

Financial Accounting Proficiency Sample Test

1. Fill out the tables on the next page based on the following information about ResellCo. You can rip out this page.

Beginning balance sheet

A	+dr	-cr	L	-dr	+cr
Cash	700		Accounts payable		112
Gross receivables	400		Accrued salaries		133
Allowance for bad debts		60	Deferred revenues		170
Tax refunds receivable	97		Deferred tax liabilities		88
Inventories	352		Interest payable		45
			Debt: Principal portion		400
Prepaid advertising	92		OE		
Property, plant, and equipment: Cost	800		Contributed capital		700
Accumulated depreciation		160	Retained earnings		773
			Treasury stock	200	

Ending balance sheet

A	+dr	-cr	L	-dr	+cr
Cash	768		Accounts payable		131
Gross receivables	500		Accrued salaries		157
Allowance for bad debts		78	Deferred revenues		190
Tax refunds receivable	102		Deferred tax liabilities		101
Inventories	411		Interest payable		54
			Debt: Principal portion		545
Prepaid advertising	147		OE		
Property, plant, and equipment: Cost	885		Contributed capital		678
Accumulated depreciation		191	Retained earnings		884
			Treasury stock	196	

Assume the following:

- There were no mergers, acquisitions, spin-offs, foreign exchange translations, non-cash acquisitions or non-cash sales of PP&E, or other comprehensive income.
- Dividends declared were paid instantly.
- Accounts payable were payable only to suppliers of inventory.
- There was no production and all costs except cost of buying inventory are period costs.
- Receivables written off during the period: \$14
- Cost (or gross book value) of PP&E sold: \$135
- Accumulated depreciation of PP&E sold: \$65
- Cash proceeds from sale of PP&E: \$104.
- The firm bought back \$31 of stock this year and kept it in its treasury. The firm also retired Treasury stock that had been repurchased for \$35 in prior years. The original price at which the repurchased stock had been issued in the past was \$22.

Enclose numbers to be subtracted in parentheses. If you don't write your answers here, you will get zero. You must also show your derivations on the following pages. Merely writing the equations without plugging the actual numbers will not get you any points.

Income statement for the year.

Sales	1013
COGS	(390)
Bad debt expense	?
Advertising expense	(85)
Salary expense	(146)
Depreciation expense	?
?	?
(This is not a subtotal.)	
Interest expense	(68)
Income before tax	= ?
Tax expense	(55)
Net income	= ?

Direct operating cash flows

Cash receipts from customers	?
Cash paid to suppliers	?
Cash paid for advertising	?
Cash paid for salaries	?
Cash paid for interest	?
Cash paid for taxes	?
Operating cash flow	=?

Indirect

cash-flow statement for the year.

Net income	?
Adjustments due to:	
Depreciation	?
Receivables	?
Deferred revenues	?
Allowance for bad debt	?
Inventories	?
Accounts payable	?
Prepaid advertising	?
Accrued salaries	?
Interest payable	?
?	?
Tax refunds	?
Deferred tax liabilities	?
Operating cash flow	=?
Capital expenditures	?
?	?
Investing cash flow	= ?
Debt issued	?
Stock buyback	(31)
Dividends paid	(51)
Financing cash flow	= ?
Net cash flow	= ?

- 1.1. (2 points) Bad debt expense _____
- 1.2. (4 points) Cash receipts from customers _____
- 1.3. (3 points) Cash paid to suppliers _____
- 1.4. (2 points) Cash paid for advertising _____
- 1.5. (2 points) Cash paid for salaries _____
- 1.6. (2 points) Cash paid for interest _____
- 1.7. (2 points) As an intermediate step compute current tax expense (You cannot assume a 40% tax rate.) _____

1.8. (2 points) Cash paid for taxes (You cannot assume a 40% tax rate.) _____

1.9. (2 points) Capital expenditures (Cash spent to buy PP&E) _____

1.10. (2 points) Missing item in the investing section of the cash-flow statement.

