

AICPA Released Questions from the 2022 Uniform CPA Exam - Released April 2022 -

FINANCIAL ACCOUNTING AND REPORTING



2022 AICPA Released Questions for FAR

The Key gives the correct letter answer for each question.

Key: A

The numbering system indicates the AICPA Blueprint Representative Task and Skill Level for each question.

FAR.CSO.20190701: FAR.002.001.000

FAR.SSO.20190701: Application:2

MULTIPLE CHOICE - MODERATE

It can be reasonably assumed that the FASB has made an amendment to generally accepted accounting principles when the FASB issues

- A. An exposure draft.
- B. A staff accounting bulletin.
- C. An accounting standards update.
- D. A statement on standards for attestation engagements.

Generally accepted accounting principles (GAAP) is developed by the Financial Accounting Standards Board (FASB), who is authorized to establish accounting standards by the Securities and Exchange Commission (SEC). The **FASB Accounting Standards Codification** (ASC) is the single source of authoritative GAAP for nongovernmental entities.

GAAP hierarchy consists of two levels:

- Authoritative (in ASC): **updated with Accounting Standards Updates** (ASUs), but which are not in themselves authoritative
- Nonauthoritative (not in ASC)

ASUs provide background information, update ASC, and provide the basis for conclusions on changes in the Codification.

(Choice A) An exposure draft is published by the FASB to get public comment on a proposed new accounting standard.

(Choice B) A staff accounting bulletin is a summary of the SEC's staff regarding how GAAP principles are applied.

(Choice D) Statement on standards for attestation engagements (SSAE) from the AICPA provide a framework for attestation engagements, including standards for specific types of attestation engagements.

Things to remember:

The FASB Accounting Standards Codification (ASC) is the single source of authoritative GAAP for nongovernmental entities. GAAP is updated with Accounting Standards Updates.

Item ID: 101297

Key: C

FAR.CSO.20210701: FAR.001.001.002

FAR.SSO.20210701: Remembering and Understanding:1

In a company's notes to its financial statements, the first note described significant changes in accounting policies related to valuations of inventory and plant assets. Subsequent notes included a separate note detailing inventories and a separate note detailing plant assets. For which of these subsequent notes, if any, should the company duplicate a description of its changes to significant accounting policies?

- A. The plant assets note, but **not** the inventory note.
- B. The inventory note, but **not** the plant assets note.
- C. Both the plant assets note and the inventory note.
- D. Neither the inventory note nor the plant assets note.

The purpose of financial statements (F/S) is to give users information to make decisions. However, not all relevant information can be presented directly on the F/S (ie, on the face of the F/S). Therefore, GAAP requires F/S be accompanied by informative disclosures known as F/S notes, which aid in interpreting and understanding the F/S.

One prominent F/S note is the **summary of significant accounting policies** (SSAP), which identifies **choices made** (principles and methods of application) when more than one **accounting method** is permitted. Other information relating to **classification of accounts** (eg, cash equivalents, investments) is also disclosed as part of the SSAP.

Note that while the SSAP discloses policies, specific **amounts** are always **disclosed** in a **separate note**. For example, significant changes in accounting policies related to valuations of inventory and plant assets are disclosed under SSAP, yet actual detailed listings of inventory and plant assets are disclosed in a separate note. The company **should not duplicate** a description of its **changes to significant accounting policies in the separate notes (Choices A, B, and C)**.

Things to remember:

GAAP requires financial statements to be accompanied by note disclosures. One prominent note is the summary of significant accounting policies (SSAP) which identifies accounting principles and methods of application when more than one accounting method is permitted. Specific amounts are always disclosed in a separate note and should not be duplicated from the SSAP.

Item ID: 79420

Key: D

FAR.CSO.20210701: FAR.001.002.006

FAR.SSO.20210701: Application:2

Pardelle, Inc. acquired 80% of Soran Co.'s outstanding common stock on December 31, year 1. Pardelle's retained earnings total \$600,000 and Soran's retained earnings total \$400,000 on the acquisition date. What amount should be reported for consolidated retained earnings in the consolidated statement of financial position on the acquisition date?

- A. \$600,000
- B. \$680,000
- C. \$920,000
- D. \$1,000,000

When consolidated F/S are prepared by the parent company (ie, Pardelle, Inc.), the consolidation process eliminates certain account balances (eg, subsidiary retained earnings [RE]) that treat the parent and subsidiary (ie, Soran Co.) as separate entities.

Subsidiary R/E represents earnings from before the consolidation, so it is eliminated as part of the consolidation process. Consolidated statements are prepared as if the group of legal entities were one economic entity, based on the **economic entity concept**.

A noncontrolling interest (NCI) arises when a parent company prepares consolidated financial statements that include a subsidiary in which the parent owns less than 100% (eg, 80%). NCI is recognized as a component of the parent's stockholders' equity at its fair value.

When consolidating the two entities, the **entry to combine equity removes 100% of the acquiree's equity account balances**. Therefore, only the **Pardelle's \$600,000 RE** should be reported for consolidated RE in the consolidated statement of financial position on the acquisition date.

(Choices B and C) Consolidated RE of \$680,000 and \$920,000 incorrectly add 20% and 80% of Soran's RE, respectively, to Pardelle's RE.

(Choice D) Consolidated RE of \$1,000,000 incorrectly includes all of Soran's RE.

Things to remember:

When consolidated financial statements are prepared by the parent company, certain account balances must be eliminated. Subsidiary R/E represents earnings from before the consolidation, so it is eliminated as part of the consolidation process. The entry to combine equity removes 100% of the subsidiary's equity account balances.

Item ID: 48175

Key: A

FAR.CSO.20210701: FAR.001.002.007

FAR.SSO.20210701: Application:2

In year 1, a donor promised to give \$100,000 to a nongovernmental, not-for-profit kitchen if it provides 20,000 meals by March 31, year 2. At the end of year 1, the kitchen had provided 20,000 meals. In which line item, if any, should the contribution be reported in the kitchen's statement of financial position at the end of year 1?

- A. Cash.
- B. Deferred revenue.
- C. Contributions receivable.
- D. The contribution should **not** be reported in the statement of financial position.

Conditional promises to give are pledges that contain donor-imposed conditions representing a barrier that must be overcome. Such promises will become payable to the not-for-profit (NFP) entity when the donor-imposed conditions have been met (ie, provide 20,000 meals by March 31, year 2).

As a result, conditional promises to give are not recognized as revenues until they become unconditional. This occurs when the conditions on which the promise depends have been substantially met.

In year 1, a donor promised to give \$100,000 to NFP kitchen if it provides 20,000 meals by March 31, year 2. The **donor-imposed condition** was **met** by the end of year 1. Therefore, the pledge is included in contribution revenue for year 1. Cash has not yet been received (**Choice A**), and a receivable is recorded for the pledge with the following entry:

Contributions receivable	100,000
Revenues (without donor restriction)	100,000

The NFP kitchen's statement of financial position reports assets, liabilities, and net assets. **Contributions receivable** for the **\$100,000** pledge is reported as an asset at the **end of year 1 (Choice D)**.

(Choice B) Deferred revenue is revenue that is collected but not yet earned. The NFP has earned, but not collected the contribution revenue.

Things to remember:

Conditional promises to give are pledges that contain donor-imposed conditions representing a barrier that must be overcome. They are not recognized as revenues until they become unconditional. This occurs when the conditions on which the promise depends have been substantially met.

Item ID: 92207

Key: C

FAR.CSO.20210701: FAR.001.003.001

FAR.SSO.20210701: Application:2

Bramble, Inc. reported the following at the end of year 1: revenue, \$100,000; assets, \$300,000; and operating profit, \$50,000. One of Bramble's product lines reported the following at the end of year 1: revenue, \$10,000; assets, \$35,000; and operating profit, \$3,000. Which of the following classifications should Bramble use to describe this product line for financial statement presentation purposes?

- A. Operating segment.
- B. Reportable segment.

- C. Subsidiary.
- D. Asset group.

GAAP requires publicly traded entities to separately report and disclose information about major components (ie, reportable segments). A component comprises operations and cash flows that can be clearly distinguished from the rest of the entity. A component of an entity may be a reportable segment or an operating segment, a reporting unit, a subsidiary (ie, >50% owned by another entity), or an asset group.

To determine whether a component is a reportable segment for financial statement (F/S) presentation purposes, three tests are used to compare the revenues, assets, and profits of individual segments with those of the whole company. A **component** needs to **meet only one of the three 10% thresholds to be reportable (Choices A, C, and D).**

- Revenue test: segment's revenue $\geq 10\%$ of the combined company's total revenue (includes intercompany sales).
- Assets test: segment's assets $\geq 10\%$ of the company's identifiable assets, excludes goodwill.
- Profit test: segment's profit $\geq 10\%$ of the company's combined profit/loss. The calculation of total profit is calculated using the absolute value of either combined profits or combined losses, whichever is greater.

Bramble, Inc.'s **product line is a reportable segment** for F/S purposes, because it meets the revenue test and the asset test.

Test	Bramble	Product line	Meets test?
Revenue	$\$100,000 \times 10\% = \$10,000$	\$10,000	Yes
Asset	$\$300,000 \times 10\% = \$30,000$	\$35,000	Yes
Operating profit	$\$50,000 \times 10\% = \$5,000$	\$3,000	No

Things to remember:

GAAP requires publicly traded entities to separately report and disclose information about major components (ie, reportable segments). A segment/component is reportable/a reportable segment if it contributes at least 10% of the total for the whole company of one or more of the following: revenue, assets, or profits.

Item ID: 47265

Key: B

FAR.CSO.20210701: FAR.001.004.000

FAR.SSO.20210701: Application:2

A company entered into a loan with a lender for \$100,000 and pledged \$120,000 of the company's accounts receivable as collateral. The lender does **not** have the right to sell or repledge the accounts receivable. When the company receives the cash for the loan proceeds, what entry, if any, should be made to accounts receivable?

- A. Credit accounts receivable \$20,000.
- B. Credit accounts receivable \$100,000.
- C. Credit accounts receivable \$120,000.

D. No entry is made to accounts receivable.

When a company (ie, debtor) provides a lender (ie, creditor) with collateral for a loan, the accounting depends on who retains control of the collateral (ie, pledged accounts receivable). In most cases, the debtor retains control of the collateral.

Control of the collateral is surrendered (ie, considered a sale) only when all three of the following conditions are met:

- The collateral is beyond the reach of the debtor or its creditors.
- The creditor has the right to pledge or exchange the collateral.
- The debtor does not maintain effective control of the collateral.

