

CHAPTER 15(14): FINANCIAL STATEMENT ANALYSIS

Test Bank for Managerial Accounting 13th Edition by Warren Reeve and Duchac 1285868806 9781285868806

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1. Comparable financial statements are designed to compare the financial statements of two or more corporations.

- a. True
- b. False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSAP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

2. In horizontal analysis, the current year is the base year.

- a. True
- b. False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSAP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

3. On a common-sized income statement, all items are stated as a percent of total assets or equities at year-end.

- a. True
- b. False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSAP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

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4. The analysis of increases and decreases in the amount and percentage of comparative financial statement items is referred to as horizontal analysis.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

5. A 15% change in sales will result in a 15% change in net income.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

6. A financial statement showing each item on the statement as a percentage of one key item on the statement is called a common-sized financial statement.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
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7. The relationship of each asset item as a percent of total assets is an example of vertical analysis.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

8. Vertical analysis refers to comparing the financial statements of a single company over several years.
- True
 - False

ANSWER: False
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

9. In a common-sized income statement, each item is expressed as a percentage of net income.
- True
 - False

ANSWER: False
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

10. In the vertical analysis of a balance sheet, the base for current liabilities is total liabilities.
- True
 - False

ANSWER: False
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01
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11. Using vertical analysis of the income statement, a company's net income as a percentage of sales is 15%; therefore, the cost of goods sold as a percentage of sales must be 85%.
- True
 - False

ANSWER: False

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

12. In the vertical analysis of an income statement, each item is generally stated as a percentage of total assets.
- True
 - False

ANSWER: False

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

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13. Factors that reflect the ability of a business to pay its debts and earn a reasonable amount of income are referred to as solvency and profitability.
- True
 - False

ANSWER: True

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

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14. The excess of current assets over current liabilities is referred to as working capital.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

15. Dollar amounts of working capital are difficult to assess when comparing companies of different sizes or in comparing such amounts with industry figures.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

16. Using measures to assess a business's ability to pay its current liabilities is called current position analysis.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

17. Current position analysis measures a company's ability to pay its current liabilities.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02
ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

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18. An advantage of the current ratio is that it considers the makeup of the current assets.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

19. If two companies have the same current ratio, their ability to pay short-term debt is the same.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

20. The ratio of the sum of cash, receivables, and marketable securities to current liabilities is referred to as the current ratio.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

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21. A balance sheet shows cash, \$75,000; marketable securities, \$115,000; receivables, \$150,000; and inventories, \$222,500. Current liabilities are \$225,000. The current ratio is 2.5.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

22. If a firm has a current ratio of 2, the subsequent receipt of a 60-day note receivable on account will cause the ratio to decrease.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis

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BUSPROG: Analytic

23. If a firm has a quick ratio of 1, the subsequent payment of an account payable will cause the ratio to increase.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

24. Solvency analysis focuses on the ability of a business to pay its current and noncurrent liabilities.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

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BUSPROG: Analytic

25. If the accounts receivable turnover for the current year has decreased when compared with the ratio for the preceding year, there has been an acceleration in the collection of receivables.

- True
- False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

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BUSPROG: Analytic

26. An increase in the accounts receivable turnover may be due to an improvement in the collection of receivables or to a change in the granting of credit and/or in collection practices.

- True
- False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

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BUSPROG: Analytic

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27. The number of days' sales in receivables is one means of expressing the relationship between average daily sales and accounts receivable.
- True
 - False

ANSWER: True

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

28. A firm selling food should have higher inventory turnover rate than a firm selling office furniture.
- True
 - False

ANSWER: True

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.BB.07 - Critical Thinking
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

29. The number of days' sales in inventory is one means of expressing the relationship between the cost of goods sold and inventory.
- True
 - False

ANSWER: True

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

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30. Assuming that the quantities of inventory on hand during the current year were sufficient to meet all demands for sales, a decrease in the inventory turnover for the current year when compared with the turnover for the preceding year indicates an improvement in inventory management.
- True
 - False

ANSWER: False

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

31. The ratio of fixed assets to long-term liabilities provides a measure of a firm's ability to pay dividends.
- True
 - False

ANSWER: False

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

32. A decrease in the ratio of liabilities to stockholders' equity indicates an improvement in the margin of safety for creditors.
- True
 - False

ANSWER: True

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

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33. In computing the ratio of sales to assets, long-term investments are excluded from average total assets.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

34. The rate earned on total assets measures the profitability of total assets, without considering how the assets are financed.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

35. In computing the rate earned on total assets, interest expense is subtracted from net income before dividing by average total assets.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

36. The denominator of the rate of return on total assets ratio is the average total assets.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

37. When the rate of return on total assets ratio is greater than the rate of return on common stockholders' equity ratio, the management of the company has effectively used leverage.

- True
- False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

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BUSPROG: Analytic

38. When computing the rate earned on total common stockholders' equity, preferred stock dividends are subtracted from net income.

- True
- False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

39. If a company has issued only one class of stock, the earnings per share are determined by dividing net income plus interest expense by the number of shares outstanding.
- a. True
 - b. False

ANSWER: False

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

40. The ratio of the market price per share of common stock on a specific date to the annual earnings per share is referred to as the price-earnings ratio.
- a. True
 - b. False

ANSWER: True

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

41. The dividend yield rate is equal to the dividends per share divided by the par value per share of common stock.
- a. True
 - b. False

ANSWER: False

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

42. Comparing dividends per share to earnings per share indicates the extent to which the corporation is retaining its earnings for use in operations.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

43. When you are interpreting financial ratios, it is useful to compare a company's ratios to some form of standard.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

44. Ratios and various other analytical measures are **not** a substitute for sound judgment, nor do they provide definitive guides for action.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

45. Interpreting financial analysis should be considered in light of conditions peculiar to the industry and the general economic conditions.
- a. True
 - b. False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

46. A company can use comparisons of its financial data to the data of other companies and industry averages to evaluate its position.
- a. True
 - b. False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

47. The effects of differences in accounting methods are of little importance when analyzing comparable data from competing businesses.
- a. True
 - b. False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

48. The report on internal control required by the Sarbanes-Oxley Act of 2002 may be prepared by either management or the company's auditors.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSAPPC.10 - Internal Control
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

49. The auditor's report is where the auditor certifies that the financial statements are correct and accurate.
- True
 - False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSAPPC.01 - Purpose
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

50. In a company's annual report, the section called management discussion and analysis provides critical information in interpreting the financial statements and assessing the future of the company.
- True
 - False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSAPPC.01 - Purpose
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

51. A clean audit opinion is the same as a qualified audit opinion.

- a. True
- b. False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSB.APC.01 - Purpose
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

52. Unusual items affecting the current period's income statement consist of changes in accounting principles and discontinued operations.

- a. True
- b. False

ANSWER: False

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

53. When a corporation discontinues a segment of its operations at a loss, the loss should be reported as a separate item after income from continuing operations on the income statement.

- a. True
- b. False

ANSWER: True

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
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BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

54. An extraordinary item must be either unusual in nature or infrequent in occurrence.
- True
 - False

ANSWER: False
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP
ACCREDITING STANDARDS: ACCT.ACBSAPPC.02 - GAAP
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

55. Reporting unusual items separately on the income statement allows investors to isolate the effects of these items on income and cash flows.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP
ACCREDITING STANDARDS: ACCT.ACBSAPPC.02 - GAAP
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

56. When a corporation discontinues a segment of its operations at a loss, the loss should be reported as a separate item before income from continuing operations on the income statement.
- True
 - False

ANSWER: False
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP
ACCREDITING STANDARDS: ACCT.ACBSAPPC.02 - GAAP
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

57. Unusual items affecting the prior period's income statement consist of errors and changes in accounting principles.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP
ACCREDITING STANDARDS: ACCT.ACBSAPPC.02 - GAAP
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

58. Earnings per share amounts are only required to be presented for income from continuing operations and net income on the face of the statement.
- True
 - False

ANSWER: True
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP
ACCREDITING STANDARDS: ACCT.ACBSAPPC.02 - GAAP
ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

59. The percentage analysis of increases and decreases in individual items in comparative financial statements is called
- vertical analysis
 - solvency analysis
 - profitability analysis
 - horizontal analysis

ANSWER: d
DIFFICULTY: Easy
Bloom's: Remembering
LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01
ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

60. Which of the following is the most useful in analyzing companies of different sizes?
- comparative statements
 - common-sized financial statements
 - price-level accounting
 - audit report

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

61. The percent of fixed assets to total assets is an example of
- vertical analysis
 - solvency analysis
 - profitability analysis
 - horizontal analysis

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

62. What type of analysis is indicated by the following?

	<u>Current Year</u>	<u>Preceding Year</u>	<u>Increase (Decrease)</u>	
			<u>Amount</u>	<u>Percent</u>
Current assets	\$ 430,000	\$ 500,000	\$ (70,000)	(14%)
Fixed assets	1,740,000	1,500,000	240,000	16%

- a. vertical analysis
- b. horizontal analysis
- c. liquidity analysis
- d. common-size analysis

ANSWER: b

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

63. An analysis in which all the components of an income statement are expressed as a percentage of sales is a

- a. vertical analysis
- b. horizontal analysis
- c. liquidity analysis
- d. solvency analysis

ANSWER: a

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

64. A balance sheet that displays only component percentages is a

- a. trend balance sheet
- b. comparative balance sheet
- c. condensed balance sheet
- d. common-sized balance sheet

ANSWER: d

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

65. One reason that a common-sized statement is a useful tool in financial analysis is that it enables the user to
- judge the relative potential of two companies of similar size in different industries
 - determine which companies in a single industry are of the same value
 - determine which companies in a single industry are of the same size
 - make a better comparison of two companies of different sizes in the same industry

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

66. Assume the following sales data for a company:

Current year	\$325,000
Preceding year	250,000

What is the percentage increase in sales from the preceding year to the current year?

