at par by $1,000, increase the paid-in capital in excess of par account by $19,000, and increase the cash account by $20,000.

E) decrease the capital stock at par by $1,000, decrease the paid-in capital in excess of par account by $19,000, and increase the cash account by $20,000.

Answer: D

Diff: 2

Objective: L.O. 1-6

5) Passport Global sold 250 shares of $4.00 par value capital stock in exchange for equipment worth $3,000. The effect of this transaction on Passport Global would be to

A) increase the equipment account by $1,000 and increase the capital at par by $1,000.

B) increase the equipment account by $3,000 and increase the capital at par by $3,000.

C) increase the equipment account by $3,000, increase the capital stock at par by $1,000, and increase the paid-in capital in excess of par account by $2,000.

D) increase the equipment account by $3,000 and decrease the capital stock at par by $3,000.

E) increase the equipment account by $3,000, decrease the capital stock at par by $1,000, and decrease the paid-in capital in excess of par account by $2,000.

Answer: C

Diff: 2

Objective: L.O. 1-6

6) Halo Corporation repaid an $8,000 note payable by issuing 500 shares of its $4.00 par value capital stock. The effect of this transaction on Halo Corporation would be to

A) increase the capital stock at par by $8,000 and decrease the notes payable account by $8,000.

B) increase the capital stock at par by $2,000 and decrease the notes payable account by $2,000.

C) increase the capital stock at par by $2,000, increase the paid-in capital in excess of par account by $6,000, and decrease the notes payable account by $8,000.

D) increase the capital stock at par by $2,000, decrease the paid-in capital in excess of par account by $6,000, and decrease the notes payable account by $8,000.

E) increase the capital stock at par by $2,000, decrease the cash account by $6,000, and decrease the notes payable account by $8,000.

Answer: C

Diff: 2

Objective: L.O. 1-6

7) Pandey Company's capital stock is currently selling for $25 per share. Pandey Company has the following accounts included within the owners' equity section of the balance sheet:

Capital stock, $1.00 par value, 10,000 shares issued $ 10,000

Additional paid-in capital $ 60,000

Assuming that the only transaction affecting these accounts was the sale of the company's capital stock, Pandey Company originally sold its capital stock for

A) $ 1.00 per share.

B) $ 7.00 per share.

C) $6.00 per share.

D) $10.00 per share.

E) The selling price of the capital stock cannot be determined from the information given.

Answer: B

Diff: 2

Objective: L.O. 1-6

8) Postal Manufacturing began business on July 1, 20X5, by selling 1,000 shares of $10 par value capital stock at $30 per share. The effect of this transaction on Postal Manufacturing would be to

A) increase the capital stock at par by $10,000, increase the paid-in capital in excess of par account by $20,000, and increase the cash account by $30,000.

B) decrease the capital stock at par by $30,000 and increase the cash account by $30,000.

C) increase the capital stock at par by $30,000 and increase the cash account by $30,000.

D) decrease the capital stock at par by $10,000, decrease the paid-in capital in excess of par account by $20,000, and increase the cash account by $30,000.

E) increase paid-in capital in excess of par account by $30,000 and increase the cash account by $30,000.

Answer: A

Diff: 2

Objective: L.O. 1-6

9) When stock is sold, the difference between the total amount the company receives and the par value is called

A) stated value.

B) par value.

C) additional paid-in capital.

D) stockholders' equity value.

E) common stock.

Answer: C

Diff: 2

Objective: L.O. 1-6

10) The two equity accounts that Total Paid-in Capital is split between are

A) capital stock at par and owners' equity.

B) capital stock at par and paid-in capital in excess of par.

C) capital stock at par and stockholders' equity.

D) paid-in capital in excess of par and owners' equity.

E) paid-in capital in excess of par and stockholders' equity.

Answer: B

Diff: 2

Objective: L.O. 1-6

11) Common stockholders

A) upon dissolution are paid the same amount as all creditors.

B) must purchase all shares directly from the issuing organization.

C) purchase stock certificates at par value.

D) have a claim on whatever is left over after all other claimants have been paid upon liquidation.

E) are also members of the New York Stock Exchange after the purchase of the stock.

Answer: D

Diff: 2

Objective: L.O. 1-6

12) The board of directors' duty is to manage a company.

Answer: FALSE

Diff: 2

Objective: L.O. 1-6

13) Typically, a company sells its stock at par value.

Answer: FALSE

Diff: 2

Objective: L.O. 1-6

14) Regardless of the type of corporation, companies generally account for assets and liabilities similarly.