In this case, the lender does **not** have the right to sell or repledge the accounts receivable. The company remains the legal owner of the accounts receivable, and simply records a liability for the \$100,000 loan:

Cash	100,000
Note payable	100,000

No entry is made to accounts receivable when the company receives the cash for the loan proceeds (**Choice A, B, and C**).

Things to remember:

When a company (ie, debtor) provides a lender (ie, creditor) with collateral for a loan, the accounting depends on who retains control of the collateral (ie, pledged accounts receivable). If the debtor retains control of the collateral, no entry is made to remove the collateral from the debtor's books.

Item ID: 86849

Key: D

FAR.CSO.20210701: FAR.002.002.000

FAR.SSO.20210701: Application:2

On December 31 of the current year, Letterman Co.'s cost of goods sold amounted to \$1,050,000. However, Letterman's auditors determined the beginning merchandise inventory was understated by \$20,000 and the ending merchandise inventory was overstated by \$12,000. What is the correct cost of goods sold for the current year?

- A. \$1,018,000
- B. \$1,042,000
- C. \$1,058,000
- D. \$1,082,000

COGS is calculated as (**Beginning inventory + Cost of net purchases for the period – Ending inventory**). In this case, beginning inventory is understated, and ending inventory is overstated as determined by Letterman Co.'s auditors.

Understated beginning inventory results in COGS that is understated. To correct understated beginning inventory, add the \$20,000 to COGS (**Choice B**). However, *ending inventory has an inverse relationship to COGS*. Overstated ending inventory results in understated COGS. This is corrected by adding the \$12,000 to COGS (**Choice C**).

The correct **COGS** for the current year is **\$1,082,000** (\$1,050,000 original COGS + \$20,000 beginning inventory + \$12,000 ending inventory).

(**Choice A**) COGS of \$1,018,000 incorrectly subtracts adjustments to beginning and ending inventory.

Things to remember:

COGS is calculated as (Beginning inventory + Cost of net purchases for the period – Ending inventory). Understated beginning inventory results in COGS that is understated. However, ending inventory has an inverse relationship to COGS. Overstated ending inventory results in understated COGS.

Item ID: 43029

Key: D

FAR.CSO.20210701: FAR.002.003.000

FAR.SSO.20210701: Application:2

At the beginning of the current year, a company held trading debt securities with a fair value of \$250,000. During the year, the company received interest income of \$25,000 from the securities and purchased an additional \$50,000 of trading debt securities. At the end of the current year, the company recognized an unrealized loss of \$20,000 on the trading debt securities held as of the end of the year. What amount should the company report for the trading debt securities in its statement of financial position at the end of the current year?

- A. \$280,000
- B. \$300,000
- C. \$305,000
- D. \$325,000

Trading debt securities are investments in debt instruments (eg, bonds) which the investor has acquired in an attempt to make profits by buying and selling within a short period of time. They are **recorded at cost**, but they are **carried at fair value**. Carrying values are adjusted to their current market prices every period (**Choice B**).

The unrealized (ie, holding) gains and losses from market price fluctuations are recorded in net income along with realized gains and losses from sales or other disposals. Interest income is reported in net income; it does not impact the fair value of the securities (**Choices C and D**).

This company should report **\$280,000 in trading debt securities** in its statement of financial position at the end of the current year as calculated below:

Beginning of year balance at fair value	\$250,000
Plus: purchases	50,000
Less: unrealized loss	<u>(20,000)</u>
Ending of year balance at fair value	\$280,000

Things to remember:

Trading debt securities are recorded at cost and carried at fair value. The unrealized (ie, holding) gains and losses from market price fluctuations are recorded in net income along with realized gains and losses from sales or other disposals. Interest income is reported in net income; it does not impact the fair value of the securities.

Item ID: 84062

Key: A

FAR.CSO.20210701: FAR.002.005.001

FAR.SSO.20210701: Application:2

A public business entity has a December 31 year-end reporting period and is aware that a goodwill impairment test must be performed at least once during each reporting period. The entity's controller has compiled a list of four potential dates in year 1 and year 2 to test for goodwill impairment. Assuming that there are **no** events or circumstances requiring impairment testing between the two scheduled dates, which of the following dates in year 1 and year 2, when viewed together, would comply with appropriate guidance?

- A. Year 1, June 20; year 2, December 20.

- B. Year 1, December 31; year 2, June 30.
- C. Year 1, December 31; year 2, March 31.
- D. Year 1, April 15; year 2, April 15.

Goodwill has an indefinite useful life and, similar to other intangibles with indefinite useful lives, it is **tested** for impairment at least **annually** at the same time of year (**Choices A, B, and C**). Goodwill is considered impaired when the carrying value of the reporting unit with which it is associated exceeds that reporting unit's fair value.

In addition to the annual impairment tests, the entity may have reason to believe that goodwill has been impaired between impairment dates. If the entity does determine that it is more likely than not that goodwill has been impaired between the most recent evaluation date and the date of the financial statements, an additional interim impairment test will be performed.

Here, there are **no** events or circumstances requiring impairment testing between the two scheduled dates. Therefore, the testing is required annually. Of the dates provided, only April 15, year 1 and April 15, year 2 meet the annual test requirements.

Things to remember:

Goodwill has an indefinite useful life and, similar to other intangibles with indefinite useful lives, it is tested for impairment at least annually. If the entity determines that it is more likely than not that goodwill has been impaired between the most recent evaluation date and the date of the financial statements, an additional interim impairment test will be performed.

Item ID: 80438

Key: D

FAR.CSO.20210701: FAR.002.006.000

FAR.SSO.20210701: Application:2

A company issued a financial instrument that unconditionally requires the company to settle the obligation by issuing common stock with a value of \$500,000 on the settlement date. How should the company report this instrument in its financial statements?

- A. As a liability in the balance sheet.
- B. As an equity instrument in the balance sheet.
- C. By only disclosing a liability in the notes.
- D. By only disclosing an equity instrument in the notes.

Some financial instruments issued by an entity have characteristics of both debt and equity. ASC 480, *Distinguishing Liabilities from Equity*, requires financial instruments that embody an **obligation** of the issuing entity be reported as a liability. An obligation in this context is a duty or responsibility to transfer assets or issue equity shares. The obligation may be conditional or unconditional.

In this case, the company issued a financial instrument that unconditionally requires it to settle the obligation by issuing common stock with a value of \$500,000 on the settlement date. This is **recorded as a liability in the balance sheet** along with an accompanying disclosure in the notes of the financial statements (**Choices B, C, and D**).

Things to remember:

Some financial instruments issued by an entity have characteristics of both debt and equity. Financial instruments that embody an obligation of the issuing entity are reported as a liability. The obligation may be conditional or unconditional. A financial instrument issued that requires a company to settle the obligation by issuing common stock is recorded as a liability in the balance sheet.

Item ID: 93902

Key: A

FAR.CSO.20210701: FAR.002.008.001

FAR.SSO.20210701: Remembering and Understanding:1

Which of the following items is considered a permanent book to tax difference?

- A. Warranty payable.
- B. Prepaid insurance.
- C. Tax penalties paid to tax authorities.
- D. Accounting for sales of property under the installment method.

Because of the different objectives in financial reporting and taxable income calculations, book net income will differ from taxable income. There are two types of differences between pretax GAAP income and taxable income.

A **permanent difference** is a difference that will appear on **either the F/S or the tax return, but not both**. They do not result in deferred tax differences since they will never reverse. **Tax penalties** paid to tax authorities are recorded as an expense for book purposes but are not tax deductible; therefore, creating a **permanent book to tax difference**.

A **temporary difference** results from items being **taxable or deductible** in a **different period** than the item is reported on the income statement. These differences will reverse over time and are reported as deferred tax assets or deferred tax liabilities.

(Choice A) A warranty payable is a temporary difference resulting from warranty expense recorded for book today, but deductible for tax when paid (ie, deferred tax asset).

(Choices B and D) Prepaid insurance and sales of property using the installment method are temporary differences because future taxable income is expected to be greater than future book income (ie, deferred tax liabilities).

Things to remember:

There are two types of differences between pretax GAAP income and taxable income. A permanent difference is a difference that will appear on either the F/S or the tax return, but not both (ie, tax penalties paid). A temporary difference results from items being taxable or deductible in a different period than the item is reported on the income statement (ie, prepaid expenses).

Item ID: 47865

Key: C

FAR.CSO.20210701: FAR.002.012.000

FAR.SSO.20210701: Remembering and Understanding:1

A defendant has three outstanding lawsuits at the end of year 1. The estimated loss for the first, second, and third cases are \$5,000,000, \$2,000,000, and \$1,000,000, respectively. The likelihood that the defendant will lose the first case is highly probable. The chance of losing the second case is reasonably possible, but not probable. The chance of losing the third case is remote. What amount should the defendant accrue as a contingent liability at the end of year 1?

- A. \$8,000,000
- B. \$7,000,000
- C. \$5,000,000
- D. \$2,000,000

A contingency is a gain or loss that may occur in the future as a result of an existing condition. If the event occurs before the balance sheet date, but the resolution is contingent upon a future event (eg, outstanding lawsuit), there may be a liability that should be recorded.

Contingent losses should be **accrued and disclosed** if they are **probable and estimable**. If the contingency is reasonably possible but not probable it should be disclosed, but not accrued. Remote contingencies are neither disclosed nor accrued.

The defendant has three outstanding lawsuits at the end of year 1:

- First case: Loss highly probable. **Disclose and accrue \$5,000,000**
- Second case: Loss is reasonably possible, but not probable. Disclose \$2,000,000 potential loss but not accrue.
- Third case: Loss is remote. No disclosure or accrual necessary.

At the end of year one, the defendant should accrue a contingent liability of \$5,000,000 for the probable loss of the first case (**Choices A, B, and D**). It should disclose both the first and second case.

Things to remember:

Contingent losses should be accrued and disclosed if they are probable and estimable. If the contingency is reasonably possible but not probable it should be disclosed, but not accrued. Remote contingencies are neither disclosed nor accrued.

Item ID: 48037

Key: C

FAR.CSO.20210701: FAR.003.003.000

FAR.SSO.20210701: Application:2

A company that is translating account balances from another currency into U.S. dollars for year-end financial statements should use the current exchange rate as of the date of the balance sheet for which of the following accounts?

- A. Revenue.
- B. Accounts receivable.