- 70%
- 76.9%
- 30%
- 50%

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

67. On a common-sized balance sheet, 100% is

- total property, plant, and equipment
- total current assets
- total liabilities
- total assets

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

68. In a common-sized income statement, 100% is the
- net cost of goods sold
 - net income
 - gross profit
 - sales

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

69. Horizontal analysis is a technique for evaluating financial statement data
- for one period of time
 - over a period of time
 - on a certain date
 - as it may appear in the future

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

70. Horizontal analysis of comparative financial statements includes
- development of common-sized statements
 - calculation of liquidity ratios
 - calculation of dollar amount changes and percentage changes from the previous to the current year
 - evaluation of each component in a financial statement to a total within the statement

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

71. In horizontal analysis, each item is expressed as a percentage of the
- base year figure
 - retained earnings figure
 - total assets figure
 - net income figure

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

72. Assume the following sales data for a company:

Current year	\$1,025,000
Preceding year	820,000

What is the percentage increase in sales from the preceding year to the current year?

- 100%
- 25%
- 125%
- 75%

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

73. Income statement information for Sadie Company is below:

Sales	\$175,000
Cost of goods sold	<u>115,000</u>
Gross profit	<u>\$ 60,000</u>

Using vertical analysis of the income statement for Sadie Company, determine the gross profit margin.

- a. 100%
- b. 66%
- c. 34%
- d. 29%

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

74. In a vertical analysis, the base for cost of goods sold is

- a. total selling expenses
- b. sales
- c. total expenses
- d. gross profit

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

75. Percentage analyses, ratios, turnovers, and other measures of financial position and operating results are
- a substitute for sound judgment
 - useful analytical measures
 - enough information for analysis; industry information is not needed
 - unnecessary for analysis, but reaction is better

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01
ACCT.WARD.16.17-02 - 17-02
ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

76. The relationship of \$325,000 to \$125,000, expressed as a ratio, is
- 2.0
 - 2.6
 - 2.5
 - 0.45

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

77. The ability of a business to pay its debts as they come due and to earn a reasonable net income is
- solvency and leverage
 - solvency and profitability
 - solvency and liquidity
 - solvency and equity

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

Accounts payable	\$ 40,000
Accounts receivable	65,000
Accrued liabilities	7,000
Cash	30,000
Intangible assets	40,000
Inventory	72,000
Long-term investments	110,000
Long-term liabilities	75,000
Marketable securities	36,000
Notes payable (short-term)	30,000
Property, plant, and equipment	625,000
Prepaid expenses	2,000

78. Based on the above data, what is the amount of quick assets?

- a. \$205,000
- b. \$203,000
- c. \$131,000
- d. \$66,000

ANSWER: c

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

79. Based on the above data, what is the amount of working capital?

- a. \$238,000
- b. \$128,000
- c. \$168,000
- d. \$203,000

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

80. Based on the above data, what is the quick ratio, rounded to one decimal point?

- a. 2.7
- b. 2.6
- c. 1.7
- d. 0.9

ANSWER: c

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

81. A company with working capital of \$720,000 and a current ratio of 2.2 pays a \$125,000 short-term liability. The amount of working capital immediately after payment is

- a. \$845,000
- b. \$595,000
- c. \$720,000
- d. \$125,000

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

82. Which of the following measures a company's ability to pay its current liabilities?

- a. earnings per share
- b. inventory turnover
- c. current ratio
- d. number of times interest charges earned

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

83. Which of the following is **not** included in the computation of the quick ratio?
- inventory
 - marketable securities
 - accounts receivable
 - cash

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

84. The numerator in calculating the accounts receivable turnover is
- total assets
 - sales
 - accounts receivable at year-end
 - average accounts receivable

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSA.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

85. Based on the following data, what is the accounts receivable turnover?

Sales on account during year	\$700,000
Cost of merchandise sold during year	270,000
Accounts receivable, beginning of year	45,000
Accounts receivable, end of year	35,000
Inventory, beginning of year	90,000
Inventory, end of year	110,000

- a. 17.5
- b. 2.6
- c. 20.0
- d. 15.5

ANSWER:

a

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

86. An acceleration in the collection of receivables will tend to cause the accounts receivable turnover to

- a. decrease
- b. remain the same
- c. either increase or decrease
- d. increase

ANSWER:

d

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

87. Based on the following data for the current year, what is the number of days' sales in accounts receivable?

Sales on account during year	\$584,000
Cost of merchandise sold during year	300,000
Accounts receivable, beginning of year	45,000
Accounts receivable, end of year	35,000
Inventory, beginning of year	90,000
Inventory, end of year	110,000

- a. 7.3
- b. 2.5
- c. 14.6
- d. 25

ANSWER: d

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

88. Based on the following data for the current year, what is the inventory turnover?

Sales on account during year	\$700,000
Cost of merchandise sold during year	270,000
Accounts receivable, beginning of year	45,000
Accounts receivable, end of year	35,000
Inventory, beginning of year	90,000
Inventory, end of year	110,000

- a. 2.7
- b. 9.7
- c. 2.5
- d. 3.0

ANSWER: a

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

89. Based on the following data for the current year, what is the number of days' sales in inventory?

Sales on account during year	\$1,204,500
Cost of merchandise sold during year	657,000
Accounts receivable, beginning of year	75,000
Accounts receivable, end of year	85,000
Inventory, beginning of year	85,600
Inventory, end of year	98,600

- a. 51.2
- b. 44.4
- c. 6.5
- d. 7.5

ANSWER:

a

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

90. Which of the following ratios provides a solvency measure that shows the margin of safety of bondholders and also gives an indication of the potential ability of the business to borrow additional funds on a long-term basis?

- a. ratio of fixed assets to long-term liabilities
- b. ratio of net sales to assets
- c. number of days' sales in receivables
- d. rate earned on stockholders' equity

ANSWER:

a

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

91. The number of times interest expense is earned is computed as
- net income plus interest expense, divided by interest expense
 - income before income tax plus interest expense, divided by interest expense
 - net income divided by interest expense
 - income before income tax divided by interest expense

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

92. Balance sheet and income statement data indicate the following:

Bonds payable, 10% (due in two years)	\$1,000,000
Preferred 5% stock, \$100 par (no change during year)	300,000
Common stock, \$50 par (no change during year)	2,000,000
Income before income tax for year	550,000
Income tax for year	80,000
Common dividends paid	50,000
Preferred dividends paid	15,000

Based on the data presented above, what is the number of times bond interest charges were earned (round to one decimal point)?

- 1.5
- 6.4
- 6.5
- 5.5

ANSWER: c

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

93. The current ratio is
- used to evaluate a company's liquidity and short-term debt paying ability
 - a solvency measure that indicates the margin of safety of a bondholder
 - calculated by dividing current liabilities by current assets
 - calculated by subtracting current liabilities from current assets

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

94. A company with \$70,000 in current assets and \$50,000 in current liabilities pays a \$1,000 current liability. As a result of this transaction, the current ratio and working capital will
- both decrease
 - both increase
 - increase and remain the same, respectively
 - remain the same and decrease, respectively

ANSWER: c

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

95. Hsu Company reported the following on its income statement:

Income before income taxes	\$420,000
Income tax expense	<u>120,000</u>
Net income	<u>\$300,000</u>

Interest expense was \$80,000. Hsu Company's times interest earned is

- 8 times
- 6.25 times
- 5.25 times
- 5 times

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

96. Brock Company's financial information is listed below. Assume that all balance sheet amounts represent both average and ending balance figures and that all sales were on credit.

<u>Assets</u>	
Cash and short-term investments	\$ 0,000
Accounts receivable (net)	0,000
Inventory	5,000
Property, plant, and equipment	<u>15,000</u>
Total assets	<u>\$10,000</u>

<u>Liabilities and Stockholders' Equity</u>	
Current liabilities	\$ 60,000
Long-term liabilities	95,000
Stockholders' equity—Common	<u>155,000</u>
Total liabilities and stockholders' equity	<u>\$310,000</u>

<u>Income Statement</u>	
Sales	\$90,000
Cost of goods sold	<u>45,000</u>
Gross margin	\$45,000
Operating expenses	<u>20,000</u>
Net income	<u>\$25,000</u>

Number of shares of common stock	6,000
Market price of common stock	\$20

What is the current ratio?