Answer: TRUE

Diff: 2

Objective: L.O. 1-6

15) Below are owners' equity accounts for three different forms of business entities. Identify which form of business entity each set of owners' equity accounts represents and explain how you arrived at your decision.

**Business entity #1**

Sara Kromar, capital $100,000

Daniel Tondra, capital 15,000

Ann Pamer, capital 90,000

Kathy Brenan, capital 110,000

Total capital $315,000

**Business entity #2**

Stockholders' equity:

Paid-in capital:

Capital stock, 25,000 shares issued at par value of $5 per share $125,000

Paid-in capital in excess of par value 250,000

Total paid-in capital $375,000

**Business entity #3**

Mary Housel, capital $100,000

Answer: Business entity #1 is a partnership since the capital accounts show straight forward records of the capital invested by each owner. These capital accounts are similar to a sole proprietorship except that a partnership has more than one owner account.

Business entity #2 is a corporation since the capital account is labeled stockholders' equity. In addition, other typical corporation entity accounts used that are also shown in this example are paid-in capital, capital stock, paid-in capital in excess of par, and total paid-in capital.

Business entity #3 is a sole proprietorship since it has an amount invested by a single owner.

Diff: 2

Objective: L.O. 1-6

Learning Objective 1.7 Questions

1) The principal task of the FASB is to

A) be a link between the business community and the Securities and Exchange Commission (SEC).

B) establish GAAP in the United States.

C) audit each public company's financial statements and records.

D) act as a counsel and advocate for business in its dealings with the government, particularly, but not solely, to the SEC.

E) review financial statements, so as to ensure adherence to GAAP.

Answer: B

Diff: 1

Objective: L.O. 1-7

2) With respect to the role of the government in establishing accounting standards in the United States, which of the following statements is incorrect?

A) Most accounting reporting requirements are determined by the FASB, which is a non-government institution.

B) The SEC, and not the FASB, has the ultimate legal authority over most financial reporting to investors.

C) The FASB can act independently of the SEC and does not need the SEC's support in establishing accounting standards.

D) The SEC, which is an agency of the federal government, is empowered to ensure full and fair disclosures by corporations.

E) The SEC is allowed to take an active role in establishing accounting standards.

Answer: C

Diff: 2

Objective: L.O. 1-7

3) The hierarchy (1 is top) of U.S. accounting rule-making responsibility is

A) 1. congress, 2. AICPA, 3. FASB.

B) 1. SEC, 2. IASB, 3. FASB.

C) 1. FASB, 2. IASB, 3. AICPA.

D) 1. congress, 2. SEC, 3. FASB.

E) 1. PCAOB, 2. FASB, 3. IASB.

Answer: D

Diff: 2

Objective: L.O. 1-7

4) International Financial Reporting Standards are

A) used by all European Union countries.

B) never used by corporations operating in the United States.

C) identical to Generally Accepted Accounting Principles.

D) guidelines used by corporations to determine a company's fair value upon cessation.

E) drastically different from Generally Accepted Accounting Principles.

Answer: A

Diff: 2

Objective: L.O. 1-7

5) The Financial Accounting Standards Codification

A) classifies U.S. GAAP to make it easy to research financial reporting issues.

B) classifies U.S. tax laws to make it easy to research U.S. tax laws.

C) classifies International Financial Reporting Standards to make it easy to research reporting issues.

D) classifies international tax laws to make it easy to research international tax laws.

E) classifies financial statements by type of organization and structure.

Answer: A

Diff: 2

Objective: L.O. 1-7

6) The U.S. Congress has charged the SEC with ultimate responsibility for specifying GAAP for publicly traded companies.

Answer: TRUE

Diff: 1

Objective: L.O. 1-7

Learning Objective 1.8 Questions

1) An auditor's opinion is not

A) a report describing the auditor's examination of transactions and financial statements.

B) included in the financial statements in the annual report issued by the corporation.

C) another name for independent opinion.

D) certified by the Securities Exchange Commission.

E) a third party review.

Answer: D

Diff: 1

Objective: L.O. 1-8

2) The auditor's opinion includes all except which of the following statements?

A) The financial statements are in conformity with generally accepted accounting principles.

B) The financial statements are the responsibility of the company's management.

C) The audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements.

D) The auditor's responsibility is to express an opinion on the financial statements.

E) The financial statements are free of any and all misstatements.

Answer: E

Diff: 2

Objective: L.O. 1-8

3) Public accounting is

A) the field of accounting where accountants work for businesses, government agencies, or other nonprofit organizations.

B) the field of accounting where services are offered to the general public on a fee basis.