C. Capital stock.

D. Retained earnings.

When a company has an investment in a foreign division or subsidiary included in its consolidated financial statements (F/S), it must remeasure and/or translate the subsidiary's financial information. The subsidiary's F/S are converted from its local currency, the currency it uses for its books and records, into the parent's reporting currency (ie, U.S. dollar).

If the subsidiary's functional currency (ie, currency with the greatest economic impact) is its local currency, the F/S are translated to the parent's reporting currency. The normal translation process used in periods where there is not significant inflation involves applying exchange rates to F/S accounts as follows:

- **Assets and liabilities** are reported as of the F/S date (eg, **accounts receivable**); therefore, they are translated using the F/S date exchange rate (ie, **current exchange rate**).
- The results of operations over a period are reported in the income statement; therefore, income statement items are translated using a weighted average exchange rate for that period (**Choice A**).
- Capital accounts and dividends are translated at historical rates (**Choice C**).
- Retained earnings is rolled forward with translated net income and dividends added to the prior ending balance (**Choice D**).

The translation adjustment is recognized in other comprehensive income on the parent's balance sheet.

Things to remember:

When translating a foreign subsidiary's financial statements (F/S) into the parent's reporting currency, exchange rates are applied as follows. Assets and liabilities use current F/S date exchange rate. Income statement items use a weighted average exchange rate. Capital accounts and dividends use historical rates. Retained earnings is rolled forward with translated net income and dividends and added to the prior ending balance.

Item ID: 44351

Key: B

FAR.CSO.20210701: FAR.003.005.000

FAR.SSO.20210701: Remembering and Understanding:1

Which of the following types of agreement represents a split-interest arrangement?

- A. A perpetual trust naming ABC as sole beneficiary.
- B. A charitable remainder trust.
- C. A direct bequest to ABC in the donor's will.
- D. A direct gift to ABC to be made by the donor next year.

Split-interest arrangements are charitable **giving arrangements** set up by an individual where a not-for-profit **shares the benefits of assets with other beneficiaries** that are typically not charitable organizations. These arrangements can come in different types of structures. They typically span a specified number of years and end when a specific event occurs. In general, this event is the death of the individual donor.

Giving involving sole beneficiaries and direct bequests are not split interest agreements, because there is only *one beneficiary* to the arrangement. In this case, all the choices except for the charitable remainder trust involve a single beneficiary **(Choices A, C, and D)**.

A **charitable remainder trust** is a gift of cash or other assets to a trust. The donor receives income from the trust, and the named charity receives the remaining trust assets at the end of the trust term. Because the benefits of the trust assets are shared between the not-for-profit and the donor, this is a **split-interest arrangement**.

Things to remember:

Split-interest arrangements are giving arrangements where a not-for-profit shares the benefits of assets with other beneficiaries that are typically not charitable organizations. A charitable remainder trust is a gift of cash or other assets to a trust. The donor receives income from the trust, and the named charity receives the remaining trust assets at the end of the trust term.

Item ID: 43127

Key: B

FAR.CSO.20210701: FAR.003.007.000

FAR.SSO.20210701: Remembering and Understanding:1

In year 1, a corporation incurred \$3,500,000 of costs related to the development of a new software product. Of these costs, \$1,000,000 was incurred after technological feasibility was established. The product development was completed, and the product was available for sale to customers early in year 2. The corporation estimated that revenues from the sale of the new product would be \$1,200,000 over five years. What amount of expense should the company report for year 1?

- A. \$500,000
- B. \$700,000
- C. \$2,500,000
- D. \$3,500,000

Businesses acquire knowledge through research and development (R&D). Matching R&D costs from software development to related benefits is virtually impossible because R&D work often results in failure, or the benefits may be unknown. Therefore, **R&D costs** are typically **expensed as incurred**.

Software products become technically feasible when the entity has completed all planning, designing, coding, and testing activities necessary to meet design specifications and performance requirements. Once this milestone has been achieved, costs associated with the product are considered part of the cost of sales and not treated as R&D costs.

The corporation incurred \$3,500,000 of costs related to the development of a new software product in year 1 (**Choice D**). Of these costs, \$1,000,000 was incurred *after technological feasibility* was established. This is capitalized and will be recognized as part of the cost of sales over five years when sales begin in year 2.

Therefore, in **year 1, \$2,500,000 is expensed as R&D** (\$3,500,000 – \$1,000,000).

(Choices A and B) Expenses of \$500,000 and \$700,000 are 1/5 of the \$3,500,000 (total cost) and \$2,500,000 (R&D costs), respectively.

Things to remember:

R&D costs are typically expensed as incurred. When developing a new software product, costs incurred before technical feasibility are expensed as R&D costs. Software becomes technically feasible when all activities necessary to meet design and performance specifications are met. Once you get to technical feasibility, the costs are capitalized and then expensed or amortized.

Item ID: 49153

Key: C

FAR.CSO.20210701: FAR.003.009.000

FAR.SSO.20210701: Application:2

Old Town added a water and sewer department to its municipal services. The department provided the services to the residents of Old Town and issued quarterly billings to customers. In which of the following types of funds would this activity be recorded?

- A. Special revenue.
- B. Capital projects.
- C. Permanent.
- D. Enterprise.

A government's enterprise funds resemble private businesses. They are funded primarily by **voluntary payments** from **external users** in exchange **for goods and services** (eg, utilities). In addition, enterprise funds generally have **pricing policies** that require the **cost of providing services** to be **recovered** primarily through user **fees** and charges.

In this scenario, Old Town added a water and sewer department to its municipal services. The department provided the services to the residents of Old Town and issued quarterly billings to customers (ie, external users). Therefore, the **water and sewer department** should be recorded in an **enterprise fund**.

(Choice A) A special revenue fund is used to account for specific revenues from earmarked sources that are restricted or committed to finance designated activities (eg, gas tax used for road maintenance).

(Choice B) A capital projects fund is used to account for major acquisition or construction activities of capital assets (eg, construction of city hall).

(Choice C) A permanent fund is used to account for assets whose principal is restricted and may not be spent but must be invested permanently (eg, endowment fund). The income generated is available, however.

Things to remember:

A government's enterprise funds resemble private businesses. They are funded primarily by voluntary payments from external users in exchange for goods and services (eg, utilities). In addition, enterprise funds generally have pricing policies that require the cost of providing services to be recovered primarily through user fees and charges.

Item ID: 53035

Key: D

FAR.CSO.20210701: FAR.004.001.003

FAR.SSO.20210701: Application:2

A local government should report expenses, **excluding** special or extraordinary items, by which of the following in its government-wide statement of activities?

- A. Function.
- B. Major source.
- C. Major then minor funds.
- D. Descending order by amount.

Government-wide financial statements (F/S) are prepared on the economic resources measurement focus and accrual basis of accounting. All activities of the primary government are included. *Fund F/S* include a breakdown by major fund.

Government-wide F/S are designed to provide information about operational accountability, which shows how effective the organization has been at using its resources and the resources available to meet its future obligations.

The **Statement of Activities** is similar to an income statement and **reports revenues and expenses**. The net expense or revenue is broken out between governmental activities, business-type activities, and component units. **Expenses are reported by function (eg, public safety, parks) (Choices B, C, and D).**

Things to remember:

The government-wide Statement of Activities is similar to an income statement and reports revenues and expenses. The net expense or revenue is broken out between governmental activities, business-type activities, and component units. Expenses are reported by function.

Item ID: 56307

Key: A

FAR.CSO.20210701: FAR.004.002.001

FAR.SSO.20210701: Remembering and Understanding:1

MULTIPLE CHOICE - HARD

Which of the following is a qualitative characteristic that enhances the usefulness of financial information?

- A. Neutrality.
- B. Materiality.
- C. Verifiability.
- D. Confirmatory value.

FASB has outlined **two fundamental** (ie, relevance, faithful representation) and **four enhancing** (ie, comparability, understandability, timeliness, verifiability) **qualitative characteristics** of useful financial information. To be considered useful, information must have both sets of fundamental characteristics. The enhancing characteristics **increase the usefulness** of information for decision makers.

Enhancing characteristics include the following:

- Comparability means users can identify and understand similarities and differences between financial items (ie, inventory vs cash) from period to period and within similar industries.
- Understandability means classifying, characterizing, and presenting information clearly and concisely.
- Timeliness means that information is available to a decision maker when it is useful to make the decision.
- **Verifiability** means the information can be corroborated by outside parties.

(Choice A) Neutrality is a component of faithful representation, a fundamental characteristic.

(Choices B and D) Materiality and confirmatory value are components of relevance, a fundamental characteristic.

Things to remember: FASB has outlined two fundamental and four enhancing (ie, comparability, understandability, timeliness, verifiability) qualitative characteristics of useful financial information.

Item ID:94710

Key: C

FAR.CSO.20210701: FAR.001.001.001

FAR.SSO.20210701: Remembering and Understanding:1

A company reported the following for the current year:

Retained earnings appropriated for plant expansion	\$32,500
Correction of understated depreciation expense from prior periods	9,300
Unrealized loss on available-for-sale debt securities	8,100
Unrealized gain on foreign currency translation	3,400

The company's current-year net income was \$86,500, and the company has a 30% effective income tax rate. What amount of comprehensive income should be reported for the current year?

- A. \$40,000
- B. \$76,700
- C. \$81,800
- D. \$83,210

An entity's comprehensive income is the sum of its net income (loss) plus total other comprehensive income (OCI), net of tax. **OCI** reports certain **gains** and **losses** from transactions **not** captured in **net income**. Because these transactions have not been realized, they have the potential to distort net income and therefore are not included in net income. Instead, they are reported as other comprehensive income.

Components of OCI include:

- Derivative cash flow hedges
- Excess adjustment on defined benefit pension plans
- Net unrealized gains and losses on available-for-sale debt securities
- Translation gains and losses (foreign currency)

In this scenario comprehensive income is calculated as follows:

Net income		\$	86,500
Other comprehensive income (net of tax)			
Unrealized loss on available-for-sale debt securities (\$8,100 x (1- 30% tax rate))	(5,670)		
Unrealized gain on foreign currency translation (\$3,400 x (1- 30% tax rate))	<u>2,380</u>		
Total other comprehensive income			<u>(3,290)</u>
Comprehensive income		\$	83,210

(Choice A) An amount of \$40,000 incorrectly includes appropriated retained earnings and the depreciation correction and does not adjust any of the items for tax.

(Choice B) An amount of \$76,700 incorrectly includes the correction for depreciation expense (net of tax).

(Choice C) An amount of \$81,800 is not calculated net of tax.