- a. 1.42
- b. 0.78
- c. 1.58
- d. 0.67

ANSWER: c

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

Accounts payable	\$ 30,000
Accounts receivable	35,000
Accrued liabilities	7,000
Cash	25,000
Intangible assets	40,000
Inventory	72,000
Long-term investments	100,000
Long-term liabilities	75,000
Marketable securities	36,000
Notes payable (short-term)	20,000
Property, plant, and equipment	400,000
Prepaid expenses	2,000

97. Based on the above data, what is the amount of quick assets?

- a. \$168,000
- b. \$96,000
- c. \$60,000
- d. \$61,000

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

98. Based on the above data, what is the amount of working capital?

- a. \$213,000
- b. \$113,000
- c. \$153,000
- d. \$39,000

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSAPPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

99. Based on the above data, what is the quick ratio, rounded to one decimal point?

- a. 1.7
- b. 2.9
- c. 1.1
- d. 1.0

ANSWER: a

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSAPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

100. The tendency of the rate earned on stockholders' equity to vary disproportionately from the rate earned on total assets is

- a. leverage
- b. solvency
- c. yield
- d. quick assets

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSAPC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

The balance sheets at the end of each of the first two years of operations indicate the following:

	<u>Year 2</u>	<u>Year 1</u>
Total current assets	\$600,000	\$560,000
Total investments	60,000	40,000
Total property, plant, and equipment	900,000	700,000
Total current liabilities	125,000	65,000
Total long-term liabilities	350,000	250,000
Preferred 9% stock, \$100 par	100,000	100,000
Common stock, \$10 par	600,000	600,000
Paid-in capital in excess of par—Common stock	75,000	75,000
Retained earnings	310,000	210,000

Chapter 15(14): Financial Statement Analysis

101. If net income is \$150,000 and interest expense is \$20,000 for Year 2, what is the rate earned on total assets for the year?
- 10.4%
 - 11.9%
 - 10.5%
 - 8.4%

ANSWER:

b

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBS.PC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

102. If net income is \$150,000 and interest expense is \$20,000 for Year 2, what is the rate earned on stockholders' equity for Year 2?
- 6.9%
 - 14.5%
 - 16.4%
 - 13.8%

ANSWER:

c

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBS.PC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

103. If net income is \$250,000 and interest expense is \$30,000 for Year 2, what are the earnings per share on common stock for Year 2?
- \$4.16
 - \$4.32
 - \$4.02
 - \$2.49

ANSWER:

c

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBS.PC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

104. If net income is \$250,000 and interest expense is \$20,000 for Year 2, and the market price of common shares is \$30, what is the price-earnings ratio on common stock for Year 2? (Round intermediate calculation to two decimal places and final answers to one decimal place.)
- a. 7.5
 - b. 13.4
 - c. 12.1
 - d. 8.5

ANSWER: a

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

105. The numerator of the rate earned on common stockholders' equity ratio is
- a. net income
 - b. net income minus preferred dividends
 - c. income before income tax
 - d. operating income minus interest expense

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

106. The numerator of the rate earned on total assets ratio is
- a. net income
 - b. net income plus tax expense
 - c. net income plus interest expense
 - d. net income minus preferred dividends

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

107. The following information is available for Jase Company:

Market price per share of common stock	\$25.00
Earnings per share on common stock	\$1.25

Which of the following statements is correct?

- The price-earnings ratio is 20 and a share of common stock was selling for 20 times the amount of earnings per share at the end of the year.
- The price-earnings ratio is 5% and a share of common stock was selling for 5% more than the amount of earnings per share at the end of the year.
- The price-earnings ratio is 10 and a share of common stock was selling for 125 times the amount of earnings per share at the end of the year.
- The market price per share and the earnings per share are not statistically related to each other.

ANSWER: a

DIFFICULTY: Moderate
Bloom's: Applying

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

108. The following information is available for Meyer Company:

Dividends per share of common stock	\$1.80
Market price per share of common stock	\$30.00

Which of the following statements is correct?

- The dividend yield is 6.0%, which is of interest to investors seeking an increase in market price of their stocks.
- The dividend yield is 6.0%, which is of special interest to investors seeking to earn revenue on their investments.
- The dividend yield is 16.7%, which is of interest to bondholders.
- The dividend yield is 16.7% which is an important measure of solvency.

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Applying

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

109. The particular analytical measures chosen to analyze a company may be influenced by all of the following **except**
- industry type
 - capital structure
 - diversity of business operations
 - product quality or service effectiveness

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

110. Which of the following is **not** a characteristic evaluated in ratio analysis?
- liquidity
 - profitability
 - solvency
 - marketability

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

111. Short-term creditors are typically most interested in analyzing a company's
- marketability
 - profitability
 - operating results
 - solvency

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

112. A common measure of liquidity is
- the ratio of sales to assets
 - dividends per share of common stock
 - the accounts receivable turnover
 - the profit margin

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

113. Richards Corporation had net income of \$250,000 and paid dividends to common stockholders of \$50,000. It had 50,000 shares of common stock outstanding during the entire year. Richards Corporation's common stock is selling for \$35 per share. The price-earnings ratio is
- 7 times
 - 14 times
 - 2 times
 - 5 times

ANSWER: a

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

114. Leverage implies that a company
- contains debt financing
 - contains equity financing
 - has a high current ratio
 - has a high earnings per share

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

The following information pertains to Diane Company. Assume that all balance sheet amounts represent both average and ending balance figures and that all sales were on credit.

<u>Assets</u>	
Cash and short-term investments	\$ 0,000
Accounts receivable (net)	0,000
Inventory	5,000
Property, plant, and equipment	<u>85,000</u>
Total assets	<u>\$50,000</u>

<u>Liabilities and Stockholders' Equity</u>	
Current liabilities	\$ 5,000
Long-term liabilities	0,000
Stockholders' equity—Common	<u>35,000</u>
Total liabilities and stockholders' equity	<u>\$50,000</u>

<u>Income Statement</u>	
Sales	\$ 85,000
Cost of goods sold	<u>45,000</u>
Gross margin	\$ 40,000
Operating expenses	(15,000)
Interest expense	<u>(5,000)</u>
Net income	<u>\$ 20,000</u>

Number of shares of common stock outstanding	6,000
Market price of common stock	\$20
Total dividends paid	\$9,000
Cash provided by operations	\$30,000

115. What is the ratio of sales to total assets for Diane Company?

- a. 1.00
- b. 2.94
- c. 0.18
- d. 0.34

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

116. What is the rate earned on total assets for Diane Company?

- a. 10.0%
- b. 8.0%
- c. 0.10%
- d. 1.0%

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

117. What are the dividends per common share for Diane Company?

- a. \$20.00
- b. \$3.00
- c. \$0.67
- d. \$1.50

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

118. What is the dividend yield for Diane Company?

- a. 7.5%
- b. 0.75%
- c. 13.3%
- d. 1.3%

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

119. What is the rate earned on common stockholders' equity for Diane Company?

- a. 6.75%
- b. 14.8%
- c. 7.4%
- d. 13.5%

ANSWER: b

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.PC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

120. What is the price earnings ratio for Diane Company?

- a. 8.0 times
- b. 2.5 times
- c. 4.0 times
- d. 6.0 times

ANSWER: d

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBS.PC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

121. The following information pertains to Newman Company. Assume that all balance sheet amounts represent both average and ending balance figures and that all sales were on credit.

<u>Assets</u>	
Cash and short-term investments	\$ 40,000
Accounts receivable (net)	30,000
Inventory	25,000
Property, plant, and equipment	<u>215,000</u>
Total Assets	<u>\$310,000</u>

<u>Liabilities and Stockholders' Equity</u>	
Current liabilities	\$ 60,000
Long-term liabilities	95,000
Stockholders' equity—Common	<u>155,000</u>
Total liabilities and stockholders' equity	<u>\$310,000</u>

<u>Income Statement</u>	
Sales	\$90,000
Cost of goods sold	<u>45,000</u>
Gross margin	\$45,000
Operating expenses	<u>20,000</u>
Net income	<u>\$25,000</u>

Number of shares of common stock	6,000
Market price of common stock	\$40
Dividends per share	\$1.00
Cash provided by operations	\$40,000

What is the rate earned on total assets for this company?

- a. 8.1%
- b. 6.8%
- c. 10.5%
- d. 16.1%

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

122. The following information pertains to Dallas Company. Assume that all balance sheet amounts represent both average and ending balance figures and that all sales were on credit.

Assets	
Cash and short-term investments	\$ 40,000
Accounts receivable (net)	30,000
Inventory	25,000
Property, plant, and equipment	<u>280,000</u>
Total assets	<u>\$375,000</u>

Liabilities and Stockholders' Equity	
Current liabilities	\$ 0,000
Long-term liabilities	5,000
Stockholders' equity—Common	<u>20,000</u>
Total liabilities and stockholders' equity	<u>\$75,000</u>

Income Statement	
Sales	\$90,000
Cost of goods sold	<u>45,000</u>
Gross margin	\$45,000
Operating expenses	<u>15,000</u>
Net income	<u>\$30,000</u>

Number of shares of common stock	6,000
Market price of common stock	\$20
Dividends per share	\$1.00
Cash provided by operations	\$40,000

What is the rate earned on stockholders' equity?

- a. 7.3%
- b. 13.6%
- c. 20.5%
- d. 40.9%

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

123. A company reports the following:

Net income	\$160,000
Preferred dividends	\$10,000
Shares of common stock outstanding	20,000
Market price per share of common stock	\$35

The company's earnings per share on common stock is

- a. \$13.33
- b. \$8.50
- c. \$7.50
- d. \$35.00

ANSWER:

c

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

124. Corporate annual reports typically do **not** contain

- a. management discussion and analysis
- b. an SEC statement expressing an opinion
- c. accompanying notes
- d. an auditor's report

ANSWER:

b

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.20 - Accounting for Corporations

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

ACCT.AICPA.FN.04 - Reporting

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

125. The independent auditor's report
- describes which financial statements are covered by the audit
 - gives the auditor's opinion regarding the fairness of the financial statements
 - summarizes what the auditor did
 - states that the financial statements were presented on time

ANSWER: b

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSP.APC.01 - Purpose
ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

126. The purpose of an audit is to
- determine whether or not a company is a good investment
 - render an opinion on the fairness of the statements
 - determine whether or not a company complies with corporate social responsibility
 - determine whether or not a company is a good credit risk

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSP.APC.01 - Purpose
ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

127. Which of the following is required by the Sarbanes-Oxley Act?
- a price-earnings ratio
 - a report on internal control
 - a vertical analysis
 - a common-sized statement

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBSP.APC.10 - Internal Control
ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

128. All of the following are typically included in the management's discussion and analysis in annual reports **except**
- explanations of any significant changes between the current and prior years' financial statements
 - management's assessment of liquidity
 - journal entries
 - off-balance-sheet arrangements

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.20 - Accounting for Corporations
ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
ACCT.AICPA.FN.04 - Reporting
BUSPROG: Analytic

129. Which of the following would appear as an extraordinary item on the income statement?
- loss resulting from the sale of fixed assets
 - gain resulting from the disposal of a segment of the business
 - loss from land condemned for public use
 - liquidating dividend