Title _____ Amount _____

1.11. (2 points) Depreciation expense _____

1.12. (2 points) Missing item on the income statement. (This is not a subtotal.)

Title _____ Amount _____

1.13. (1 point) Income before tax _____

1.14. (1 points) Net income _____

1.15. (2 points) Debt issued _____

1.16. (2 points) Adjustment for depreciation. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

1.17. (2 points) Adjustment for receivables. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

1.18. (2 points) Adjustment for deferred revenues. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

1.19. (2 points) Adjustment for allowance for bad debt. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

- 1.20. (2 points) Adjustment for inventories. Amount _____.
Adjustment for accounts payable. Amount _____.

Pick one of the statements below that best describes the reason for the combined effect of these adjustments.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

- 1.21. (2 points) Adjustment for prepaid advertising. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

- 1.22. (2 points) Adjustment for accrued salaries. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

- 1.23. (2 points) Adjustment for interest payable. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

- 1.24. (2 points) Missing adjustment on the indirect operating cash flow section

Title _____ Amount _____

Pick one of the statements below that best describes the reason for the adjustment.

- a. Operating cash inflows exceed revenues.
- b. Expenses exceed operating cash outflows.
- c. Losses that are not operating cash flow items.
- d. Revenues exceed operating cash inflows.
- e. Operating cash outflows exceed expenses.
- f. Gains that are not operating cash flow items.

- 1.25. (2 points) Adjustment for tax refunds receivable. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Tax paid exceeds the current tax expense.
- b. Tax paid is less than the current tax expense.
- c. Income tax expense exceeds the current tax expense because of a deferred tax expense.
- d. Income tax expense is less than the current tax expense because of a deferred tax benefit.

1.26. (2 points) Adjustment for deferred tax liabilities. Amount _____.

Pick one of the statements below that best describes the reason for the adjustment.

- a. Tax paid exceeds the current tax expense.
- b. Tax paid is less than the current tax expense.
- c. Income tax expense exceeds the current tax expense because of a deferred tax expense.
- d. Income tax expense is less than the current tax expense because of a deferred tax benefit.

1.27. (1 point) Operating cash flow _____.

Investing cash flow _____.

Financing cash flow _____.

1.28. (2 points) Net cash flow _____. Which account on the balance sheet should the net cash flow reconcile with? _____ Does it reconcile? Circle YES or NO.

1.29. (2 points) Explain changes in Treasury stock account by showing the causes of increases and decreases.

1.30. (2 points) Explain changes in retained earnings by showing the causes of increases and decreases.

2. MinorityInterest: Assume that PCo owns 90% of SCo. Assume that PCo had no other transactions. Beginning balance of minority interest on the consolidated balance sheet = \$100

SCo's income statement for the year

Sales revenue	100
Salary expense	(80)
Net income	=20

SCo's indirect cash-flow statement for the year

Net income	20
Adjustment for increase in receivables	(4)
Adjustment for increase in salary payable	3
Operating cash flow	=19
Purchase of PP&E	(7)
Investing cash flow	=(7)
Cash dividends paid	(10)
Financing cash flow	=(10)
Net cash flow	=2

- 2.1. (3 points) Consolidated income statement (You may not need all rows.)

- 2.2. (4 points) Consolidated indirect-cash flow statement with the operating, investing, and financing sections. You may not need all rows.

- 2.3. (3 points) Ending balance of minority interest on the consolidated balance sheet = _____ (If you don't write your answer in the space provided above AND SHOW YOUR COMPUTATIONS BELOW, you will get a zero.)

