

## Financial Reporting and Analysis – Topic Test 5

1. Mozart Technologies has a long-term asset on its balance sheet. The carrying value of the asset is \$50,000 and the tax base of the asset is \$30,000. The tax rate is 40%. What is the deferred tax asset/liability created by the asset on the balance sheet of the company?
  - a) Deferred tax asset of \$20,000
  - b) Deferred tax asset of \$8,000
  - c) Deferred tax liability of \$8,000
  
2. Which of the following criteria is least likely to be a criterion for the recognition of temporary deferred tax assets related to subsidiaries, branches, and associates?
  - a) Sufficient taxable profits exist against which the temporary difference can be used
  - b) The temporary difference will not reverse in the future
  - c) The temporary difference will reverse in the future
  
3. A company had total taxes of \$25,450 in 2016 as income tax expense in the income statement and \$2,550 were the deferred tax liabilities arising in that year. What is the total taxes paid by the company assuming that there had been no changes in the taxes payable?
  - a) \$22,900
  - b) \$25,450
  - c) \$28,000
  
4. Which of the following items is most likely to increase the total value of a firm?
  - a) Deferred tax assets that are not expected to reverse in the future
  - b) Deferred tax liabilities that are not expected to reverse in the future
  - c) Increase in valuation allowance
  
5. A company has 150,000 common shares at the beginning of the year. It pays 20% cash dividend on 1st April to each common shareholder. It also issues 30,000 additional shares on 1st October. What is the number of weighted average share for the company for the year?
  - a) 135,000
  - b) 155,000
  - c) 157,500

6. A company did a reverse stock split of 5:2 during a year. Which of the following statements is least likely to be accurate for the company for the year?
- a) Total outstanding shares will decrease
  - b) Earnings per share will increase
  - c) Earning yield will increase
7. Bosch Inc. had a net income of \$250,000 for the year 2015. It paid total dividends worth \$50,000 for the year. 40% of the total dividends were preferred dividends. It also had 1,000 convertible bonds with each bond having a face value of \$1,000 and a coupon of 10%. Each convertible bond can be converted into 25 common shares. The company had 100,000 common shares outstanding during the year. Compute the diluted EPS for the company for 2015 assuming the tax rate to be 40%.
- a) \$2.08
  - b) \$2.30
  - c) \$2.32
8. Dope Inc. sells its products on credit and the payments are expected to be received over an extended period of time. The collectability of revenue cannot be reasonably estimated. It sells products for \$500 million in 2015 and the cost of goods sold for those products was \$400 million. In the first year, it receives \$200 million from the customers in cash. How much profit should be recognized by the company in the first year?
- a) Zero
  - b) \$40 million
  - c) \$50 million
9. A company has entered into a long-term contract. The outcome of the project cannot be reliably estimated. The company is using IFRS. The total estimated cost of the project is \$300 million and the company will receive \$400 million for it. The company expends \$150 million on the project in the first year. How much revenue should be recognized by the company in the first year in the income statement due to this project?
- a) Zero
  - b) \$150 million
  - c) \$200 million

10. The following financial data has been extracted from the financial statements of a company:

Revenues	\$375 million
Ordinary expenses	\$200 million
Other income	\$75 million
Other expenses	\$60 million
Gain on sale of land	\$12 million
Loss on sale of a machine	\$4 million

What is the net income for the company for the given year?

- a) \$175 million
  - b) \$190 million
  - c) \$198 million
11. What should be the treatment of bad debt expense and warranty expense on the income statement?
- a) Bad debt expense should be recognized in the period of sale and warranty expense should be recognized when the expense is actually incurred
  - b) Bad debt expense should be recognized when the firm is actually not able to recover it and warranty expense should be recognized in the period of sale
  - c) Both bad debt expense and warranty expense should be recognized in the period of sale
12. "The income statement may be presented as a separate statement followed by a statement of comprehensive income that begins with the profit or loss from the income statement or as a section of a single statement of comprehensive income."  
The above is true for which of the following accounting standards?
- a) U.S. GAAP
  - b) IFRS
  - c) Both U.S. GAAP and IFRS
13. Apex Inc. has \$15 million as restructuring costs in 2015. The tax rate of the company is 40%. How should this amount be recognized in the income statement?
- a) \$15 million expense and is reported part of continuing operation
  - b) \$9 million expense and is reported after income from continuing operation
  - c) \$15 million expense and is reported after income from continuing operation

14. In which of the following accounting standard, a firm will report a higher gross profit in the year when the inventory is written back up?
- a) U.S. GAAP
  - b) IFRS
  - c) Same gross profit under both U.S. GAAP and IFRS
15. Which of the following elements of balance sheet tells about the operating activities of a firm?
- a) Current assets
  - b) Non-current assets
  - c) Non-current liabilities

16. Liquidity ratio and solvency ratio of three firms are given below:

	Firm A	Firm B	Firm C
Liquidity ratio	1.20	0.95	1.45
Solvency ratio	0.80	1.20	1.05

Identify the most liquid and most solvent firm out of these three firms.