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.02 - GAAP
ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

130. A loss on disposal of a segment would be reported in the income statement as a(n)
- administrative expense
 - other expense
 - deduction from income from continuing operations
 - selling expense

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBS.P.APC.02 - GAAP
ACCT.ACBS.P.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

131. An extraordinary item can result from
- a segment of the business being sold
 - corporate income tax being paid
 - a change from one accounting method to another acceptable accounting method
 - a transaction or event that is unusual and occurs infrequently

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

132. Which of the following is considered an unusual item affecting the prior period's income statement?
- a change in accounting principles
 - fixed asset impairments
 - an extraordinary item
 - discontinued operations

ANSWER: a

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

133. Which of the following should be classified as an extraordinary item on the income statement?
- gain on a sale of a long-term investment
 - loss due to discontinued operations
 - restructuring charges
 - loss resulting from an infrequent natural disaster

ANSWER: d

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

134. A loss due to a discontinued operation should be reported on the income statement
- above income from continuing operations
 - without related tax effect
 - below income from continuing operations
 - as an operating expense

ANSWER: c

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

135. A change from one acceptable accounting method to another is reported
- on the statement of retained earnings, as a correction to the beginning balance
 - on the income statement, below income from continuing operations
 - on the income statement, above income from continuing operations
 - through a retroactive restatement of prior-period earnings

ANSWER: d

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

136. Which of the following items should be classified as an extraordinary item on an income statement?
- gain on the retirement of a bond payable
 - loss from hurricane damage in Iowa
 - loss due to a discontinued operation in Colorado
 - selling treasury stock for more than the company paid for it

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

137. Which of the following items appear on the corporate income statement before income from continuing operations?
- cumulative effect of a change in accounting principle
 - income tax expense
 - extraordinary gain
 - loss on discontinued operations

ANSWER: b

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS: ACCT.ACBSB.APC.02 - GAAP
ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

138. Cash and accounts receivable for Adams Company are provided below:

	<u>Current Year</u>	<u>Prior Year</u>
Cash	\$70,000	\$50,000
Accounts receivable (net)	70,400	80,000

What is the amount and percentage of increase or decrease that would be shown with horizontal analysis?

ANSWER: Cash \$20,000 increase (\$70,000 – \$50,000) or 40%
Accounts receivable \$9,600 decrease (\$80,000 – \$70,400) or (12%)

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSB.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

139. The following items were taken from the financial statements of Tilden, Inc., over a three-year period:

Item	Year 3	Year 2	Year 1
Sales	\$360,000	\$335,000	\$290,000
Cost of goods sold	225,000	205,000	185,000
Gross profit	\$135,000	\$130,000	\$105,000

Compute the following for each of the above time periods.

(a) The amount and percentage change from Year 2 to Year 3.

(b) The amount and percentage change from Year 1 to Year 2.

Round percentages to one decimal place.

ANSWER:

	<u>(a) Year 3</u>		<u>(b) Year 2</u>	
	\$	Percent	\$	Percent
Sales	\$25,000	7.5%	\$45,000	15.5%
Cost of goods sold	20,000	9.8%	20,000	10.8%
Gross profit	\$ 5,000	3.8%	\$25,000	23.8%

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

140. Comparative information taken from the Friction Company's financial statements is shown below:

	<u>Year 2</u>	<u>Year 1</u>
(a) Notes receivable	\$ 10,000	\$ 0
(b) Accounts receivable	106,200	90,000
(c) Retained earnings	30,000	(40,000)
(d) Sales	654,000	600,000
(e) Operating expenses	160,000	200,000
(f) Income taxes payable	28,000	20,000

Using horizontal analysis, show the percentage change and direction (increase or decrease) from Year 1 to Year 2 with Year 1 as the base year.

ANSWER:

- (a) Base year is zero. Not possible to compute.
- (b) $\$16,200 \div \$90,000 = 18\%$ increase
- (c) Base year is negative. Not possible to compute.
- (d) $\$54,000 \div \$600,000 = 9\%$ increase
- (e) $\$40,000 \div \$200,000 = 20\%$ decrease
- (f) $\$8,000 \div \$20,000 = 40\%$ increase

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

141. Revenue and expense data for Young Technologies are as follows:

	Year 2	Year 1
Sales	\$500,000	\$440,000
Cost of goods sold	325,000	242,000
Selling expense	70,000	79,200
Administrative expenses	75,000	70,400
Income tax expense	10,500	16,400

- (a) Prepare an income statement in comparative form, stating each item for both years as an amount and as a percent of sales. Round to the nearest whole percent.
- (b) Comment on the significant changes disclosed by the comparative income statement.

ANSWER:

(a)

Young Technologies Inc.
Comparative Income Statement
For the Years Ended December 31, Year 2 and Year 1

	<u>Year 2</u> <u>Amount</u>	<u>Year 2</u> <u>Percent</u>	<u>Year 1</u> <u>Amount</u>	<u>Year 1</u> <u>Percent</u>
Sales	\$500,000	100%	\$440,000	100%
Cost of goods sold	325,000	65%	242,000	55%
Gross profit	\$175,000	35%	\$198,000	45%
Selling expenses	70,000	14%	79,200	18%
Administrative expenses	75,000	15%	70,400	16%
Total expenses	\$145,000	29%	\$149,600	34%
Income from operations	30,000	6%	48,400	11%
Income tax expense	10,500	2%	16,400	4%
Net income	\$ 19,500	4%	\$ 32,000	7%

- (b) The vertical analysis indicates that the cost of goods sold as a percent of sales increased by 10% (65% vs. 55%) between the two years. Selling and administrative expense as a percentage of sales decreased by 5% and income tax expense decreased by 2%. Overall net income as a percent of sales dropped by 3%.

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

142. Cash and accounts receivable for Ashfall Co. are provided below:

	<u>Current Year</u>	<u>Prior Year</u>
Cash	\$62,400	\$58,000
Accounts receivable (net)	42,000	50,000

Based on this information, what is the amount and percentage of increase or decrease that would be shown on a balance sheet with horizontal analysis?

ANSWER: Cash \$4,400 increase (\$62,400 – \$58,000) or 7.6%
 Accounts receivable \$8,000 decrease (\$42,000 – \$50,000) or (16%)

DIFFICULTY: Easy
 Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

143. Income statement information for Lucy Company is provided below:

Sales	\$75,000
Cost of goods sold	<u>05,000</u>
Gross profit	<u>\$ 70,000</u>

Prepare a vertical analysis of the income statement for Lucy Company.

ANSWER:

	<u>Amount</u>	<u>Percentage</u>	
Sales	\$175,000	100%	(\$175,000/\$175,000)
Cost of goods sold	<u>105,000</u>	<u>60%</u>	(\$105,000/\$175,000)
Gross profit	<u>\$ 70,000</u>	<u>40%</u>	(\$70,000/\$175,000)

DIFFICULTY: Easy
 Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

144. Why would you or why wouldn't you compare an organization like Ford Motor Company to the local car dealer "Johnson City Ford/Lincoln/Mercury" in vertical and horizontal analysis?

ANSWER:

Ford Motor Company is an automobile manufacturer with many aspects within the overall company such as military sales, foundries, credit and financing operations, and its car sales are usually limited to resellers or large fleet purchasers.

Johnson City Ford/Lincoln/Mercury is a local reseller that does not have the diverse operations of the Ford Motor Company. Most of its sales, which would include new and used vehicles, would be to ultimate consumers and to smaller fleet operations. Major revenues may come from repairs and upgrades of vehicles. Its "credit" department may actually be a representative of another organization specializing in automobile financing.

While they both sell cars and contain the same name elements, they are not comparable.

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.ACBS.P.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

145. The balance sheet data of Randolph Company for two recent years appears below:

Assets:	Year 2	Year 1
Current assets	\$ 440	\$280
Plant assets	675	520
Total assets	\$1,115	\$800
Liabilities and stockholders' equity:		
Current liabilities	\$ 280	\$120
Long-term debt	250	160
Common stock	325	320
Retained earnings	260	200
Total liabilities and stockholders' equity	\$1,115	\$800

- (a) Using horizontal analysis, show the percentage change for each balance sheet item using Year 1 as a base year.
- (b) Using vertical analysis, prepare a comparative balance sheet.

Round percentages to one decimal place.

ANSWER:

(a)			Increase	(Decrease)
	Year 2	Year 1	Amount	Percent
Assets				
Current assets	\$ 440	\$280	\$160	57.1%
Plant assets	675	520	155	29.8%
Total assets	\$1,115	\$800	\$315	39.4%
Liabilities & Stockholders' Equity				
Current liabilities	\$ 280	\$120	\$160	133.3%
Long-term debt	250	160	90	56.3%
Common stock	325	320	5	1.6%
Retained earnings	260	200	60	30.0%
Total liabilities and stockholders' equity	\$1,115	\$800	\$315	39.4%

Chapter 15(14): Financial Statement Analysis

(b) Assets	<u>Year 2</u>		<u>Year 1</u>	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
Current assets	\$ 440	39.5%	\$280	35.0%
Plant assets	675	60.5%	520	65.0%
Total assets	<u>\$1,115</u>	<u>100.0%</u>	<u>\$800</u>	<u>100.0%</u>
Liabilities and Stockholders'				
Current liabilities	\$280	25.1%	\$120	15.0%
Long-term debt	250	22.4%	160	20.0%
Common stock	325	29.1%	320	40.0%
Retained earnings	260	23.3%	200	25.0%
Total liabilities and stockholders' equity	<u>\$1,115</u>	<u>100.0%</u>	<u>\$800</u>	<u>100.0%</u>

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

146. Condensed data taken from the ledger of St. Louis Company at December 31, for the current and preceding years, are as follows:

	<u>Year 2</u>	<u>Year 1</u>
Current assets	\$160,000	\$130,000
Property, plant, and equipment	450,000	400,000
Intangible assets	20,700	30,000
Current liabilities	70,000	80,000
Long-term liabilities	210,000	250,000
Common stock	225,000	150,000
Retained earnings	125,700	80,000

Prepare a comparative balance sheet, with horizontal analysis, for December 31, Year 2 and Year 1. (Round percents to one decimal point.)