Things to remember: Comprehensive income equals net income plus other comprehensive income. Other comprehensive income consists of derivative cash flow hedges, excess adjustment on defined benefit pension plans, net unrealized gains and losses on available-for-sale debt securities, and translation gains and losses (foreign currency).

Item ID:100364

Key: D

FAR.CSO.20210701: FAR.001.002.003

FAR.SSO.20210701: Application:2

A U.S. company owns 80% of a non-U.S. company located in a foreign country with a very unstable political and economic climate. In which of the following situations should the U.S. company **not** consolidate its financial statements with the non-U.S. company?

- A. The foreign country has currency exchange rate fluctuations on a daily basis.
- B. The government of the foreign country has increased the tax rate for all companies that are majority-owned by U.S. companies.
- C. The government of the foreign country has required all companies operating within its borders to implement International Financial Reporting Standards.
- D. The government of the foreign country has recently imposed a number of severe sanctions and controls on all companies that are majority-owned by U.S. companies.

When one company (ie, parent) has a controlling financial interest (ie, greater than 50%) in another entity (ie, subsidiary), consolidated financial reporting is *typically* required. The **combined company** is viewed as a **single economic entity** because the parent *controls* all of the subsidiary's resources and financial decisions.

Having control of a subsidiary in a foreign country is accompanied by certain **normal** business expectations (eg, exchange rate fluctuations, changes in tax rates, adoption of International Financial Reporting Standards as the standard of accounting reporting) (Choices A, B, and C).

However, if the subsidiary operates under **severe foreign restrictions** (eg, severe sanctions on all majority-owned by U.S. companies), which interfere with the parent's ability to control the subsidiary, the majority-owned subsidiary shall **not** be **consolidated**.

Things to remember: Consolidated financial statements are *normally* required when a parent-subsidiary relationship exists. If the parent cannot exercise control over the subsidiary because of severe foreign restrictions, consolidated statements are not required.

Item ID:75074

Key: D

FAR.CSO.20210701: FAR.001.002.007

FAR.SSO.20210701: Application:2

In the current year a nongovernmental, not-for-profit entity incurred \$630,000 in expenditures during the year. It also received donated legal services, which otherwise would have cost \$40,000, and consumed donated supplies with a value of \$15,000. What should the entity report as total expenses in its statement of activities for the current year?

- A. \$630,000
- B. \$645,000
- C. \$685,000
- D. \$670,000

The financial statements (F/S) of a not-for-profit organization (NPO) provide useful information to members, creditors, and donors. Among the required statements is the **statement of activities**, which presents the inflows and outflows of resources, allowing stakeholders to assess how efficiently the NPO operated its programs and services.

Donations of goods, which defray **general expenses** (eg, donated supplies) must be recognized as an inflow and expensed as supplies. Donations of time to perform routine services (eg, mailing informational fliers) are *generally* not recognized. However, **specialized services** (eg, legal services) must be recognized because they **defray expenses** for which the NPO would otherwise be required to pay.

In this scenario, the total expenses recorded would be **\$685,000** (\$630,000 + \$40,000 + \$15,000).

(Choice A) An amount of \$630,000 ignores the supplies and services used by the organization.

(Choice B) An amount of \$645,000 includes the supplies used, but incorrectly excludes the specialized legal services.

(Choice D) An amount of \$670,000 includes the specialized legal services, but incorrectly excludes the supplies used.

Things to remember: The NFP must recognize a contribution for the donation of supplies and specialized/professional services if the NFP would have otherwise paid for the services. These costs are then recorded as expenses as they defray the costs that would normally be incurred.

Item ID:92217

Key: C

FAR.CSO.20210701: FAR.001.003.002

FAR.SSO.20210701: Application:2

A company provides a defined-contribution pension plan for its employees. For the plan administrator to report contributions from the company, contributions from participants, benefits paid to participants, and changes in fair value of investments, which of the following financial statements is required?

- A. Statement of net assets available for benefits.
- B. Statement of cash flows.
- C. Statement of changes in net assets available for benefits.
- D. Statement of changes in financial position.

A pension plan is an employment-based retirement plan that provides **income** to plan participants **after retiring**. There are two types of pension plans, **defined benefit** and **defined contribution**. The required F/S for both types of pension plans provide users with information about the plan's ability to pay benefits. The two statements and related information are:

- A statement of net assets available for benefits (as of fiscal year end), which reports **(Choice A)**
 - Total assets
 - Total liabilities
 - Net assets available for benefits.
- A statement of **changes in net assets available for benefits (for the fiscal year)**, which reports
 - Contributions from employers.
 - Contributions from participants.
 - Benefits paid to participants.
 - Net increase/decrease in the fair value of investments held at year end.
 - Contributions from other sources (eg, state subsidies or federal grants).
 - Payments to insurance entities
 - Administrative expenses.

Neither type of pension plan is required to provide a statement of cash flows or a statement of changes in financial position **(Choices B and D)**.

Things to remember: Included in the statement of changes in net assets available for benefits are contributions from employers, contributions from participants, benefits paid to participants, and changes in the fair value of investments.

Item ID:51615

Key: C

FAR.CSO.20210701: FAR.001.005.000

FAR.SSO.20210701: Remembering and Understanding:1

On the first day of the year, a donor established a \$100,000 irrevocable perpetual trust with a third-party trustee naming a not-for-profit entity as the sole income beneficiary in perpetuity. During the year, the trust earned and distributed \$4,000 in income to the entity for unrestricted use. On the last day of the year, the fair value of the trust had increased by \$5,000. What amount should the entity report in its year-end statement of financial position as beneficial interest in perpetual trust?

- A. \$96,000
- B. \$100,000
- C. \$101,000
- D. \$105,000

The **statement of financial position** (SFP) of a not-for-profit organization (NPO) is similar to a balance sheet of a for-profit entity, and reports assets, liabilities, and net assets.

Investments, whether donated or purchased, are initially recorded at **fair value** (FV) and **revalued** each reporting period (if FV is determinable). Realized and unrealized gains and losses are reported directly in the statement of activities each reporting period.

In this case, the FV of the investment has increased by \$5,000, from \$100,000 to **\$105,000**. The additional \$4,000 is income earned, not a change in the fair value.

(Choice A) An amount of \$96,000 incorrectly deducts the income earned from the initial donation.

(Choice B) An amount of \$100,000 is the initial value of the donation, rather than the fair value at year-end.

(Choice C) An amount of \$101,000 incorrectly deducts the income distribution from the year-end fair value.

Things to remember: The statement of financial position for a not-for-profit organization recognizes donated investments at fair value. Any interest earned on the investment is recorded as income.

Item ID:74819

Key: D

FAR.CSO.20210701: FAR.002.005.001

FAR.SSO.20210701: Application:2

In which of the following circumstances would trademarks acquired by an entity most likely be deemed to have an indefinite useful life?

- A. The entity pays substantial amounts of money to renew the trademarks.
- B. The entity operates in an industry with a rapidly changing regulatory environment governing trademarks.
- C. The entity plans to use the trademark until the planned phase-out date of the underlying asset.
- D. The entity's trademark has a remaining legal life of five years but is renewable at very little cost.

A trademark is an intangible asset that provides legal protection for the exclusive use of an identifying word, phrase, symbol, or design associated with goods or services. The protection afforded by a trademark must be maintained at regular intervals and can be **renewed** every 10 years **in perpetuity**, resulting in an **indefinite life**.

Generally, the ongoing renewal of the trademark is **less likely** when there are **substantial costs** for renewal, rapid **regulatory changes** which govern trademarks, and plans to **phase-out the underlying asset (Choices A, B and C)**. These factors are indicative of a trademark which might provide limited use or limited value for the entity, resulting in limited life.

If there are no legal or economic factors that limit the use of the trademark, it may have an indefinite life, which is *not* subject to amortization. Intangible assets with an indefinite life are **tested** at least annually **for impairment** and written down if the value is deemed unrecoverable.

Things to remember: A trademark (ie, an intangible asset) may have an indefinite life if the registration is maintained and renewed every 10 years. The entity must be willing and able to renew the trademark.

Item ID:56117

Key: D

FAR.CSO.20210701: FAR.002.006.000

FAR.SSO.20210701: Remembering and Understanding:1

A nongovernmental, not-for-profit entity calculated a \$4,000 increase in net assets with donor restrictions for the current fiscal year before consideration of the following:

A cash donation designated by the donor as an endowment in perpetuity	\$28,000
Net assets released from restrictions	12,000
A donation received that was designated as a quasi-endowment	21,000

Which of the following should be reported as the increase in net assets with donor restrictions in the current-year statement of activities?

- A. \$16,000
- B. \$20,000
- C. \$37,000
- D. \$41,000

A statement of activities for a not-for-profit organization (NPO) presents **net assets** (assets minus liabilities) and the **change in net assets**. The net assets section is divided into two categories: **with donor restrictions** and **without donor restrictions**.

An **endowment** has a **donor restriction**, which requires investing the principal amount donated and using only the investment income for general operations. **Quasi-endowments** are funds subject to **restrictions**, but only those which are **internally imposed** by the NPO's governing board. Because the endowment designation is **not donor imposed** and the board may alter its designation, the asset is categorized as without donor restrictions.

In this scenario, the calculated increase in **net assets with donor restrictions** is shown below. Because the quasi endowment is not *donor-restricted*, it is not included.

Calculated increase in net assets with donor restrictions	\$4,000
A cash donation designated by the donor as an endowment in perpetuity	28,000
Net assets released from restrictions	(12,000)
Total net assets with donor restrictions	\$20,000

(Choice A) An amount of \$16,000 (\$4,000 + \$12,000) incorrectly adds the funds release from restrictions.

(Choice C) An amount of \$37,000 (\$4,000 + \$12,000 + \$21,000) incorrectly adds the funds released from restriction and the quasi-endowment.

(Choice D) An amount of \$41,000 (\$4,000 + \$28,000 – \$12,000 + \$21,000) incorrectly includes the quasi-endowment (ie, board-restricted).

Things to remember: When the donor's restrictions are lifted, the funds are considered unrestricted (ie, *without* donor restrictions). Net assets with donor restrictions include only funds restricted by donors, not internally restricted funds (ie, board-restricted).

Item ID:98640

Key: B

FAR.CSO.20210701: FAR.002.009.000

FAR.SSO.20210701: Application:2

A company signed a five-year contract with a customer in Year 1 and agreed to modify the contract at the beginning of Year 2. Which of the following is a condition that must be present in order for the contract modification to be accounted for as a separate contract?