- a) Most liquid: Firm C; Most Solvent: Firm B
- b) Most liquid: Firm B; Most Solvent: Firm A
- c) Most liquid: Firm C; Most Solvent: Firm A

17. The common size balance sheets of three firms are given below:

	Firm A	Firm B	Firm C
Cash	3%	5%	7%
Accounts receivable	12%	8%	7%
Inventory	14%	18%	13%
Current assets	29%	31%	27%
Plant and equipment	71%	64%	65%
Goodwill	0%	5%	8%
Total assets	100%	100%	100%
Current liabilities	22%	23%	21%
Long-term debt	30%	44%	24%
Total liabilities	52%	67%	45%
Equity	48%	33%	55%
Total liabilities and equity	100%	100%	100%

Which of the firms has the best quick ratio?

- a) Firm A
  - b) Firm B
  - c) Firm C
18. Three companies have the identical revenue in the recently completed year. The revenue of company A grows at a CAGR (compounded annual growth rate) of 12%. The revenue of company B grows at a CAGR of 10% and the revenue of company C grows at a CAGR of 15% for next years. The net profit margins for three companies in the fifth year are 10%, 12%, and 9% respectively. Which of the following companies would have the maximum net income in the fifth year?
- a) Company A
  - b) Company B
  - c) Company C
19. A company decides to change its depreciation policy from a straight line to double declining balance method. Which of the following items would see the maximum reduction in its value?
- a) Gross profit
  - b) Operating income
  - c) Net income

20. An analyst extracts the following data from the financial statements of a company:  
Earnings for the year ended 31 December 2015: \$18,900  
Earnings for the six months ended 30 June 2015: \$8,400  
Earnings for the six months ended 30 June 2016: \$11,000  
What is the company's trailing 12 months earnings for the period ended 30 June 2016?
- a) \$18,900
  - b) \$19,400
  - c) \$21,500
21. For a company, receivables are growing at a faster rate than the revenue. What would be its most likely impact on the receivables turnover ratio?
- a) Increase
  - b) Decrease
  - c) No impact
22. In a horizontal common-size balance sheet, the inventory is shown as a percentage of
- a) Total assets
  - b) Revenue
  - c) Base year value of inventory
23. What will the most likely impact of LIFO liquidation on the gross profit of the company using LIFO as the inventory cost flow method? Assume that the inventory prices have been decreasing over the years.
- a) Increase in gross profit
  - b) No change in gross profit
  - c) Decrease in gross profit
24. Grover Inc. is following U.S. GAAP. The carrying value of the inventory on the balance sheet is EUR 25,000. The current replacement cost for the inventory equals EUR 24,000. The estimated selling price for the inventory is EUR 25,500 and the estimated selling cost is EUR 300. The normal profit margin on the inventory is \$600. How much inventory write down will be recognized by the company?
- a) Zero
  - b) EUR 400
  - c) EUR 1,000

25. Which of the following is least likely to increase because of the reversal of inventory write-down under IFRS?
- a) Working capital
  - b) Days of inventory on hand
  - c) Debt to equity ratio
26. Which of the following is least likely to be an indication of the high growth of finished good inventory growth relative to the sales growth?
- a) Possibility of firm carrying obsolete inventory
  - b) Inefficient use of working capital
  - c) Increase in demand of product
27. The following data have been extracted from the financial statements and footnotes to financial statements for a company:

	2015	2014
Ending inventory (in units)	810	805
Ending inventory (in thousands of dollars)	34.04	34.38

- The firm is following U.S. GAAP and LIFO as its inventory cost flow method and sells only one kind of product. Which of the following statements is least likely to be accurate about the company?
- a) The prices of inventory have decreased from 2014 to 2015
  - b) Inventory liquidation has occurred during 2015
  - c) There has been an inventory write-down in 2015
28. A company borrowed \$200,000 at an interest rate of 8 percent per year on January 1, 2012, to finance the construction of a factory that will have a useful life of 30 years. The construction is completed in 3 years. During those three years, the company also earned \$5,000 by temporarily investing the loan proceeds. What is the amount of interest that will be capitalized under IFRS? The maturity of the loan is 5 years and the face value is \$200,000.
- a) \$80,000
  - b) \$32,000
  - c) \$27,000