3. DealCo is a car dealership. It sells cars and provides a two-year warranty with each car sold. Assume the following:
- Assume that the firm had no assets, liabilities, or equity at the beginning of year 1. It bought and sold one car in year 1 and bought and sold another car in year 2, and so on.
 - The firm bought the car each year on credit and immediately repaid it from the cash it received from customers.
 - Ignore time value of money.
 - Selling price of a car: \$100
 - Selling price is received in full in cash at the time of sale.
 - Cost of the car excluding warranty cost: \$60
 - There are no other costs except warranties.
 - Actual warranty costs equal expected warranty costs and are paid in cash.
 - Expected warranty cost in a car's first year: \$10.
 - Expected warranty cost in a car's second year: \$20.
 - Tax rate: 40%.
 - Current tax expense is fully paid in cash in the year in which it is booked.
 - For financial and tax reporting, the firm recognizes the full selling price of \$100 as revenue in the year in which the car is sold.
 - For financial reporting, the firm expenses the full cost of \$60+\$10+\$20 in the year in which the car is sold. The \$60+\$10 is actually paid in the year of the sale, while the remaining \$20 is accrued as an expense in the year of the sale although the actual cash is paid for warranty repairs in the next year. The estimated payment of \$20 is shown as "accrued warranty costs" on the balance sheet.
 - For tax reporting, the firm is not allowed to accrue the warranty expense for the second year. Thus, for tax reporting, the allowable expenses are \$60+\$10 in the first year and \$20 in the second year. [This is not meant to be an accurate depiction of the tax code. This is only for illustration here.]

See the next page for questions. You can try journal entries, T-accounts, or equations on separate sheets of paper. We care only about the answers you write in the assigned spaces.

Fill in the tables below. Answers written elsewhere will be ignored.

3.1. (3 points) Income statement for year 1. Show numbers to be subtracted in parentheses.

	Y1
Sales	
Cost of goods sold	
Warranty expense	
Income before taxes	
Income tax expense	
Net income	

3.2. (3 points) Balance sheet at the end of year 1

A	+dr	-cr	L	-dr	+cr
			OE on B/S		

3.3. (3 points) Direct operating cash-flow statement for year 1. Show numbers to be subtracted in parentheses.

	Y1
Operating cash flow=	

3.4. (3 points) Indirect operating cash-flow statement for year 1

	Y1
Operating cash flow=	

Fill in the tables below. Answers written elsewhere will be ignored. Note that a car was bought and sold in year 1 as well as year 2.

3.5. (2 points) Income statement for year 2. Show numbers to be subtracted in parentheses.

	Y2
Sales	
Cost of goods sold	
Warranty expense	
Income before taxes	
Income tax expense	
Net income	

3.6. (2 points) Balance sheet at the end of year 2

A	+dr	-cr	L	-dr	+cr
			OE on B/S		

3.7. (1 points) Direct operating cash-flow statement for year 2. Show numbers to be subtracted in parentheses.

	Y2
Operating cash flow=	

3.8. (1 points) Indirect operating cash-flow statement for year 2

	Y2
Operating cash flow=	

4. StepUp’s beginning and ending balance sheets are given below. Assume a tax rate of 40%.

Beginning balance sheet

A	+dr	-cr	L	-dr	+cr
Available-for-sale securities: Cost	100		Deferred tax liability		12
Securities fair value adjustment	30		OE		
			Capital		100
			Accumulated other		18
			Comprehensive income		
			(Unrealized gains)		

- Securities with a cost of \$30 and a securities fair value adjustment of \$9 were sold for \$55 in cash. The current tax expense were paid in cash.
- The market value of remaining securities at the end of the year is \$105.

4.1. (4 points) Fill in the balance sheet at the end of the year.

A	+dr	-cr	L	-dr	+cr
Available-for-sale securities: Cost	?		Deferred tax liability		?
Securities fair value adjustment	?		OE		
			Capital		?
?		?	?		?
			Accumulated other		?
			Comprehensive income		
			(Unrealized gains)		

4.2. (3 points) Prepare an income statement for the year

Realized gain	?
Tax expense	?
Net income	= ?

4.3. (3 points) Prepare an indirect cash flow statement for the year. You may not need all rows.

Net income	?
Adjustments if any:	? ?
	? ?
Operating cash flow	= ?
? if any	?
Investing cash flow	= ?
? if any	
Financing cash flow	= ?
Net cash flow	= ?

4.4. (2 points) Do the changes in the deferred tax account on the balance sheet reconcile with adjustment for deferred taxes on the operating cash flow statement? Circle YES or NO.