C) a field of accounting where no audits occur.

D) the field that provides management with internal company reports.

E) unregulated.

Answer: B

Diff: 1

Objective: L.O. 1-8

4) Generally accepted accounting principles

A) are advisory guidelines for management.

B) are only applicable to balance sheets.

C) are to be followed in the preparation of financial statements.

D) can never be deviated from.

E) are uniform world-wide.

Answer: C

Diff: 2

Objective: L.O. 1-8

5) The accuracy and truthfulness of the financial statements is the responsibility of the

A) external auditors.

B) stockholders.

C) management.

D) staff accountants.

E) external auditors and the staff accountants.

Answer: C

Diff: 2

Objective: L.O. 1-8

6) To ensure proper application of a CPA's technical knowledge, the Public Company Accounting Oversight Board issues:

A) Generally Accepted Accounting Principles.

B) Statements of Financial Accounting Standards.

C) Accounting Standards Updates.

D) Generally Accepted Auditing Standards.

E) Sarbanes-Oxley Acts for Accounting.

Answer: D

Diff: 1

Objective: L.O. 1-8

7) The Sarbanes-Oxley Act was passed in 2002 to regulate the accounting profession. Although the act encompasses many aspects, what is one of the parts of the act?

A) Requires rotation every ten years of the lead audit or coordinating partner and the reviewing partner on an audit

B) Established the Public Company Accounting Oversight Board

C) Requires all accounting firms to register with the SEC

D) Prohibits public accounting firms from auditing SEC regulated companies

E) Excludes certain industries from conducting business with public accounting firms

Answer: B

Diff: 1

Objective: L.O. 1-8

8) Which of the following international public accounting firms is not considered one of the four largest?

A) Deloitte Touche Tohmatsu

B) Ernst & Young

C) KPMG

D) PwC

E) Grant Thornton

Answer: E

Diff: 1

Objective: L.O. 1-8

9) The auditor's opinion is also called an independent opinion.

Answer: TRUE

Diff: 1

Objective: L.O. 1-8

10) The auditor's opinion is included with the annual report issued by the corporation.

Answer: TRUE

Diff: 1

Objective: L.O. 1-8

11) An audit is an examination of transactions and financial statements.

Answer: TRUE

Diff: 2

Objective: L.O. 1-8

12) Public accountants are those whose services are offered to the general public on a fee basis.

Answer: TRUE

Diff: 1

Objective: L.O. 1-8

13) The American Institute of Certified Public Accountants prepares and grades a CPA exam on a national basis.

Answer: TRUE

Diff: 1

Objective: L.O. 1-8

14) The American Institute of Certified Public Accountants is responsible for establishing GAAP in the United States

Answer: FALSE

Diff: 1

Objective: L.O. 1-8

15) The U.S. Congress has charged the Public Company Accounting Oversight Board with the ultimate responsibility for developing generally accepted accounting principles.

Answer: FALSE

Diff: 2

Objective: L.O. 1-8

Learning Objective 1.9 Questions

1) Public accountants follow the code of ethics for professional conduct established by the

A) Sarbanes-Oxley Act.

B) Securities and Exchange Commission.

C) Financial Accounting Standards Board.

D) Congress of the United States.

E) American Institute of Certified Public Accountants.

Answer: E

Diff: 1

Objective: L.O. 1-9

2) The AICPA Code of Professional Ethics is especially concerned with integrity and independence.

Answer: TRUE

Diff: 2

Objective: L.O. 1-9

3) How do generally accepted accounting principles present an ethical issue in financial accounting?

Answer: Because financial accounting provides information to external decision makers, the information must be relevant and reliable. Those individuals who generate the information must do so according to generally accepted accounting principles or the decision makers will misallocate resources. The preparers of information are typically different people than the investors/financial statement users. The preparers of information may have incentives to make the company's performance look better than it really is. Managers may be overly optimistic about company conditions because they are making the decisions and plans. Their bonuses and salaries may also be dependent on the reported net income figures.

Diff: 2

Objective: L.O. 1-9

Learning Objective 1.10 Questions

1) The regulatory body overseeing disclosures for governmental organizations is

A) Government Accounting Standards Board

B) Government Accounting Standards Commission

C) Governmental Financial Reporting Board

D) Governmental Financial Reporting Commission

E) Governmental Taxation Standards Board

Answer: A

Diff: 1

Objective: L.O. 1-10

2) Nonprofit organizations do not need to analyze financial statement information since their purpose is not to increase net income like profit-seeking organizations.

Answer: FALSE

Diff: 2

Objective: L.O. 1-10