ANSWER:

St. Louis Company				
Comparative Balance Sheet				
December 31, Year 2 and Year 1				
	<u>Year 2</u>	<u>Year 1</u>	<u>Increase (Decrease)</u>	
			<u>Amount</u>	<u>Percent</u>
Assets				
Current assets	\$160,000	\$130,000	\$30,000	23.1%
Property, plant, and equipment	450,000	400,000	50,000	12.5%
Intangible assets	20,700	30,000	(9,300)	(31.0%)
Total assets	<u>\$630,700</u>	<u>\$560,000</u>	<u>\$70,700</u>	12.6%
Liabilities				
Current liabilities	\$ 70,000	\$ 80,000	\$(10,000)	(12.5%)
Long-term liabilities	210,000	250,000	(40,000)	(16.0%)
Total liabilities	<u>\$280,000</u>	<u>\$330,000</u>	<u>\$(50,000)</u>	(15.2%)
Stockholders' Equity				
Common stock	\$225,000	\$150,000	\$ 75,000	50.0%
Retained earnings	125,700	80,000	45,700	57.1%
Total stockholders' equity	<u>\$350,700</u>	<u>\$230,000</u>	<u>\$120,700</u>	52.5%
Total liabilities and stockholders' equity	<u>\$630,700</u>	<u>\$560,000</u>	<u>\$ 70,700</u>	12.6%

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

147. Revenue and expense data for Bluestem Company are as follows:

	<u>Year 2</u>	<u>Year 1</u>
Administrative expenses	\$ 37,000	\$ 20,000
Cost of goods sold	350,000	320,000
Income tax	40,000	32,000
Sales	800,000	700,000
Selling expenses	150,000	110,000

- (a) Prepare a comparative income statement, with vertical analysis, stating each item for both years as a percent of sales.
 (b) Comment upon significant changes disclosed by the comparative income statement.
 Round percentages to one decimal place.

ANSWER:

(a)

Bluestem Company
 Comparative Income Statement
 For Years Ended December 31, Year 2 and Year 1

	<u>Year 2</u>		<u>Year 1</u>	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
Sales	\$800,000	100.0%	\$700,000	100.0%
Cost of goods sold	<u>350,000</u>	<u>43.8</u>	<u>320,000</u>	<u>45.7</u>
Gross profit	<u>\$450,000</u>	<u>56.2%</u>	<u>\$380,000</u>	<u>54.3%</u>
Selling expenses	\$150,000	18.8%	\$110,000	15.7%
Administrative expenses	<u>37,000</u>	<u>4.6</u>	<u>20,000</u>	<u>2.9%</u>
Total operating expenses	<u>\$187,000</u>	<u>23.4%</u>	<u>\$130,000</u>	<u>18.6%</u>
Income before income tax	\$263,000	32.8%	\$250,000	35.7%
Income tax	<u>40,000</u>	<u>5.0</u>	<u>32,000</u>	<u>4.6</u>
Net income	<u>\$223,000</u>	<u>27.8%</u>	<u>\$218,000</u>	<u>31.1%</u>

- (b) There was a 1.9% decrease in the cost of goods sold, and a 1.7% increase in administrative expenses. However, the more significant increase of 3.1% in selling expenses offset the 1.9% decrease in cost of goods sold and contributed greatly to the 3.3% decrease in net income.

DIFFICULTY:

Moderate

Bloom's: Applying

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

148. What is a major advantage of using percentages rather than dollar changes in doing horizontal and vertical analysis?

ANSWER: When percentages are utilized rather than dollars, companies that are not the same size can be compared. If Carbondale Chemicals is a \$10 billion per year sales company and Heartland Chemicals is a \$500 million per year sales company, these two companies can still be compared by using percentages determined by the analysis. These companies' results can also be compared to industry averages.

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-01 - 17-01

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

149. The following items are reported on a company's balance sheet:

Cash	\$230,000
Marketable securities	50,000
Accounts receivable	200,000
Inventory	240,000
Accounts payable	300,000

Determine the (a) current ratio, and (b) quick ratio. Round your answer to one decimal place.

ANSWER:

- (a) Current ratio = Current assets (cash, marketable securities, accounts receivable and inventory)/Current liabilities (accounts payable)
Current ratio = $(\$230,000 + \$50,000 + \$200,000 + \$240,000)/\$300,000$
Current ratio = 2.4
- (b) Quick ratio = Quick assets (cash, marketable securities and accounts receivable)/Current liabilities (accounts payable)
Quick ratio = $(\$230,000 + \$50,000 + \$200,000)/\$300,000$
Quick ratio = 1.6

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

150. The following items are reported on a company's balance sheet:

Cash	\$400,000
Marketable securities	50,000
Accounts receivable	150,000
Inventory	200,000
Accounts payable	250,000

Determine the (a) current ratio, and (b) quick ratio. Round your answer to one decimal place.

ANSWER:

- (a) Current ratio = Current assets (cash, marketable securities, accounts receivable, and inventory)/Current liabilities (accounts payable)

$$\text{Current ratio} = (\$400,000 + \$50,000 + \$150,000 + \$200,000)/\$250,000$$

$$\text{Current ratio} = \underline{3.2}$$

- (b) Quick ratio = Quick assets (cash, marketable securities and accounts receivable)/Current liabilities (accounts payable)

$$\text{Quick ratio} = (\$400,000 + \$50,000 + \$150,000)/\$250,000$$

$$\text{Quick ratio} = \underline{2.4}$$

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

151. The following items are reported on Denver Company's balance sheet:

Cash	\$190,000
Marketable securities	160,000
Accounts receivable (net)	240,000
Inventory	350,000
Accounts payable	600,000

Determine (a) the current ratio and (b) the quick ratio. Round to one decimal place.

ANSWER:

- (a) Current ratio = Current assets ÷ Current liabilities
Current ratio = $(\$190,000 + \$160,000 + \$240,000 + \$350,000) \div \$600,000$
Current ratio = 1.6
- (b) Quick ratio = Quick assets ÷ Current liabilities
Quick ratio = $(\$190,000 + \$160,000 + \$240,000) \div \$600,000$
Quick ratio = 1.0

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBS.PC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

152. For Garrison Corporation, the working capital at the end of the current year is \$10,000 more than the working capital at the end of the preceding year, reported as follows:

	<u>Year 2</u>	<u>Year 1</u>
Current assets:		
Cash, marketable securities, and receivables	\$ 80,000	\$ 84,000
Inventories	<u>120,000</u>	<u>66,000</u>
Total current assets	\$200,000	\$150,000
Current liabilities	<u>100,000</u>	<u>60,000</u>
Working capital	<u>\$100,000</u>	<u>\$ 90,000</u>

Has the current position of Garrison Corporation improved? Explain.

ANSWER:

The amount of working capital and the change in working capital are just two indicators of the strength of the current position. A comparison of the current ratio and the quick ratio, along with the amount of working capital, gives a better analysis of the current position.

	<u>Year 2</u>	<u>Year 1</u>
Working capital	\$100,000	\$90,000
Current ratio	2.0	2.5
Quick ratio	0.8	1.4

Although working capital has increased, the current ratio has fallen from 2.5 to 2.0, and the quick ratio has fallen from 1.4 to 0.8.

A reduction in the current ratio and quick ratio imply that it has become difficult for the company to convert its assets into cash to pay off its short-term liabilities, the current position has deteriorated.

DIFFICULTY:

Moderate

Bloom's: Applying

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBSB.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

153. A company reports the following:

Sales	\$720,000
Average accounts receivable (net)	45,000

Determine the (a) accounts receivable turnover, and (b) number of days' sales in receivables. Round your answer to one decimal place.

- ANSWER:**
- (a) Accounts receivable turnover = Sales/Average accounts receivable
Accounts receivable turnover = $\$720,000/\$45,000$
Accounts receivable turnover = 16.0
- (b) Number of days' sales in receivable = Average accounts receivable/
Average daily sales
Number of days' sales in receivable = $\$45,000/(\$720,000/365)$
Number of days' sales in receivables = 22.8

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

154. A company reports the following:

Sales	\$1,200,000
Average accounts receivable (net)	50,000

Determine the (a) accounts receivable turnover, and (b) number of days' sales in receivables. Round your answer to one decimal place.

- ANSWER:**
- (a) Accounts receivable turnover = Sales/Average accounts receivable
Accounts receivable turnover = $\$1,200,000/\$50,000$
Accounts receivable turnover = 24.0
- (b) Number of days' sales in receivable = Average accounts receivable/
Average daily sales
Number of days' sales in receivable = $\$50,000/(\$1,200,000/365)$
Number of days' sales in receivables = 15.2

DIFFICULTY: Easy

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

155. A company reports the following:

Cost of goods sold	\$610,000
Average inventory	80,000

Determine the (a) inventory turnover, and (b) number of days' sales in inventory. Round your answer to one decimal place.

- ANSWER:**
- (a) Inventory turnover = Cost of goods sold/Average inventory
 Inventory turnover = \$610,000/\$80,000
 Inventory turnover = 7.6
- (b) Number of days' sales in inventory = Average inventory/Average daily cost of goods sold
 Number of days' sales in inventory = \$80,000/(\$610,000/365)
 Number of days' sales in inventory = 47.9 days

DIFFICULTY: Easy
 Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

156. The following information was taken from Slater Company's balance sheet:

Fixed assets (net)	\$1,250,000
Long-term liabilities	500,000
Total liabilities	672,000
Total stockholders' equity	1,680,000

Determine the company's (a) ratio of fixed assets to long-term liabilities, and (b) ratio of liabilities to stockholders' equity. Round your answer to one decimal place.