- A. The original contract is terminated.
- B. The price of the original contract remains the same.
- C. The performance obligations of the original contract are partially satisfied.
- D. The scope of the original contract increases through the addition of distinct goods or services.

There are **five steps** in the **revenue recognition** process.

Step 1. Identify contracts with customers.

Step 2. Identify all separate performance obligations within each contract.

Step 3. Determine the total consideration for the contract.

Step 4. Allocate the total consideration among the separate performance obligations.

Step 5. Recognize revenue.

Step 1 involves identifying contracts with customers, including occasional **modifications** to existing contracts. Modifications could include a change in transaction price or the addition of a performance obligation. A modification that is *not* distinct is accounted for as if it were a part of the existing contract.

However, a **modification** that includes additional **distinct** goods/services that are a **significant change** in *both scope* and **price** of an existing contract is accounted for as a new, **separate contract**.

Things to remember: In order for a contract modification to be accounted for as a separate contract, the modification must include additional distinct goods/services and include a significant change in *both* scope and price.

Item ID:96047

Key: D

FAR.CSO.20210701: FAR.002.010.000

FAR.SSO.20210701: Remembering and Understanding:1

Which of the following statements is correct regarding the Black-Scholes-Merton option-pricing model used to estimate the fair value of stock options granted to employees as part of a company's compensatory stock option plan?

- A. The model's formula assumes that option exercises occur at the beginning of an option's contractual term.
- B. The model's formula assumes that expected dividends vary over the option's term.
- C. The model's formula assumes that risk-free interest rates are constant over the option's term.
- D. The model is referred to as a lattice model.

GAAP outlines a fair value hierarchy that is used to measure the value of certain assets and liabilities. The hierarchy has **three levels** that are ordered by preference and reliability, which serves to enhance the quality and comparability in fair value reporting. **Level 1** is the most preferred and reliable because it is based on **observable** unadjusted quoted prices in **active markets** for identical items.

For a future share option (ie, future stock price), an observable market price may not be available, thus an **estimate** of the **fair value** is needed. A valuation technique such as an **option-pricing model** (eg, Black-Scholes-Merton) or **binomial model** (eg, lattice model) may be used to estimate the fair value of share options or similar instruments (**Choice D**).

Black-Scholes-Merton assumes that option exercises occur at the **end** of the option's contractual term and that the following are **constant** over the option term (**Choices A and B**):

- Expected volatility
- Expected dividends
- Risk-free interest rates

Things to remember: The Black-Scholes-Merton (BSM) option pricing model is used to estimate the fair value of employee-granted stock options. The underlying assumptions of BSM are that option exercises occur at the end of the term and expected volatility, expected dividends and risk-free interest rates are constant.

Item ID:46491

Key: C

FAR.CSO.20210701: FAR.002.011.000

FAR.SSO.20210701: Remembering and Understanding:1

A company reported \$130,000 in income from continuing operations for its first year of operations. The tax-basis depreciation deduction for the year exceeded GAAP depreciation expense by \$12,500, and the warranty accrual exceeded the amount spent for warranty repairs by \$8,300. The company properly calculated a \$840 increase in its deferred tax liability for the year. If the enacted tax rate for the current year is 20%, what amount of income taxes payable should be reported in the year-end balance sheet?

- A. \$24,340
- B. \$25,160
- C. \$26,000
- D. \$26,840

Pretax book income differs from taxable income because their reporting requirements are governed by two **different** sets of **regulations** (ie, GAAP and Internal Revenue Code). Taxes payable are based on taxable income $\times$ tax rate. To determine the current amount of taxes payable, the **pretax book income** is **adjusted** for differences between book and tax items (ie, permanent and temporary).

After adjusting pretax book income, the calculated taxable income is multiplied by the current tax rate to arrive at the current tax liability (ie, taxes payable).

In this case the pretax book income is

- Reduced by \$12,500 because the tax return allows more depreciation expense.
- Increased by \$8,300 because the accrued warranty costs were not paid in the current period. Tax only permits the deduction of actual warranty costs, not *estimated* warranty costs.

Pretax income		\$	130,000
Temporary differences			
Depreciation	(12,500)		
Warranty costs	8,300		
Net temporary differences			<u>(4,200)</u>
Taxable income			125,800
Tax rate			20%
Income tax payable		\$	25,160

(Choice A) An amount of \$24,340 excludes depreciation and incorrectly subtracts, rather than adds warranty costs.

(Choice C) An amount of \$26,000 ignores both required adjustments.

(Choice D) An amount of \$26,840 incorrectly adds depreciation and subtracts warranty costs.

Things to remember: The current tax liability (ie, taxes payable) is calculated by multiplying taxable income by the current enacted tax rate. The current taxable income is determined by adjusting pretax book income for any permanent and temporary differences.

Item ID:505103

Key: B

FAR.CSO.20210701: FAR.002.012.000

FAR.SSO.20210701: Application:2

With regard to a fair value hedge, hedge effectiveness is a measure of the extent to which the

- A. Cash flows from the hedge transaction offset cash flows from the hedged risk.
- B. Hedge transaction results in eliminating changes in fair value of the hedged item.
- C. Hedge transaction offsets the exposure to changes in the hedged item's fair value.
- D. Actual change in the hedge's fair value corresponds to the expected change in the hedge's fair value.

Derivative contracts can be used to hedge against the risk associated with another contract or planned activity (ie, hedged item). Hedging can **reduce** or **eliminate** the **risk** of an adverse change in circumstances.

Some hedges do not entirely protect a company against the risk that the hedge is intended to mitigate. A **fair value hedge**, for example, may not offset all changes in the FV of the hedged item. The degree to which a change in the value of a FV hedge **offsets the change** in the value of the hedged item is called the **hedge's effectiveness**.

(Choice A) The effectiveness of a cash flow hedge is the degree to which a change in the cash flows from the hedge transaction offset cash flows from the hedged risk.

(Choice B) Hedges offset the change in FV. They cannot eliminate the change in FV.

(Choice D) Effectiveness measures the offset of the change in FV. It does not measure the change in the price/FV of the hedge.

Things to remember: A fair value hedge is a derivative contract used to reduce the risk of changes in the values of recognized assets and liabilities. The effectiveness of a hedge is based on the degree to which a change in its value offsets the change in the value of the hedged item.

Item ID:84818

Key: C

FAR.CSO.20210701: FAR.003.004.000

FAR.SSO.20210701: Remembering and Understanding:1

The lessee should recognize amounts probable of being owed under a residual value guarantee as a component of lease payments

- A. At the conclusion of the lease.
- B. At **no** time during the lease term.
- C. On a straight-line basis during the lease.
- D. On the commencement date of the lease.

A lessee initially measures a lease as the PV of the lease payments. **Lease payments** represent the amount that the **lessee** will likely **pay** for the use of the underlying asset. Such payments may include fixed payments, in substance fixed payments, certain variable lease payments, and amounts likely to be owed under residual value guarantees.

A **residual value guarantee** is when the lessee guarantees that the property will be worth at least a certain amount when it is returned to the lessor at the termination of the lease. Any deficiency will be made up by the lessee. To determine the probable amount included in the lease payments, the guaranteed value is compared with the leased asset's expected residual value at the end of the lease term. When the guaranteed value is:

- **Greater than** the leased asset's expected value, the difference is **included** in the total **lease payments**.
- **Less than** the leased asset's expected value, the guarantee is **excluded** from the total lease payments because the lessee will **not have to pay** any extra to the lessor related to the guarantee.

When the lessee has a probable obligation to pay the residual value guarantee, the calculation of the **total lease payments** **includes** the amount of the **residual value guarantee** at the **inception** of the lease.

Things to remember: A residual value guarantee is a probable amount that a lessee will have to pay for the leased asset at the end of the lease. If the guaranteed value is greater than the leased asset's expected value, the guaranteed value is recognized as part of the lease payment at the inception of the lease.

Item ID:502945

Key: D

FAR.CSO.20210701: FAR.003.006.000

FAR.SSO.20210701: Remembering and Understanding:1

In Year 4, a nongovernmental, not-for-profit school began a campaign to raise funds for a proposed capital addition. The following information is available as of June 30, Year 4:

<u>Information</u>	<u>Amount</u>
Received on February 1, Year 4: cash contributions from parents and alumni	\$450,000
Received on February 1, Year 4: unconditional promises to give, of which \$300,000 was received as of June 30, Year 4	600,000
Received on March 1, Year 4: a promise from a Year 1 alumnus to give \$50,000 if other year 1 alumni give a total of \$50,000 before September 30, Year 5	50,000
Received on June 30, Year 4: cash contributions from Year 1 alumni in response to March 1, Year 4, alumni challenge	20,000

What amount of cash contributions for this campaign should the school report in its June 30, Year 4, statement of activities?

- A. \$770,000
- B. \$1,050,000
- C. \$1,070,000
- D. \$1,090,000

The financial statements (F/S) of a not-for-profit organization (NPO) provide useful information to members, creditors, and donors. Among the required statements is the **statement of activities**, which presents the inflows and outflows of resources, allowing stakeholders to assess how efficiently the NPO operated its programs and services.

The statement of activities reports **cash contributions** that are **unconditional** (ie, not subject to *donor* conditions) on the date contributed. If there are donor-imposed conditions (ie, other alumni must also give), the **promise to give** is not reported until the conditions have been satisfied or removed.

In this case, the following contributions were received, and any conditions met. Thus, the NPO would report cash contributions for June 30, Year 4 in the following amount:

Received on February 1, Year 4: cash contributions from parents and alumni	\$450,000
Received on February 1, Year 4: unconditional promises to give, of which \$300,000 was received as of June 30, Year 4	600,000
Received on June 30, Year 4: cash contributions from Year 1 alumni in response to March 1, Year 4, alumni challenge	20,000
Total	\$1,070,000

The conditional pledge based on giving by other alumni will not be recorded until the conditions have been met (ie, \$50,000 matching contributions).

(Choice A) An amount of \$770,000 only includes half of the unconditional promised amount. The full amount of the *unconditional* pledge should be recognized.

(Choice B) An amount of \$1,050,000 excludes the *unconditional* cash contributions received on June 30.

(Choice D) An amount of \$1,090,000 includes an additional \$20,000 of unreceived matched funds, which cannot be recorded until the condition is met.

Things to remember: Unconditional pledges to a not-for-profit organization are reported as cash contributions on the statement of activities. Conditional pledges are not recognized until the condition is satisfied.