29. Company A acquired 80% of the another company B. There was an unidentifiable intangible asset worth \$10,000 on the balance sheet of the company B before the acquisition. What would be the treatment of that unidentifiable intangible asset on the balance sheet of A post-acquisition?
- a) Recognized in the goodwill
  - b) Recognized separately as an unidentifiable intangible asset
  - c) Recognized separately as an identifiable intangible asset
30. The cash inflows from investing activities for a firm are \$20,400 during a year and the cash outflows from operations are \$8,700. The firm has expensed as an asset worth \$5,000 during the year. You, as an analyst, find that classification inappropriate. The asset should have been capitalized on the balance sheet as it would be used for a period of five years. What would be the CFO and CFI after making an adjustment for that asset? Ignore the impact of taxes.
- a) Cash inflow from investing activities: \$15,400; Cash outflow from operating activities: \$13,700
  - b) Cash inflow from investing activities: \$25,400; Cash outflow from operating activities: \$3,700
  - c) Cash inflow from investing activities: \$15,400; Cash outflow from operating activities: \$3,700
31. An asset has been purchased and capitalized by a company. If the asset had been expensed off instead of capitalized what would have been the impact on the cash flow items in the subsequent years from the year of purchase?
- a) Lower CFO, Higher CFI
  - b) Higher CFO, Lower CFI
  - c) No impact
32. A company purchased a machine for \$33,000. The salvage value of the machine is 5 years and its salvage value is \$3,000. What would be the depreciation expense due to this machine in the second year of operation if the company is using double declining balance method for depreciation?
- a) \$7,200
  - b) \$7,920
  - c) \$8,400

33. What would be the impact on the cash flow from operations if the company uses double declining balance depreciation method instead of straight line depreciation method?
- a) Increase in cash flow from operation in earlier years and decrease in later years
  - b) Decrease in cash flow from operation in earlier years and increase in later years
  - c) No impact
34. The information about the legal proceedings against a company are most likely to be present in which of the following statements?
- a) Financial statement notes and supplementary schedules
  - b) Management discussion and analysis
  - c) Audit statements
35. The information about the election of board members is most likely to found in
- a) Proxy statements
  - b) Corporate reports and press releases
  - c) Trade journals
36. Timetable and budgeted resources of completion are the output of which phase of the financial statement analysis framework?
- a) Articulate the purpose and context of analysis
  - b) Develop and communicate conclusions and recommendations
  - c) Follow-up
37. Depreciation and amortization are part of which of the following elements of the financial statements?
- a) Assets
  - b) Liabilities
  - c) Expense

38. A company earns a net income of \$12,000 during a year and its accumulated retained earnings decreases by \$1,500 during the year. The company also repurchased stocks worth \$4,000 during the year by borrowing the amount. How much dividends is paid by the company for the year?
- a) \$9,500
  - b) \$10,500
  - c) \$13,500
39. In a general ledger, the data is sorted by
- a) Time
  - b) Account
  - c) Amount
40. Which of the following forms is filed to report employee stock purchase, savings, and similar plans?
- a) Form 3, 4, and 5
  - b) Form 144
  - c) Form 11-K
41. Which of the following differences between IFRS and U.S. GAAP frameworks is least likely to be correct?
- a) The FASB framework defines an asset as "a future economic benefit" rather than the "resource" from which future economic benefits are expected to flow to the entity as in the IASB framework
  - b) The IASB framework does not discuss the term "probable" in its recognition criteria
  - c) The FASB framework prohibits revaluations except for certain categories of financial instruments, which have to be carried at fair value
42. The U.S. GAAP accounting standards are based on which of the following approaches to the standard setting?
- a) Principles-based approach
  - b) Rules-based approach
  - c) Objectives-oriented approach