- ANSWER:**
- (a) Ratio of fixed assets to long-term liabilities = Fixed assets/Long-term liabilities
 Ratio of fixed assets to long-term liabilities = \$1,250,000/\$500,000
 Ratio of fixed assets to long-term liabilities = 2.5
- (b) Ratio of liabilities to total stockholders' equity = Total liabilities/Total stockholders' equity
 Ratio of liabilities to total stockholders' equity = \$672,000/\$1,680,000
 Ratio of liabilities to total stockholders' equity = 0.40

DIFFICULTY: Easy
 Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

157. The following data are available for Martin Solutions, Inc.

	<u>Year 2</u>	<u>Year 1</u>
Sales	\$1,139,600	\$1,192,320
Beginning inventory	80,000	64,000
Cost of goods sold	500,800	606,000
Ending inventory	72,000	80,000

- (1) Determine for each year:
- (a) The inventory turnover
 - (b) The number of days' sales in inventory (Round intermediate calculation to the nearest whole number and your final answer to one decimal place).
- (2) What conclusions can be drawn from these data concerning the inventories?

ANSWER:

(1)(a) Inventory turnover = Cost of goods sold / Average inventory

	$\frac{\$500,800}{(\$72,000 + \$80,000)/2}$	= <u>6.6</u>
Year 2		
Year 1	$\frac{\$606,000}{(\$80,000 + \$64,000)/2}$	= <u>8.4</u>

(b) Number of days' sales in inventory = Average inventory / Average daily cost of goods sold

	$\frac{(\$72,000 + \$80,000)/2}{\$1,372 *}$	= <u>55.4</u>
Year 2		
Year 1	$\frac{(\$80,000 + \$64,000)/2}{\$1,660 **}$	= <u>43.4</u>

*\$1,372 = \$500,800 ÷ 365 days

**\$1,660 = \$606,000 ÷ 365 days

- (2) The inventory position of the business has deteriorated. The inventory turnover has decreased, while the number of days' sales in inventory has increased. The sales volume has declined faster than the inventory has declined, thus resulting in the deteriorating inventory position.

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBSAPC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

158. A company reports the following:

Income before income tax	\$600,000
Interest expense	150,000

Determine the number of times interest charges are earned. Round your answer to one decimal place.

ANSWER: Number of times interest charges are earned = (Income before income tax + Interest expense)/Interest expense
Number of times interest charges are earned = $(\$600,000 + \$150,000)/\$150,000$
Number of times interest charges are earned = 5.0

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

159. The following data are taken from the balance sheet at the end of the current year.

Cash	\$154,000
Accounts receivable	210,000
Inventory	240,000
Prepaid expenses	15,000
Temporary investments	350,000
Property, plant, and equipment	375,000
Accounts payable	245,000
Accrued liabilities	4,000
Income tax payable	10,000
Notes payable, short-term	85,000

Determine the (a) working capital, (b) current ratio, and (c) quick ratio. Round ratios to the nearest tenth.

ANSWER: (a) Current assets (\$969,000) – Current liabilities (\$344,000) = \$625,000
(b) Current assets (\$969,000)/Current liabilities (\$344,000) = 2.8
(c) Cash + temporary investments + accounts receivable (\$714,000)/Current liabilities (\$344,000) = 2.1

DIFFICULTY: Easy
Bloom's: Applying

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

160. The following data are taken from the financial statements:

	Current <u>Year</u>	Preceding <u>Year</u>
Average accounts receivable (net)	\$123,000	\$ 95,000
Accounts receivable (net), end of year	129,012	87,516
Sales on account	950,000	825,000

- (a) Assuming that credit terms on all sales are n/45, determine for each year (1) the accounts receivable turnover and (2) the number of days' sales in receivables. Round intermediate calculations to whole numbers and final answers to two decimal places.
- (b) Comment on any significant trends revealed by the data.

ANSWER:

(a)

	Current <u>Year</u>	Preceding <u>Year</u>
(1) Sales on account/Average accounts receivable (net)	7.72	8.68
(2) Average accounts receivable/Average daily sales on account**	47.25	42.04

**Current: $\$950,000/365 = \$2,603$

Preceding: $\$825,000/365 = \$2,260$

- (b) Although sales increased during the current year, a favorable trend, several unfavorable trends are disclosed by the analysis. The accounts receivable turnover has declined from 8.68 in the preceding year to 7.72 in the current year. Based on credit terms of n/45, a turnover of less than 8 indicates that some receivables are not being collected within the 45-day period. Likewise, the number of days' sales in receivables indicates an unfavorable trend, increasing from 42.04 at the end of the preceding year to 47.25 at the end of the current year.

DIFFICULTY:

Easy

Bloom's: Applying

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

161. The following data are taken from the financial statements:

	Current <u>Year</u>	Preceding <u>Year</u>
Sales	\$3,600,000	\$4,000,000
Cost of goods sold	2,000,000	2,700,000
Average inventory	372,000	352,000
Inventory, end of year	372,000	347,000

- (a) Determine for each year (1) the inventory turnover, round answer to one decimal place.
 (2) the number of days' sales in inventory. Round intermediate calculations to two decimal places and the final answer to whole number.
- (b) Comment on the favorable and unfavorable trends revealed by the data.

ANSWER:

(a)

	Current <u>Year</u>	Preceding <u>Year</u>
(1) Cost of goods sold/Average inventory	5.4	7.7
(2) Average inventory/Average daily cost of goods sold*	67.90	45.59
*Average daily cost of goods sold (Cost of goods sold ÷ 365 days)	5,479 days	7,397 days

- (b) Sales decreased while gross profit increased. The inventory turnover declined and the number of days' sales in inventory increased, which are unfavorable trends.

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

162. The balance sheet for Seuss Company at the end of the current fiscal year indicated the following:

Bonds payable, 10% (20-year term)	\$5,000,000
Preferred 10% stock, \$100 par	1,000,000
Common stock, \$10 par	2,000,000

Income before income tax was \$1,500,000 and income taxes were \$200,000 for the current year. Cash dividends paid on common stock during the current year totaled \$150,000. The common stock sells for \$70 per share at the end of the year.

Determine each of the following:

- (a) Number of times interest charges are earned
- (b) Earnings per share on common stock
- (c) Price-earnings ratio
- (d) Dividends per share of common stock
- (e) Dividend yield

Round to one decimal place except earnings per share and dividends per share, which should be rounded to two decimal places.

- ANSWER:**
- (a) Number of times interest charges are earned =
 $(\text{Income before tax} + \text{Interest expense}) / \text{Interest expense}$
 $(\$1,500,000 + \$500,000) / \$500,000 = \underline{4.0 \text{ times}}$
 - (b) Earnings per share on common stock = $(\text{Net income} - \text{Preferred dividends}) / \text{Common shares outstanding}$
 $(\$1,300,000 - \$100,000) / 200,000 \text{ shares} = \underline{\$6.00}$
 - (c) Price-earnings ratio = $\text{Market price per share} / \text{Earnings per share}$
 $\$70.00 / \$6.00 = \underline{11.7}$
 - (d) Dividends per share of common stock =
 $\text{Common dividends} / \text{Common shares outstanding}$
 $\$150,000 / 200,000 \text{ shares} = \underline{\$0.75}$
 - (e) Dividend yield = $\text{Common dividend per share} / \text{Share price}$
 $\$0.75 / \$70.00 = \underline{1.1\%}$

DIFFICULTY: Moderate

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02
 ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

163. Define solvency and profitability. How are they alike?

ANSWER: Solvency is the ability of a company to meet its financial obligations (debts) as they become due. Profitability is the ability of a company to earn income. They are interrelated because a company that cannot pay its debts will have difficulty obtaining credit. A lack of credit can prevent a company from taking actions (i.e., expansion) that would increase profitability.

DIFFICULTY: Moderate
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-02 - 17-02
ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

164. A company reports the following:

Sales	\$2,400,000
Average total assets	1,500,000

Determine the ratio of sales to assets. Round your answer to one decimal place.

ANSWER: Ratio of sales to assets = Sales/Average total assets
Ratio of sales to assets = $\$2,400,000/\$1,500,000$
Ratio of sales to assets = 1.6

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

165. A company reports the following:

Sales	\$2,520,000
Average total assets	1,400,000

Determine the ratio of sales to assets. Round your answer to one decimal place.

ANSWER: Ratio of sales to assets = Sales/Average total assets
Ratio of sales to assets = $\$2,520,000/1,400,000$
Ratio of sales to assets = 1.8

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

166. A company reports the following income statement and balance sheet information for the current year:

Net income	\$ 180,000
Interest expense	20,000
Average total assets	2,000,000

Determine the rate earned on total assets. Round your answer to one decimal place.

ANSWER: Rate earned on assets = (Net income + Interest expense)/Average total assets
Rate earned on assets = $(\$180,000 + \$20,000)/\$2,000,000$
Rate earned on assets = $\$200,000/\$2,000,000$
Rate earned on assets = 10%

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

167. A company reports the following:

Net income	\$150,000
Preferred dividends	\$10,000
Shares of common stock outstanding	20,000
Market price per share of common stock	\$35

Calculate the company's earnings per share on common stock.

ANSWER: Earnings per share on common stock = (Net income – Preferred dividends)/Shares of common stock outstanding
Earnings per share = $(\$150,000 - \$10,000)/20,000$
Earnings per share = \$7.00

DIFFICULTY: Easy
Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

168. A company reports the following:

Net income	\$ 350,000
Preferred dividends	50,000
Average stockholders' equity	1,000,000
Average common stockholders' equity	800,000

Determine the (a) rate earned on stockholders' equity, and (b) rate earned on common stockholders' equity. Round to one decimal place.

