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QUESTION 1

Hyde Corp. has three manufacturing divisions, each of which has been determined to be a reportable segment. In 1989, Clay division had sales of \$3,000,000, which was 25% of Hyde's total sales, and had operating costs of \$1,900,000, as reported to the CFO. In 1989, Hyde incurred operating costs of \$500,000 that were not directly traceable to any of the divisions. In addition, Hyde incurred corporate interest expense of \$300,000 in 1989. In reporting segment information, what amount should be shown as Clay's operating profit for 1989?

- A. \$875,000
- B. \$900,000
- C. \$975,000
- D. \$1,100,000

Correct Answer: D

Choice "d" is correct. \$1,100,000 operating profit for clay.

Rule: Operating profit by segments is based on the measure of profit reported to the "chief operating decision maker."

Allocations for general operating costs and interest, etc., should not be made solely for purposes of segment disclosures.

Sales	\$3,000,000
Less operating costs	<u>(1,900,000)</u>
Sub total	<u>\$1,100,000</u>

QUESTION 2

FASB Interpretations of Statements of Financial Accounting Standards have the same authority as the FASB:

- A. Statements of Financial Accounting Concepts.
- B. Emerging Issues Task Force Consensus.
- C. Technical Bulletins.
- D. Statements of Financial Accounting Standards.

Correct Answer: D

Choice "d" is correct. FASB interpretations of the "statements of financial accounting standards" (SFAS) have the same authority as the FASB statements of financial accounting standards (SFAS), which by themselves determine GAAP. Choice "a" is incorrect. Statements of financial accounting concepts (FAC's) have much less authority (fifth floor) and



do not by themselves determine GAAP as is the case with SFASs and interpretations of SFASs. Choice "b" is incorrect. Emerging issues task force (EITF) consensus is in the nature of a "third floor" authority. The EITF was established in 1984 to aid the FASB in identifying and implementing emerging issues before they become widespread and ultimately require action by the FASB. After discussing the issues and the relevant accounting pronouncements, the group can sometimes reach a consensus on an issue, in which case no action by the FASB is usually needed. Choice "c" is incorrect. Technical bulletins of the FASB (second floor) do not by themselves determine GAAP.

QUESTION 3

The summary of significant accounting policies should disclose the:

- A. Maturity dates of noncurrent debts.
- B. Terms for convertible debt to be exchanged for common stock.
- C. Concentration of credit risk of all financial instruments by geographical region.
- D. Criteria for determining which investments are treated as cash equivalents.

Correct Answer: D

Choice "d" is correct. The criteria for determining which investments are treated as cash equivalents would be part of the summary of significant accounting policies. Choice "a" is incorrect. The maturity dates of noncurrent debts are required disclosures, but are not a part of the summary of significant accounting policies. Choice "b" is incorrect. The terms for convertible debt to be exchanged for common stock are not accounting policies; they would be disclosed separately. Choice "c" is incorrect. The concentration of credit risk of all financial instruments by geographic region may be a required segment disclosure, especially for financial institutions. However, it would not be a part of the summary of significant accounting policies.

QUESTION 4

In Yew Co.'s 1992 annual report, Yew described its social awareness expenditures during the year as follows:

"The Company contributed \$250,000 in cash to youth and educational programs. The Company also gave \$140,000 to health and human-service organizations, of which \$80,000 was contributed by employees through payroll deductions. In addition, consistent with the Company's commitment to the environment, the Company spent \$100,000 to redesign product packaging." What amount of the above should be included in Yew's income statement as charitable contributions expense?

- A. \$310,000
- B. \$390,000
- C. \$410,000
- D. \$490,000

Correct Answer: A

Choice "a" is correct. Charitable contributions include amounts the company gave to recognized charities. This includes:



Youth and education programs	\$ 250,000
Health (\$140,000 - \$80,000)	60,000
Total	<u>\$ 310,000</u>

Note: Of the \$140,000, employees gave \$80,000, and the company \$60,000. Redesigning packaging is not a contribution to a charity.

Choice "b" is incorrect. The company gave only \$60,000 of the \$140,000. Employees gave \$80,000.

Choice "c" is incorrect. Redesigning packaging is not a contribution to a charity.

Choice "d" is incorrect. The company gave only \$60,000 of the \$140,000. Employees gave \$80,000.

Redesigning packaging is not a contribution to a charity.

QUESTION 5

If a company is not presenting comparative financial statements, the correction of an error in the financial statements of a prior period should be reported, net of applicable income taxes, in the current:

- A. Retained earnings statement after net income but before dividends.
- B. Retained earnings statement as an adjustment of the opening balance.
- C. Income statement after income from continuing operations and before extraordinary items.
- D. Income statement after income from continuing operations and after extraordinary items.

Correct Answer: B

Choice "b" is correct. The correction of an error in the financial statements of a prior period should be reported, net of tax, in the current statement of retained earnings as an adjustment of the opening balance.

Choice "a" is incorrect. The adjustment is before net income, not after net income.

Choices "c" and "d" are incorrect. Corrections of errors of prior periods go to retained earnings and do not affect the income statement.

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