43. Which of the following is required to properly assess a company's past performance?
- a) High financial reporting quality
  - b) High earnings quality
  - c) Both high financial reporting quality and high earnings quality
44. Assume that the same financial statements are being used for the reporting and the taxation purpose. If the accounting treatment is aggressive in nature then it will lead to
- a) Higher tax expense in the current period
  - b) Lower tax expense in the current period
  - c) Same tax expense in the current period
45. More than 5,000 employees have been fired from Wells Fargo because they were involved in the cheating and creating fictitious accounts for their customers. Which element of the fraud triangle is most likely to be responsible for such a higher amount of employees involved in fraud?
- a) Incentives and pressures
  - b) Opportunities
  - c) Attitudes and rationalizations
46. A company is using LIFO as inventory cost flow method. The current ratio of the company decreases after making an adjustment to it to make it comparable with a firm that uses FIFO as the inventory cost flow method. Which of the following statements is least likely to be accurate?
- a) LIFO reserve is positive
  - b) LIFO reserve is negative
  - c) The prices of the inventory have been decreasing over the years
47. Rexona Inc. had an average receivables collection period of 22 days in 2015. The company wants to decrease the average receivables collection period to 18 days in 2016. The credit sales were \$100 million in 2014 and are expected to be \$120 million in 2016. What should be the change in the account receivable balance from 2015 to 2016 that must occur to achieve the desired average receivables collection period? For calculation purpose, use accounts receivables at the end of the year rather than average accounts receivables.
- a) -\$109,589
  - b) -\$125,758
  - c) \$514,382

48. For which of the following industries, the comparison of price to tangible book value ratio of a company with the industry makes the most sense?
- a) Information Technology
  - b) Automobile
  - c) Biotechnology
49. The interest expense for a bond is \$8.7 million and the annual coupon paid for the bond is \$9.0 million. The bond is most likely issued at
- a) Par
  - b) Premium
  - c) Discount
50. Which of the following kinds of the bond will have a higher amount of cash outflow from the financing activities at the maturity date?
- a) Bond issued at a premium
  - b) Bond issued at a discount
  - c) Both will have the same amount of cash outflow from the financing activities
51. Which of the following is least likely to be the different for the finance lease and the operating lease in the first year of the lease?
- a) Operating income
  - b) Noncurrent liabilities
  - c) Total cash flows
52. For which of the following types of lease, the company will have a better quick ratio?
- a) Operating lease
  - b) Finance lease
  - c) Both will have the same quick ratio
53. TTG Inc. is a lessor that sells its machines and provides financing to the lessee for buying the machines. It has provided financing for some of its machines to one company. The lease is for four years for an annual payment of \$10,000. The lease rate is 10%. The lease is classified as a finance lease. The carrying value of the machines is \$30,000. What is the total income realized due to this in the income statement in the first year of the lease?
- a) \$3,169.87
  - b) \$4,868.52
  - c) \$6,830.13

54. Company A has a debt to equity ratio of 1.0 and Company B has a debt to capital ratio of 0.55. Company C has a debt to asset ratio of 0.55. Which of the following companies is most likely to have the weakest solvency among the three companies?
- a) Company A
  - b) Company B
  - c) Company C
55. Which of the following sections of the cash flow statements are always prepared under direct method?
- a) Cash flow from investing activities
  - b) Cash flow from financing activities
  - c) Cash flow from both investing and financing activities
56. There has been a conversion of a face value \$25 million convertible debt for \$25 million of common stock. Where will this transaction be reported in the cash flow statements?
- a) Reported as a \$25 million investing cash outflow and \$25 million of financing cash inflow
  - b) Reported as a \$25 million financing cash inflow and outflow
  - c) Reported as supplementary information to the cash flow statement
57. Which of the following is least likely to appear in the operating section of a cash flow statement under the indirect method?
- a) Depreciation
  - b) Gain on sale of assets
  - c) Cash paid for interest
58. What will be the impact of an increase in cash inflow due to investing activities on the free cash flow to firm and free cash flow to equity?
- a) No impact on FCFF, Increase in FCFE
  - b) No impact on FCFF and FCFE
  - c) Increase in FCFF and FCFE

59. The cash flows from operating activities for a firm in 2015 were \$35,000. It paid \$8,000 in taxes and \$5,000 in interest during the year. What is cash flow interest coverage ratio for the company for 2015?
- a) 9.6
  - b) 8.6
  - c) 8.0
60. The net PP&E for a company at the beginning and at the end of a year were \$270,000 and \$285,000 respectively. The company sold an asset for \$20,000 during the year for a loss of \$4,000. The depreciation for the company during the year was \$15,000. What is the total cash flow from investing activities for the company during the year?
- a) Cash outflow of \$14,000
  - b) Cash outflow of \$26,000
  - c) Cash outflow of \$34,000