ANSWER:

- (a) Rate earned on stockholders' equity = Net income/Average stockholders' equity
Rate earned on stockholders' equity = $\$350,000/\$1,000,000$
Rate earned on stockholders' equity = 35.0%
- (b) Rate earned on common stockholders' equity = (Net income – Preferred dividends)/
Average common stockholders' equity
Rate earned on common stockholders' equity = $(\$350,000 - \$50,000)/\$800,000$
Rate earned on common stockholders' equity = 37.5%

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

169. A company reported the following:

Net income	\$270,000
Preferred dividends	\$10,000
Shares of common stock outstanding	20,000
Market price per share of common stock	\$36.40

Calculate the company's price-earnings ratio. Round your answer to one decimal place.

ANSWER: Price-earnings ratio = Market price per share of common stock/Earnings per share on common stock

Earnings per share on common stock = (Net income – Preferred dividends)/
Shares of common stock outstanding

Earnings per share = (\$270,000 – \$10,000)/20,000

Earnings per share = \$13.00

Price-earnings ratio = \$36.40/\$13.00

Price-earnings ratio = 2.8

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

170. Why would you compare or not compare Coca-Cola and Pepsi-Cola (PepsiCo) as companies to each other?

ANSWER:

Coca-Cola has maintained its focus on the beverage market with little distraction. Pepsi-Cola (PepsiCo) also produces beverages has diversified into the snack and fast food markets with such operations as Frito-Lay, Taco Bell, KFC, and Pizza Hut. While their carbonated soft drinks may be comparable, the direct comparison of the two companies is limited by their differences.

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.BB.07 - Critical Thinking

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Reflective Thinking

Chapter 15(14): Financial Statement Analysis

171. The following selected data were taken from the financial statements of the Winter Group for the three most recent years of operations:

	Dec. 31, Year 3	Dec.31, Year 2	Dec. 31, Year 1
Total assets	\$3,000,000	\$2,700,000	\$2,400,000
Notes payable (10% interest)	1,000,000	1,000,000	1,000,000
Common stock	400,000	400,000	400,000
Preferred \$6 stock, \$100 par	200,000	200,000	200,000
Retained earnings	1,126,000	896,000	600,000

The Year 3 net income was \$242,000 and the Year 2 net income was \$308,000. No dividends on common stock were declared during the 3 years.

- (a) Determine the rate earned on assets, the rate earned on stockholders' equity, and the rate earned on common stockholders' equity for Years 2 and 3. Round to one decimal place.
 (b) What conclusion can be drawn from these data as to the company's profitability?

ANSWER:

- (a) Rate earned on assets = (Net income + Interest expense)/Average total assets

$$\text{Year 3: } (\$242,000 + \$100,000)/\$2,850,000^* = \underline{12.0\%}$$

$$\text{Year 2: } (\$308,000 + \$100,000)/\$2,550,000^{**} = \underline{16.0\%}$$

$$^*(\$3,000,000 + \$2,700,000) \div 2$$

$$^{**}(\$2,700,000 + \$2,400,000) \div 2$$

Rate earned on stockholders' equity = Net income / Average stockholders' equity

$$\text{Year 3: } \$242,000/\$1,611,000^* = \underline{15.0\%}$$

$$\text{Year 2: } \$308,000/\$1,348,000^{**} = \underline{22.8\%}$$

$$^*(\$1,726,000 + \$1,496,000) \div 2$$

$$^{**}(\$1,496,000 + \$1,200,000) \div 2$$

Rate earned on common stockholders' equity =

(Net income – Preferred dividends)/Average common stockholders' equity

$$\text{Year 3: } (\$242,000 - \$12,000)/\$1,411,000^* = \underline{16.3\%}$$

$$\text{Year 2: } (\$308,000 - \$12,000)/\$1,148,000^{**} = \underline{25.8\%}$$

$$^*(\$1,526,000 + \$1,296,000) \div 2$$

$$^{**}(\$1,296,000 + \$1,000,000) \div 2$$

- (b) The profitability ratios indicate that The Winter Group's profitability has deteriorated. Most of this change is from net income falling from \$308,000 in Year 2 to \$242,000 in Year 3. The cost of debt is 10%. Since the rate of return on assets exceeds this amount in either year, there is positive leverage from use of debt. However, this leverage is greater in Year 2 because the rate of return on assets exceeds the cost of debt by a greater amount in Year 2.

DIFFICULTY: Moderate
 Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

172. Selected data from the Carmen Company at year end are presented below:

Total assets	\$2,000,000
Average total assets	2,200,000
Net income	250,000
Sales	1,300,000
Average common stockholders' equity	1,000,000
Net cash provided by operating activities	275,000
Shares of common stock outstanding	10,000

Calculate: (a) ratio of sales to assets; (b) rate earned on total assets; (c) rate earned on common stockholders' equity and (d) earnings per share on common stock. Assume the company had no preferred stock or interest expense. Round percentage values to one decimal place and dollar values to zero decimal place.

ANSWER: With the information provided, the profitability ratios that can be calculated are as follows:

$$\begin{aligned} \text{(a) Ratio of sales to assets} &= \text{Sales/Average total assets} \\ &= \$1,300,000/\$2,200,000 \\ &= \underline{59.1\%} \end{aligned}$$

$$\begin{aligned} \text{(b) Rate earned on total assets} &= (\text{Net income} + \text{Interest expense})/ \\ &\quad \text{Average total assets} \\ &= (\$250,000 + 0)/\$2,200,000 \\ &= \underline{11.4\%} \end{aligned}$$

$$\begin{aligned} \text{(c) Rate earned on common stockholders' equity} &= \frac{\text{Net income} - \text{Preferred dividends}}{\text{Average common stockholders' equity}} \\ &= (\$250,000 - \$0)/\$1,000,000 \\ &= \underline{25\%} \end{aligned}$$

$$\begin{aligned} \text{(d) Earnings per share on common stock} &= \$250,000/10,000 \\ &= \underline{\$25} \text{ per share} \end{aligned}$$

DIFFICULTY: Moderate

Bloom's: Remembering

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

173. The following information was taken from the financial statement of Fox Resources for December 31 of the current fiscal year:

Common stock, \$20 par value (no change during the year)	\$5,000,000
Preferred 10% stock, \$40 par (no change during the year)	2,000,000

The net income was \$600,000, and the declared dividends on the common stock were \$125,000 for the current year. The market price of the common stock is \$20 per share.

Required:

Calculate for the common stock:

- (a) earnings per share
- (b) the price-earnings ratio
- (c) the dividends per share and the dividend yield

Round to one decimal place except earnings per share, which should be rounded to two decimal places.

ANSWER:

- (a) Earnings per share = (Net income – Preferred dividends)/Common shares outstanding = $(\$600,000 - 200,000)/250,000 \text{ shares} = \underline{\$1.60}$
- (b) Price-earnings ratio = Market price per share/Earnings per share = $\$20.00/\$1.60 = \underline{12.5}$
- (c) Dividends per share = Common dividends/Common shares outstanding = $\$125,000/250,000 \text{ shares} = \underline{\$0.50}$

Dividend yield = Dividends per share of common stock/Market price per share of common stock = $\$0.50/\$20.00 = \underline{2.5\%}$

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

(f)
 Dividends per share of common stock (\$1.46)

 = 5.8%
 Market price per share of common stock (\$25)

DIFFICULTY:

Moderate
 Bloom's: Applying

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

175. The following information has been condensed from the December 31 balance sheets of Gabriel Co.:

	<u>Year 2</u>	<u>Year 1</u>
Assets:		
Current assets	\$ 825,500	\$ 674,300
Fixed assets (net)	<u>1,473,600</u>	<u>1,275,300</u>
Total assets	<u>\$2,299,100</u>	<u>\$1,949,600</u>
Liabilities:		
Current liabilities	\$ 313,500	\$ 309,600
Long-term liabilities	<u>703,000</u>	<u>545,000</u>
Total liabilities	<u>\$1,016,500</u>	<u>\$ 854,600</u>
Stockholders' equity	<u>\$1,282,600</u>	<u>\$1,095,000</u>
Total liabilities and stockholders' equity	<u>\$2,299,100</u>	<u>\$1,949,600</u>

- (a) Determine the ratio of fixed assets to long-term liabilities for each year.
 (b) Determine the ratio of liabilities to stockholders' equity for each year.
 (c) Comment on the year-to-year changes for both ratios. Round your answers to two decimal places.

ANSWER:

	<u>Year 2</u>	<u>Year 1</u>
(a)		
Ratio of fixed assets to long-term liabilities	<u>2.10</u>	<u>2.34</u>
(b)		
Ratio of liabilities to stockholders' equity	<u>0.79</u>	<u>0.78</u>

(c) In the second year, there are fewer fixed assets on a proportionate basis to protect the interests of the long-term creditors than in the first year. Also, the margin of safety to creditors, as measured by the ratio of liabilities to stockholders' equity, has risen slightly in the second year, which indicates that the creditors have a lower margin of safety.

DIFFICULTY:

Moderate
 Bloom's: Applying

LEARNING OBJECTIVES: ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS: ACCT.ACBSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

176. Abigail Company reports the following:

Net income	\$ 295,000
Preferred dividends	30,000
Average stockholders' equity	1,000,000
Average common stockholders' equity	700,000

Determine the (a) rate earned on stockholders' equity, and (b) rate earned on common stockholders' equity. Round your answer to one decimal place.