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FAR.CSO.20210701: FAR.003.007.000

FAR.SSO.20210701: Application:2

2022 AICPA Released Questions - FAR

When the recoverability of a building's carrying amount is determined to be impaired, the building's fair value is best measured as the

- A. Price the building can be sold for in an advantageous market.
- B. The selling price **less** transaction costs to complete the sale for this type of building in its principal market.
- C. Price that would be received for this type of building based on observable inputs in its principal market.
- D. Price determined using internal cost estimates to construct a similar building.

A fair value measurement estimates the price at which the asset would sell in an orderly transaction among market participants. The valuation techniques must consider the level of the fair value hierarchy.

The GAAP fair value hierarchy has **three levels** that are ordered by preference and reliability, which serves to enhance the quality and comparability in fair value reporting.

- **Level 1** inputs are based on **observable** unadjusted quoted prices in **active markets** for identical items. Level 1 is most preferred and reliable.
- **Level 2** inputs are based on observable prices, but for *similar* items, **not identical** items.
- **Level 3** inputs are prices **unobservable** by the market (ie, internally generated).

The best measure of the building's fair value is the observable unadjusted price based on identical items in the market, (ie, Level 1)

(Choice A) If the **principal market** for an asset is **not determinable**, the fair value of the asset would be measured using the price in the most advantageous market.

(Choice B) The price in the principal market used to measure the fair value of an asset or liability is not adjusted for transaction costs.

(Choice D) Using unobservable inputs (ie, internal cost estimates) is the least desirable technique

Things to remember: The goal of fair value measurement is to estimate the price of an asset or to transfer the liability objectively. The most preferred and reliable valuation technique is based on observable unadjusted quoted prices in active markets for identical assets or liabilities.

Item ID:56101

Key: C

FAR.CSO.20210701: FAR.003.011.000

FAR.SSO.20210701: Remembering and Understanding:1

A local government recorded revenues as follows: personal income tax, \$200,000; sales taxes, \$100,000; and property taxes, \$150,000. What should the local government report as total derived tax revenue?

- A. \$100,000
- B. \$150,000
- C. \$300,000
- D. \$450,000

Revenue for government entities is generated by both exchange and nonexchange transactions. **Exchange transactions** occur when something of **reciprocal value** is received and sacrificed by both parties (eg, purchase of utilities). **Nonexchange transactions** occur when the **government receives** something of value from another entity (eg, taxpayer) **without directly giving** anything of equal value in return.

Nonexchange revenue sources include

- **Derived tax revenues** are self-assessed on exchange transactions (eg, sales tax, income tax)
- Imposed nonexchange revenues are taxes or fees assessed on assets or rights rather than exchange transactions (eg, property taxes, fines)
- Government-mandated nonexchange revenue derive from transactions where one level of government provides funds to another level of government for a specific purpose (eg, federal programs that state or local governments are mandated to perform)
- Voluntary nonexchange revenue (eg, grants, donations)

Derived tax revenue is generated from taxes assessed on the exchange transactions of others. In this case, the derived tax revenue is **\$300,000** (\$200,000 personal income tax + \$100,000 sales tax).

(Choice A) An amount of \$100,000 excludes personal income tax.

(Choice B) An amount of \$150,000 represents property taxes, which are *not* derived tax revenues. These are imposed nonexchange revenues.

(Choice D) An amount of \$450,000 incorrectly includes property taxes.

Things to remember: Derived tax revenue is an inflow generated from taxes that are self-assessed on exchange transactions of others (eg, sales tax, income tax).

Item ID:84406

Key: C

FAR.CSO.20210701: FAR.004.004.006

FAR.SSO.20210701: Application:2

Which of the following is **not** required in the budgetary comparison schedule presented by a state or local government as part of required supplementary information?

- A. The original budget.
- B. The final appropriated budget.
- C. Variances between the final budget and actual amounts.
- D. Actual inflows, outflows, and balances stated on a budgetary basis.

GASB establishes financial reporting standards for state and local governments in the U.S. It identifies the components of the basic financial statements and the **required supplementary information** for government entities. A budgetary comparison schedule (BCS) must be included as part of the required supplementary information based on various GASB pronouncements.

The **BCS compares** the original **budgeted amounts** from the beginning of the year to the year's **actual amounts**. The BCS allows taxpayers to evaluate whether the government received less revenue than planned or made expenditures in excess of the budgeted amount.

The BCS should **include** the:

- Original budget **(Choice A)**
- Final appropriated budget **(Choice B)**
- Actual inflows, outflows, and balances stated on a budgetary basis **(Choice D)**.

Things to remember: The budgetary comparison schedule is required supplementary information and presents the original budget, final appropriated budget, and actual inflows, outflows and balances stated on a budgetary basis. Including a column with calculated variances is optional.

Item ID:507337

Key: C

FAR.CSO.20210701: FAR.004.004.009

FAR.SSO.20210701: Remembering and Understanding:1

TASK BASED SIMULATIONS

Item: 500178

Scroll down to complete all parts of this task.

A company has the following information relating to transactions in year 1, its first year of operations. The company applies the straight-line method to amortize its intangible assets. The company elected the private company alternative for the subsequent measurement of goodwill and concluded that the maximum amortization period permitted under the alternative was appropriate. For each transaction, enter the asset carrying amount at December 31, year 1. If an amount is zero, enter a zero (0). Round all amounts to the nearest dollar.

	A	B	C	D
1	Date	Transactions	Amount	Asset carrying amount at 12/31/year 1
2	1/1	Purchased a patent with an estimated useful life of eight years.	\$400,000	\$350,000 ¹²³
3	4/1	Recognized goodwill from the acquisition of a competitor.	\$300,000	\$277,500 ¹²³
4	6/1	Incurred sales and marketing costs to promote the company's brand name. The company expects the sales and marketing efforts to positively impact sales over the next two years.	\$325,000	\$0 ¹²³
5	7/1	Paid an initial franchise fee related to a 10-year franchise agreement.	\$600,000	\$570,000 ¹²³
6	9/1	Purchased a license that has an indefinite life. The fair value of the license at December 31, year 1, was \$235,000.	\$250,000	\$235,000 ¹²³
7	10/1	Purchased a copyright with a contractual life of 20 years and entered into an agreement to sell the copyright in 10 years for \$200,000.	\$540,000	\$531,500 ¹²³
8	12/31	Incurred current-year research and development costs for a product to be launched in year 2.	\$500,000	\$0 ¹²³

END OF CONTENT -----

	A	B	C	D
1	Date	Transactions	Amount	Asset carrying amount at 12/31/year 1
2	1/1	Purchased a patent with an estimated useful life of eight years.	\$400,000	\$350,000
The company uses the straight-line (S/L) method (ie, equal amounts each period) to amortize its intangible assets. The patent was purchased for \$400,000 and has an estimated useful life of 8 years resulting in an annual amortization of \$50,000 (\$400,000 / 8 years). Because the patent was purchased on 1/1, the carrying value of the patent is reduced by an entire year of amortization expense. On 12/31/year 1, the patent's carrying value is \$350,000 (\$400,000 – \$50,000).				
3	4/1	Recognized goodwill from the acquisition of a competitor.	\$300,000	\$277,500
The FASB created the private company council (PCC) to reduce the cost of financial reporting for nonpublic entities. A nonpublic entity can elect to amortize goodwill on a S/L basis over its useful life, not to exceed 10 years. Annual amortization equals \$30,000 (\$300,000 / 10 years). Because the acquisition was made on 4/1, the annual amortization is prorated for 9 months (April to December). Amortization in year 1 is \$22,500 (\$30,000 annual amortization × 9/12 months). On 12/31/year 1, the carrying amount of goodwill is \$277,500 (\$300,000 – \$22,500).				
4	6/1	Incurred sales and marketing costs to promote the company's brand name. The company expects the sales and marketing efforts to positively impact sales over the next two years.	\$325,000	\$0
Intangible assets are separate and distinct company assets that lack physical substance and provide economic benefits to the company. Examples of marketing related intangible assets are trademarks, trade names, and noncompetition agreements. Because sales and marketing costs are directly related to sales, they are expensed in the period incurred. Therefore, there is no intangible asset created from these expenses; carrying value is \$0.				
5	7/1	Paid an initial franchise fee related to a 10-year franchise agreement.	\$600,000	\$570,000
A franchise agreement is a contract based intangible asset. The franchise agreement has a 10-year definite life, resulting in annual amortization of \$60,000 (\$600,000 / 10 years). Because the franchise fee was paid on 7/1, the annual amortization needs to be prorated for 6 months (July to December). Amortization in year 1 is \$30,000 (\$60,000 annual amortization × 6/12 months). On 12/31/year 1, the carrying amount of the franchise is \$570,000 (\$600,000 – \$30,000).				
6	9/1	Purchased a license that has an indefinite life. The fair value of the license at December 31, year 1 was \$235,000.	\$250,000	\$235,000
Intangible assets with indefinite lives are not amortized; they are tested at least annually for impairment. The carrying value of the asset is compared to its fair value. If the fair value is less than the carrying value, the asset is impaired, and a loss is recognized in the amount equal to the excess of its carrying value over its fair value. The asset's carrying value is written down to its fair value. Here, the fair value of the license on December 31, year 1 is less than its original purchase amount indicating an impairment (\$235,000 fair value < \$250,000 purchase price). The license is written down to its fair value, and the December 31, year 1 carrying value is \$235,000.				
7	10/1	Purchased a copyright with a contractual life of 20 years and entered into an agreement to sell the copyright in 10 years for \$200,000.	\$540,000	\$531,500
The \$540,000 copyright is an intangible asset with a contractual life of 20 years. However, the company entered into an agreement to sell the copyright in 10 years for \$200,000. The company should amortize \$340,000 (\$540,000 purchase price – \$200,000 future sales price) for the 10 years it owns the copyright. The annual amortization is \$34,000 (\$340,000 / 10 years). The copyright was purchased on 10/1, therefore the annual amortization is prorated for 3 months (October to December). Amortization in year 1 is \$8,500 (\$34,000 annual amortization × 3/12 months). On 12/31/year 1, the carrying amount of the copyright is \$531,500 (\$540,000 – \$8,500).				

8	12/31	Incurred current-year research and development costs for a product to be launched in year 2.	\$500,000	\$0
	Businesses acquire knowledge through research and development (R&D). Matching R&D costs to related benefits is virtually impossible because R&D work often results in failure, or the benefits may be unknown. Therefore, R&D costs are typically expensed as incurred. Therefore, there is no asset on December 31, year 1; carrying value is \$0.			

Blueprint Information

CSO: 002.006.000

Skill: Application

Representative task: Calculate the carrying amount of finite-lived intangible assets reported in the financial statements (initial measurement, amortization and impairment) and prepare journal entries.