ANSWER:

(a) Rate earned on stockholders' equity = Net income/Average stockholders' equity
Rate earned on stockholders' equity = $\$295,000/\$1,000,000$
Rate earned on stockholders' equity = 29.5%

(b) Rate earned on common stockholders' equity = (Net income – Preferred dividends)/
Average common stockholders' equity
Rate earned on common stockholders' equity = $(\$295,000 - \$30,000)/\$700,000$
Rate earned on common stockholders' equity = 37.9%

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

177. Gallant Company reported net income of \$2,500,000. The income statement included a \$500,000 gain from condemnation of land and a \$200,000 loss on discontinued operations, both after applicable income tax. There were 100,000 shares of \$10 par common stock and 40,000 shares of 4% preferred stock of \$100 par outstanding throughout the current year.

Prepare the earnings per share section of Gallant Company's income statement.

ANSWER:

Earnings per common share:	
Income from continuing operations*	\$20.40
Loss on discontinued operations (\$200,000/ 100,000 shares)	<u>(2.00)</u>
Income before extraordinary items	\$18.40
Extraordinary items:	
Gain on condemnation of land (\$500,000/ 100,000 shares)	<u>5.00</u>
Net income	<u>\$23.40</u>

*Net income	\$2,500,000
Less gain on condemnation of land	(500,000)
Plus loss on discontinued operations	<u>200,000</u>
Income from continuing operations	<u>\$2,200,000</u>

Earnings per share on common stock =
 (Income from continuing operations – Preferred dividends)/
 Common shares outstanding = (\$2,200,000 – \$160,000)/
 100,000 shares = \$20.40 per share

DIFFICULTY:

Moderate
 Bloom's: Applying

LEARNING OBJECTIVES:

ACCT.WARD.16.17-03 - 17-03
 ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.02 - GAAP
 ACCT.AC BSP.APC.23 - Financial Statement Analysis
 ACCT.AICPA.FN.03 - Measurement
 BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

178. What information is generally included in the Management Discussion and Analysis (MD&A) section of a corporate annual report?

ANSWER:

The MD&A section typically includes:

- Management's analysis and explanations of any significant changes between the current and prior years' financial statements.
- Important accounting principles or policies that could affect interpretation of the financial statements, including the effect of changes in accounting principles or the adoption of new principles.
- Management's assessment of the company's liquidity and the availability of capital to the company.
- Significant risk exposures that might affect the company.
- Any "off-balance-sheet" arrangements such as leases not included directly on the financial statements.

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS:

ACCT.ACBSAPPC.02 - GAAP

ACCT.ACBSAPPC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

179. Prepare an income statement using the following data for New Orleans Adventures for the year ended December 31:

Sales	\$24,500,000
Cost of merchandise sold	10,900,000
Operating expenses	6,300,000
Losses from asset impairment	2,800,000
Income tax expense	500,000
Loss on discontinued operations	100,000
Net loss on extraordinary item	125,000

ANSWER:

New Orleans Adventures
Income Statement
For the Year Ended December 31

Sales		\$24,500,000
Cost of merchandise sold		<u>10,900,000</u>
Gross profit		\$13,600,000
Operating expenses	\$6,300,000	
Losses from asset impairment	<u>2,800,000</u>	<u>9,100,000</u>
Income from continuing operations before income tax		\$ 4,500,000
Income tax expense		<u>500,000</u>
Income from continuing operations		\$ 4,000,000
Loss on discontinued operations		<u>100,000</u>
Income before extraordinary expense		\$ 3,900,000
Net loss on extraordinary item		<u>125,000</u>
Net income		<u><u>\$ 3,775,000</u></u>

DIFFICULTY:

Moderate

Bloom's: Applying

LEARNING OBJECTIVES:

ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.02 - GAAP

ACCT.AC BSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

180. Zeus Company reports the following for the current year:

Income from continuing operations before income tax	\$500,000
Extraordinary property loss from hurricane	\$60,000*
Loss from discontinued operations	\$90,000*
Weighted average number of common shares outstanding	40,000
Applicable tax rate	40%

*Net of any tax effect

- Prepare a partial income statement for Zeus Company beginning with income from continuing operations before income tax.
- Calculate the earnings per common share for Zeus, including per-share amount for unusual items.

ANSWER:

(a)

Zeus, Inc.
Partial Income Statement
For the Year Ended December 31

Income from continuing operations before income tax	\$500,000
Income tax expense	<u>200,000</u>
Income from continuing operations	\$300,000
Loss from discontinued operations (net of tax)	<u>90,000</u>
Income before extraordinary item (net of tax)	\$210,000
Extraordinary item:	
Loss due to hurricane	<u>60,000</u>
Net income	<u>\$150,000</u>

(b)

Zeus, Inc.
Partial Income Statement
For the Year Ended December 31

Earnings per common share:	
Income from continuing operations	\$7.50 ¹
Loss from discontinued operations	<u>2.25²</u>
Income before extraordinary item	\$5.25
Extraordinary item:	
Loss due to hurricane	<u>1.50³</u>
Net income	<u>\$3.75</u>

¹\$7.50 = \$300,000 ÷ 40,000

²\$2.25 = \$90,000 ÷ 40,000

³\$1.50 = \$60,000 ÷ 40,000

DIFFICULTY:

Moderate
Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-APP - 17-APP

ACCREDITING STANDARDS:

ACCT.AC BSP.APC.02 - GAAP
ACCT.AC BSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

181. From the following data for Norton Company for the year ended December 31, prepare a multiple-step income statement. Show earnings per share for the following: income from continuing operations, loss on discontinued operations (less applicable income tax), income before extraordinary item, extraordinary item (less applicable income tax), and net income.

Common stock, \$50 par	\$200,000
Cost of merchandise sold	342,000
Administrative expenses	48,250
Income tax (applicable to continuing operations)	142,000
Interest expense	3,750
Loss on discontinued operations, net of applicable tax of \$2,700	5,400
Sales	865,000
Selling expenses	83,000
Uninsured flood loss, net of applicable income tax of \$4,500	14,000

Chapter 15(14): Financial Statement Analysis

ANSWER:

Norton Company	
Income Statement	
For Year Ended December 31	
Sales	\$865,000
Cost of merchandise sold	<u>342,000</u>
Gross profit	\$523,000
Operating expenses:	
Selling expenses	\$ 83,000
Administrative expenses	<u>48,250</u>
Total operating expenses	<u>\$131,250</u>
Income from operations	\$391,750
Other expense:	
Interest expense	<u>3,750</u>
Income from continuing operations before income tax	\$388,000
Income tax expense	<u>142,000</u>
Income from continuing operations	\$246,000
Loss on discontinued operations, net of applicable income tax of \$2,700	<u>5,400</u>
Income before extraordinary item	\$240,600
Extraordinary item:	
Uninsured flood loss, net of applicable income tax of \$4,500	<u>14,000</u>
Net income	<u><u>\$226,600</u></u>
Earnings per common share:	
Income from continuing operations	\$61.50
Loss on discontinued operations	<u>1.35</u>
Income before extraordinary item	\$60.15
Extraordinary item:	
Uninsured flood loss	<u>3.50</u>
Net income	<u><u>\$56.65</u></u>

DIFFICULTY: Challenging
Bloom's: Applying

ACCREDITING STANDARDS: ACCT.ACBSP.APC.02 - GAAP
ACCT.ACBSP.APC.23 - Financial Statement Analysis
ACCT.AICPA.FN.03 - Measurement
BUSPROG: Analytic

Chapter 15(14): Financial Statement Analysis

Match each definition that follows with the term (a–h) it defines.

- a. discontinued operations
- b. extraordinary items
- c. change from one generally accepted accounting principle to another
- d. horizontal analysis
- e. vertical analysis
- f. common-sized financial statements
- g. current position analysis
- h. profitability analysis

DIFFICULTY:

Easy

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-01 - 17-01

ACCT.WARD.16.17-02 - 17-02

ACCT.WARD.16.17-03 - 17-03

ACCT.WARD.16.17-04 - 17-04

ACCREDITING STANDARDS:

ACCT.ACBSAPC.02 - GAAP

ACCT.ACBSAPC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

182. a percentage analysis of increases and decreases in related items on comparative financial statements

ANSWER: d

183. an event or transaction that is both unusual and infrequent

ANSWER: b

184. an analysis of a company's ability to pay its current liabilities

ANSWER: g

185. the percentage analysis of the relationship of each component in a financial statement to a total within the statement

ANSWER: e

186. occurs when a company abandons a segment

ANSWER: a

187. focuses on a company's ability to generate net income

ANSWER: h

Chapter 15(14): Financial Statement Analysis

188. useful for comparing one company to another or a company with industry averages

ANSWER: f

189. requires a restatement of prior-period financial statements

ANSWER: c

Match each ratio that follows to its use (items a–h). Items may be used more than once.

- a. assess the profitability of the assets
- b. assess the effectiveness in the use of assets
- c. indicate the ability to meet currently maturing obligations
- d. indicate the margin of safety to creditors
- e. indicate instant debt-paying ability
- f. assess the profitability of the investment by common stockholders
- g. indicate future earnings prospects
- h. indicate the extent to which earnings are being distributed to common stockholders

DIFFICULTY:

Moderate

Bloom's: Remembering

LEARNING OBJECTIVES:

ACCT.WARD.16.17-02 - 17-02

ACCT.WARD.16.17-03 - 17-03

ACCREDITING STANDARDS:

ACCT.ACBSP.APC.23 - Financial Statement Analysis

ACCT.AICPA.FN.03 - Measurement

BUSPROG: Analytic

190. price-earnings (P/E) ratio

ANSWER: g

191. working capital

ANSWER: c

192. rate earned on total assets

ANSWER: a

193. ratio of liabilities to stockholders' equity

ANSWER: d

Chapter 15(14): Financial Statement Analysis

194. quick ratio

ANSWER: e

195. rate earned on common stockholders' equity

ANSWER: f

196. current ratio

ANSWER: c

197. ratio of sales to assets

ANSWER: b

198. dividends per share

ANSWER: h

199. earnings per share (EPS) on common stock

ANSWER: f