Item: **500713**

A nongovernmental, not-for-profit federated fundraising entity spent \$50,000 on an annual fundraising campaign for the benefit of a local charity. Which section of the authoritative literature best supports the entity's decision to report the \$50,000 as fundraising expenses?

Enter your response in the answer fields below. Unless specifically requested, your response should not cite implementation guidance. Guidance on correctly structuring your response appears above and below the answer fields.

Type the paragraph here.

Correctly formatted FASB ASC paragraphs are 1, 2, or 3 digits followed in some cases by 1, 2, 3, or 4 upper case letters. Note: Correct paragraph responses appear in bold font in FASB ASC and do not include subparagraphs denoted by a lower case letter.

FASB ASC 958 - 720 - 45 - 27

i Some examples of correctly formatted FASB ASC responses are 205-10-05-1, 323-740-S25-1, 260-10-60-1A, 715-30-35-95, 820-10-35-16BB, 810-10-55-205AE, 815-10-50-4EEE, and 815-10-50-4EEEE.

Correct answer	FASB ASC 958-720-45-27
Keyword search suggestions	Not-for-profit, expenses, federated fundraising
Solution	958: Not-for-profit entities 720: Other expenses 45: Other presentation matters 27: Expenses of federated fundraising entities
Excerpt	Federated fundraising entities solicit and receive designated and undesignated contributions and make grants and awards to other NFPs. The fundraising activities of federated fundraising entities, including activities related to fundraising on behalf of others, shall be reported as fundraising expenses.
Other considerations	Key phrases in a research question can be used to match phrases used in the Codification; searching for those key phrases will usually lead to the correct answer.

Blueprint Information

CSO: 001.003.002

Skill: Application

Representative task: ASC 958-720-45

Item: 508395

Scroll down to complete all parts of this task.

Apex Corp. is in the process of determining the appropriate accounting treatment for a number of year 7 transactions and events related to property, plant and equipment.

Review the draft memorandum below, along with the exhibits above, and make the necessary corrections, if any, to the proposed accounting treatments and to the supporting authoritative references in the FASB Accounting Standards Codification (ASC).

To revise the memorandum, click on each segment of underlined text below and select the needed correction, if any, from the list provided. If the underlined text is already correct in the context of the memorandum, select [Original text] from the list. Paragraphs may contain more than one segment of underlined text to be considered for correction.

Apex Corporation**Year ended December 31, year 7****Property, plant and equipment memorandum**

This memorandum discusses the accounting treatments for significant year 7 events and transactions related to property, plant and equipment.

Impairment of a manufacturing facility:

In March, year 7, a competitor introduced a new, directly competing product, which resulted in a significant decline in the company's revenues and a decline in its manufacturing capacity needs. The company previously used two manufacturing facilities, but as a result of the decline in demand for its product, the company's second manufacturing facility has been left largely unused since October 1, year 7. The company is preparing to repurpose the facility in year 8 to manufacture alternative products and plans to sell the facility in year 15. Accordingly, the company needs to evaluate the \$1,238,000 carrying amount of the facility as of December 31, year 7. As a result of the evaluation, the company concluded that the carrying value of the facility is not recoverable. The company estimated the fair value of the manufacturing facility using an income approach. The company should recognize a year 7 impairment loss of \$7,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value. In accordance with FASB ASC 360-10-45-15, the impairment loss should be recognized in income from discontinued operations before income taxes.

Land purchase:

On September 30, year 7, the company purchased land, which was paid in full with cash. The company will build a new facility on the land. The costs associated with the purchase of the land are included in the letter from the company's attorney. The company should capitalize \$520,800 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.

Exchange transaction:

On December 31, year 7, the company exchanged a used truck and \$2,500 in cash for a new truck with a fair value of \$18,000. The used truck had a carrying amount of \$14,000, and the company concluded that the exchange lacked commercial substance. The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-6 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered. 

Sale of corporate facility:

On December 31, year 7, the company committed to sell one of its corporate facilities with a fair value of \$200,000 and a carrying amount of \$190,000. The company's management will accept any offer between \$195,000 and \$210,000. The company plans to start actively marketing the sale of the land in May, year 8. The company will continue to use the facility until a buyer is identified. In accordance with FASB ASC 360-10-45-14, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met. 

Response 1

manufacturing facility using an income approach. The company should recognize a year 7 impairment loss of \$7,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value. 

Choose an option below 

- ☐ [Original text] The company should recognize a year 7 impairment loss of \$7,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.
 - ☐ The company should recognize a year 7 impairment loss of \$500,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the present value of the future cash flows.
 - ☐ The company should recognize a year 7 impairment loss of \$738,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.
 - ☐ The company should recognize a year 7 impairment loss of \$7,000 because FASB ASC 360-10-35-40 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.
 - ☐ The company should recognize a year 7 impairment loss of \$500,000 because FASB ASC 360-10-35-40 indicates that an impairment loss is required to be measured as the present value of the future cash flows.
 - ☐ The company should recognize a year 7 impairment loss of \$738,000 because FASB ASC 360-10-35-40 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.
- 

RESET

CANCEL

ACCEPT

Key

manufacturing facility using an income approach. **The company should recognize a year 7 impairment loss of \$738,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.** ✓

- ☐ The company should recognize a year 7 impairment loss of \$500,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the present value of the future cash flows.
- ☒ The company should recognize a year 7 impairment loss of \$738,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.
- ☐ The company should recognize a year 7 impairment loss of \$7,000 because FASB ASC 360-10-35-40 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.
- ☐ The company should recognize a year 7 impairment loss of \$500,000 because FASB ASC 360-10-35-40 indicates that an impairment loss is required to be measured as the present value of the future cash flows.
- ☐ The company should recognize a year 7 impairment loss of \$738,000 because FASB ASC 360-10-35-40 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.

RESET

CANCEL

ACCEPT

... manufacturing facility using an income approach. **The company should recognize a year 7 impairment loss of \$738,000 because FASB ASC 360-10-35-17 indicates that an impairment loss is required to be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.**

Guidance:

FASB ASC 360-10-35-17: Measurement of an impairment loss

An impairment loss shall be recognized only if the carrying amount of a long-lived asset (asset group) is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset (asset group) is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset (asset group). That assessment shall be based on the carrying amount of the asset (asset group) at the date it is tested for recoverability, whether in use (see paragraph 360-10-35-33) or under development (see paragraph 360-10-35-34). *An impairment loss shall be measured as the amount by which the carrying amount of a long-lived asset (asset group) exceeds its fair value.*

Impairment of long-lived assets held for use occurs when the carrying amount of the asset (ie, manufacturing facility) is not recoverable and a write-off is needed. The process for determining an impairment loss is as follows:

- **Review for a possible impairment.** In this case, Apex Corporation performed a review of the facility's carrying value as of December 31, year 7 and determined that there was a possible impairment.
- **Apply recoverability test.** If the sum of the undiscounted cash flows expected from the use and eventual disposition of the asset is less than the asset's carrying value, an impairment has occurred. In the *Exhibit 1: Cash Flow Analysis of the Manufacturing Facility*, the facility's undiscounted net cash

flow is \$1,231,000. This is less than the December 31, year 7 carrying value of \$1,238,000, indicating an impairment.

- **Calculate the impairment loss.** The loss is the amount by which the facility's carrying amount exceeds its fair value. Apex uses the income approach to determine the facility's fair value. This approach converts future cash flows or earnings into a single discounted present value amount. In the *Exhibit 1: Cash Flow Analysis of the Manufacturing Facility*, the facility's present value of net cash flows discounted at 8% is \$500,000. Using this amount as the fair value, the amount of **impairment loss is \$738,000** (\$1,238,000 carrying value – \$500,000 fair value).

Response 2

value. In accordance with FASB ASC 360-10-45-15, the impairment loss should be recognized in income from discontinued operations before income taxes. 

Choose an option below

- ☐ [Original text] 360-10-45-15, the impairment loss should be recognized in income from discontinued operations before income taxes.
- ☐ 360-10-45-4, the impairment loss should be recognized in income from continuing operations before income taxes.
- ☐ 360-10-45-4, the impairment loss should be recognized in income from discontinued operations before income taxes.
- ☐ 360-10-45-5, the impairment loss should be recognized in income from continuing operations before income taxes.
- ☐ 360-10-45-5, the impairment loss should be recognized in income from discontinued operations before income taxes.
- ☐ 360-10-45-15, the impairment loss should be recognized in income from continuing operations before income taxes.

RESET

CANCEL

ACCEPT

Key

value. In accordance with FASB ASC **360-10-45-4**, the impairment loss should be recognized in income from continuing operations before income taxes. ✓

Choose an option below

- ☐ [Original text] 360-10-45-15, the impairment loss should be recognized in income from discontinued operations before income taxes.
- ☒ 360-10-45-4, the impairment loss should be recognized in income from continuing operations before income taxes.
- ☐ 360-10-45-4, the impairment loss should be recognized in income from discontinued operations before income taxes.
- ☐ 360-10-45-5, the impairment loss should be recognized in income from continuing operations before income taxes.
- ☐ 360-10-45-5, the impairment loss should be recognized in income from discontinued operations before income taxes.
- ☐ 360-10-45-15, the impairment loss should be recognized in income from continuing operations before income taxes.

RESET

CANCEL

ACCEPT

... In accordance with FASB ASC **360-10-45-4**, the impairment loss should be recognized in income from continuing operations before income taxes.

Guidance:

FASB ASC 360-10-45-4: Presentation of impairment loss for long-lived assets to be held and used

An impairment loss recognized for a long-lived asset (asset group) to be held and used shall be included in income from continuing operations before income taxes in the income statement of a business entity. If a subtotal such as income from operations is presented, it shall include the amount of that loss.

Apex is planning to use the facility to manufacture alternative products until the planned sale in year 15. The \$738,000 impairment loss on the manufacturing facility (calculated in response 1) is recognized in income from continuing operations before income taxes when the asset is held for use.

Response 3

letter from the company's attorney. The company should capitalize \$520,800 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.

Choose an option below

- ☐ [Original text] The company should capitalize \$520,800 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$511,000 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$519,700 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$511,000 to land in accordance with FASB ASC 360-10-35-4, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$517,500 to land in accordance with FASB ASC 360-10-35-4, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$512,100 to land in accordance with FASB ASC 360-10-35-21, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.

RESET

CANCEL

ACCEPT

Key

letter from the company's attorney. **The company should capitalize \$519,700 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.** ✓

Choose an option below

- ☐ [Original text] The company should capitalize \$520,800 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$511,000 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☒ The company should capitalize \$519,700 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$511,000 to land in accordance with FASB ASC 360-10-35-4, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.
- ☐ The company should capitalize \$517,500 to land in accordance with FASB ASC 360-10-35-4,

RESET

CANCEL

ACCEPT

...letter from the company's attorney. **The company should capitalize \$519,700 to land in accordance with FASB ASC 360-10-30-1, which indicates that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use.**

Guidance:

FASB ASC 360-10-30-1: Historical cost including interest

Paragraph 835-20-05-1 states that the historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use. As indicated in that paragraph, if an asset requires a period of time in which to carry out the activities necessary to bring it to that condition and location, the interest cost incurred during that period as a result of expenditures for the asset is a part of the historical cost of acquiring the asset.

Acquisition costs, which are capitalized as part of an asset's cost, include not only the purchase price, but also costs associated with obtaining and preparing the asset for its intended use (eg, legal fees, delinquent taxes). The cost of land also includes surveying, clearing, grading, and demolition of old building less any proceeds from the sale of scrap materials.

In the *Exhibit 2: Attorney Letter* summarizes the September 30, year 7 land purchase. Apex should capitalize \$519,700 as calculated below.

Purchase price	\$500,000
Closing costs	6,000
Transfer tax	5,000
Delinquent property taxes	2,200

Cost to remove old building	8,000
Less: proceeds from sale of salvage materials from old building	<u>(1,500)</u>
Total	\$519,700

Current year property taxes are not capitalized. Property taxes are an ongoing cost of using the land that are expensed in the period incurred. The cost is matched with the benefit associated with using the land.

Response 4

the exchange lacked commercial substance. The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-6 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered. 

Choose an option below

- ☐ [Original text] The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-6 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered.
- ☐ The company should initially capitalize \$14,000 for the new truck because FASB ASC 845-10-30-3 requires a nonmonetary exchange to be measured based on the recorded amount of the nonmonetary asset relinquished.
- ☐ The company should initially capitalize \$14,000 for the new truck because FASB ASC 845-10-30-6 requires a nonmonetary exchange to be measured based on the recorded amount of the nonmonetary asset relinquished.
- ☐ The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-1 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered.
- ☐ The company should initially capitalize \$18,000 for the new truck because FASB ASC 845-10-30-1 requires an entity to recognize an asset received at its fair value and recognize a gain or loss on the nonmonetary asset surrendered.
- ☐ The company should initially capitalize \$18,000 for the new truck because FASB ASC 845-10-30-3 requires an entity to recognize an asset received at its fair value and to recognize a gain or loss on the nonmonetary asset surrendered.

RESET

CANCEL

ACCEPT

Key

the exchange lacked commercial substance. **The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-6 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered.** ✓

Choose an option below

- ☒ [Original text] The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-6 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered.
- ☐ The company should initially capitalize \$14,000 for the new truck because FASB ASC 845-10-30-3 requires a nonmonetary exchange to be measured based on the recorded amount of the nonmonetary asset relinquished.
- ☐ The company should initially capitalize \$14,000 for the new truck because FASB ASC 845-10-30-6 requires a nonmonetary exchange to be measured based on the recorded amount of the nonmonetary asset relinquished.
- ☐ The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-1 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered.
- ☐ The company should initially capitalize \$18,000 for the new truck because FASB ASC 845-10-30-1

RESET

CANCEL

ACCEPT

...the exchange lacked commercial substance. **The company should initially capitalize \$16,500 for the new truck because FASB ASC 845-10-30-6 requires an entity to recognize an asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered.**

Guidance:

FASB ASC 845-10-30-6: Nonmonetary transactions

The exchanges of nonmonetary assets that would otherwise be based on recorded amounts (see paragraph 845-10-30-3) may include an amount of monetary consideration. The recipient of the monetary consideration has realized gain on the exchange to the extent that the amount of the monetary receipt exceeds a proportionate share of the recorded amount of the asset surrendered. The portion of the cost applicable to the realized amount shall be based on the ratio of the monetary consideration to the total consideration received (monetary consideration plus the estimated fair value of the nonmonetary asset received) or, if more clearly evident, the fair value of the nonmonetary asset transferred. The entity paying the monetary consideration shall not recognize any gain on a transaction covered in paragraph 845-10-30-3 but shall record the asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered. If a loss is indicated by the terms of a transaction described in this paragraph or in that paragraph, the entire indicated loss on the exchange shall be recognized.

A nonmonetary exchange happens when two entities swap nonfinancial assets (eg, truck). Generally, these transactions have commercial substance (ie, risk, timing, and/or cash flows are affected by the change) and are treated as two unrelated transactions recorded at fair value.

However, some nonmonetary exchanges lack commercial substance (ie, cash flows are expected to be substantially unchanged as a result of the exchange). These exchanges are recorded using the carryover basis (ie, book value, adjusted for the cash paid/received) instead of fair value.

On December 31, year 7, Apex exchanged a used truck with a carrying amount of \$14,000 and \$2,500 cash for a new truck with a fair value of \$18,000. There is no fair value available for the used truck. Because Apex

concluded that the exchange lacked commercial substance, the used truck's carryover basis is used to record the exchange. Apex capitalizes the new truck as \$16,500 (\$14,000 used truck carrying value + \$2,500 cash paid).

Response 5

The company will continue to use the facility until a buyer is identified. In accordance with FASB ASC 360-10-45-14, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met. 

Choose an option below

- ☐ [Original text] 360-10-45-14, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.
- ☐ 360-10-45-14, the facility is prohibited from being classified as held-and-used under property, plant and equipment and must be classified as held-for-sale because all held-for-sale criteria are met.
- ☐ 360-10-45-9, the facility is prohibited from being classified as held-and-used under property, plant and equipment and must be classified as held-for-sale because all held-for-sale criteria are met.
- ☐ 360-10-45-9, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.
- ☐ 360-10-50-3, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.
- ☐ 360-10-50-3, the facility is prohibited from being classified as held-and-used under property, plant and equipment and must be classified as held-for-sale because all held-for-sale criteria are met.

RESET

CANCEL

ACCEPT

Key

The company will continue to use the facility until a buyer is identified. In accordance with FASB ASC **360-10-45-9**, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met. ✓

Choose an option below

- ☐ [Original text] 360-10-45-14, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.
- ☐ 360-10-45-14, the facility is prohibited from being classified as held-and-used under property, plant and equipment and must be classified as held-for-sale because all held-for-sale criteria are met.
- ☐ 360-10-45-9, the facility is prohibited from being classified as held-and-used under property, plant and equipment and must be classified as held-for-sale because all held-for-sale criteria are met.
- ☒ 360-10-45-9, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.
- ☐ 360-10-50-3, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.

RESET

CANCEL

ACCEPT

... The company will continue to use the facility until a buyer is identified. In accordance with FASB ASC **360-10-45-9**, the facility is prohibited from being classified as held-for-sale and must be classified as held-and-used under property, plant and equipment because not all held-for-sale criteria are met.

Guidance:

FASB ASC 360-10-45-9: Initial criteria for classification as held for sale

A long-lived asset (disposal group) to be sold shall be classified as held for sale in the period in which all of the following criteria are met:

- a. Management, having the authority to approve the action, commits to a plan to sell the asset (disposal group).
- b. The asset (disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (disposal groups). (See Examples 5 through 7 [paragraphs 360-10-55-37 through 55-41], which illustrate when that criterion would be met.)
- c. An active program to locate a buyer and other actions required to complete the plan to sell the asset (disposal group) have been initiated.
- d. The sale of the asset (disposal group) is probable, and transfer of the asset (disposal group) is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 360-10-45-11. (See Example 8 [paragraph 360-10-55-43], which illustrates when that criterion would be met.) The term probable refers to a future sale that is likely to occur.

	e. The asset (disposal group) is being actively marketed for sale at a price that is reasonable in relation to its current fair value. The price at which a long-lived asset (disposal group) is being marketed is indicative of whether the entity currently has the intent and ability to sell the asset (disposal group). A market price that is reasonable in relation to fair value indicates that the asset (disposal group) is available for immediate sale, whereas a market price in excess of fair value indicates that the asset (disposal group) is not available for immediate sale. f. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.
Long-lived assets are generally intended to be held and used in an entity's business. When a company plans on selling a long-lived asset, the asset is accounted for as held for sale if all of the following criteria are met. • Management commits to a plan to sell the asset. • The asset is available for immediate sale in its present condition. • An active program to locate a buyer and complete the sale have been initiated. • The sale is probable within one year. • The asset is being actively marketed at a reasonable price in relation to its fair value. • It is unlikely the plan to sell will be changed or withdrawn. Apex committed to sell one of its corporate facilities on December 31, year 7. Apex will begin actively marketing the sale in May of year 8. Because it is not currently actively marketing the facility, not all of the criteria are met for Apex to change the asset classification to held-for-sale.	

Exhibits Information

Exhibits included in this item

1. Cash Flow Analysis of Manufacturing Facility
2. **Attorney Letter**

Exhibit for Item: 508395

Exhibit 1: Cash Flow Analysis of Manufacturing Facility

USD (in 000's)	Year 8	Year 9	Year 10	Year 11	Year 12	Year 13	Year 14	Year 15	Total
Undiscounted net cash flow	(650)	2	75	113	171	142	167	1,211	1,231
Present value of net cash flow at 8%	(602)	2	60	83	116	90	97	654	500

Exhibit for Item: **508395**

Exhibit 2: Attorney Letter

Gordon & Gordon, Attorneys-at-Law
4500 Main Street
Springwell, GA 30089
265-555-1111

December 31, year 7 Dear

Controller:

Apex Corp. closed on the purchase of new land on September 30, year 7. Below is a summary of the costs that Apex has incurred related to this transaction:

• Purchase price for land	\$500,000
• Closing costs	6,000
• Transfer tax	5,000
• Property tax for fourth quarter of year 7	1,100
• Delinquent property taxes that the prior owner left unpaid	2,200
• Cost to remove an old building on the land	8,000
• Proceeds from the sale of materials salvaged from the old building	1,500

It has been our pleasure to assist you in this land purchase. Very

truly yours,

J.P. Gordon

Gordon & Gordon, Attorneys-at-Law

Blueprint Information

CSO: 002.004.000

Skill: Analysis

Representative task: Reconcile and investigative differences between the subledger and general ledger for property, plant and equipment to determine whether an adjustment is necessary