

# CONTENTS

Introduction.....	8
Frequently Asked Questions .....	9
Exam Strategies and Types of Questions .....	13
<b>Ch. 1 Financial Accounting Conceptual Framework and an Introduction to Financial Reporting.....</b>	<b>53</b>
Overview of the Concepts and Standards for Financial Statements Coverage on the CPA Exam ..	54
The Securities and Exchange Commission .....	54
Financial Accounting Standards Board.....	56
International Accounting Standards Board.....	58
Generally Accepted Accounting Principles (GAAP).....	59
Introduction to Financial Reporting .....	61
SFAC No. 1: Objectives of Financial Reporting by Business Entities.....	62
SFAC No. 2: Qualitative Characteristics of Accounting Information .....	63
SFAC No. 6: Elements of Financial Statements of Business Entities (A Replacement of SFAC No. 3).....	66
SFAC No. 5: Recognition and Measurement in Financial Statements of Business Entities .....	71
SFAC No. 7: Using Cash Flow Information and Present Value in Accounting Measurement .....	75
Questions: Miscellaneous Accounting Concepts .....	76
Answers: Miscellaneous Accounting Concepts .....	80
<b>Ch. 2 Structure of an Income Statement .....</b>	<b>82</b>
Overview.....	83
Statement of Income .....	83
Questions: Structure of an Income Statement .....	87
Answers: Structure of an Income Statement .....	93
<b>Ch. 3 Balance Sheet and Statement of Cash Flows .....</b>	<b>96</b>
Overview.....	97
Balance Sheet .....	97
Statement of Cash Flows.....	101
Questions: Statement of Cash Flows .....	109
Answers: Statement of Cash Flows .....	126
<b>Ch. 4 Miscellaneous Financial Statements .....</b>	<b>136</b>
Overview.....	137
Interim Reporting .....	137
Personal Financial Statements and Development Stage Entities .....	138
Questions: Miscellaneous Financial Statements.....	139
Answers: Miscellaneous Financial Statements.....	141
<b>Ch. 5 Receivables and Bad Debt Expense .....</b>	<b>142</b>
Overview.....	143
Accounts Receivable .....	143
Sales Discounts.....	144

# CHAPTER 12 – STOCKHOLDERS' EQUITY

STUDY MANUAL – FINANCIAL ACCOUNTING & REPORTING

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## OVERVIEW

This chapter covers the following technical content from the FAR content specification outline (CSO):

1. Financial reporting, presentation, and disclosures in general-purpose financial statements: statement of changes in equity.
2. Recognition, measurement, valuation, calculation, presentation, and disclosures for equity and stock compensation (share-based payments).

## STOCKHOLDERS' EQUITY

Equity (i.e., stockholders' equity, owners' equity, or net assets), is the residual interest in an entity's assets after subtracting the company's liabilities. Stockholders' equity is presented on the balance sheet and consists of the following major items:

- A. Contributed capital (or paid-in capital).
  1. *Contributed capital* refers to stockholders' investment in an entity. Contributed capital results when any class of stock is issued. It can also occur when owners make contributions for reasons other than the issuance of stock. Contributed capital includes capital stock and additional paid in-capital.
  2. For example:
    - a. Legal capital (i.e., capital stock)—the par or stated value of stock issued.
    - b. Paid-in capital in excess of par or stated value—the excess amount over par for issued common or preferred stock.
    - c. Paid-in capital from other transactions—the excess amount over par for a transaction involving an entity's own stock such as treasury stock or retirement of stock.
- B. Retained earnings.
- C. Accumulated other comprehensive income.
- D. Contra stockholders' equity items (e.g., purchase of treasury stock under the cost method).

Remember: When major changes occur in stockholders' equity accounts, entities are required to disclose them in the notes to the financial statements.

### QUESTIONS: GOVERNMENTAL ACCOUNTING

1. Government-wide statement of net assets reports capital assets:
  - A. at estimated fair value.
  - B. at historical costs including any capitalized interest.
  - C. as part of the fixed asset group.
  - D. in the statement of capital assets.
  
2. Which of the following accounts of a governmental unit is credited when the budget is recorded?
  - A. Reserve for encumbrances.
  - B. Encumbrances.
  - C. Appropriations.
  - D. Estimated revenues.
  
3. SGAS 34 requires that budgetary comparison schedules should:
  - A. not be reported.
  - B. be reported for all proprietary funds.
  - C. be reported for the permanent funds.
  - D. be reported for the general fund and each major special revenue fund with a legally adopted budget.
  
4. The budgetary fund balance reserved for encumbrances account of a governmental fund type is increased when:
  - A. a purchase order is approved.
  - B. supplies previously ordered are received.
  - C. appropriations are recorded.
  - D. the budget is recorded.
  
5. Interest paid on capital debt and leases must be reported on public colleges' cash flow statements as cash from:
  - A. investing activities.
  - B. operations.
  - C. capital and related financing activities.
  - D. noncapital financing activities.
  
6. When the budget of a governmental unit, for which the estimated revenues exceed the appropriations, is adopted and recorded in the general ledger at the beginning of the year, the budgetary fund balance account is:
  - A. debited at the beginning of the year and credited at the end of the year.
  - B. credited at the beginning of the year and no entry made at the end of the year.
  - C. debited at the beginning of the year and no entry made at the end of the year.
  - D. credited at the beginning of the year and debited at the end of the year.
  
7. Cash flows from a public university bookstore would appear on the statement of cash flows as cash flows from:
  - A. operations.
  - B. investing activities.
  - C. financing activities.
  - D. noncapital financing.

**ANSWERS: GOVERNMENTAL ACCOUNTING**

1. B At historical costs including any capitalized interest.
2. C Appropriations—the entry to record the budget:

Estimated revenue control	\$XXX	
Appropriation control		\$XXX
Budgetary fund balance		\$XXX

This entry assumes that estimated revenue exceeds appropriations, which is the normal condition.

3. D SGAS 34 requires that budgetary comparison schedules be reported for the general fund and each major special revenue fund with a legally adopted budget.
4. A A purchase order is approved. When a purchase order is approved, the following entry is made:

Encumbrances control	\$XXX	
Budgetary fund balance reserved for encumbrances		\$XXX

A credit balance is the normal balance for the budgetary fund balance reserved for encumbrances account; therefore, it is increased when a purchase order is approved. When supplies orders are received, the above entry is reversed, decreasing the balance. The account's function is to measure obligations outstanding not recorded as liabilities.

5. C Interest paid on capital debt and leases must be reported on public colleges' cash flow statements as cash from capital and related financing activities.
6. D Credited at the beginning of the year and debited at the end of the year.

Beginning of the year opening entry:

Estimated revenue control	\$1,000,000	
Appropriations		\$950,000
Budgetary fund balance		\$50,000

End of year—reverse the above entry.

7. A Cash flows from a public university's bookstore would be cash from operations.
8. B Only an error would cause a difference in balance.

When a purchase order is approved—		
Encumbrances	\$100	
Reserve for encumbrances		\$100
When the order arrives the entry is reversed—		
Reserve for encumbrances	\$100	
Encumbrances		\$100

9. A Interperiod equity assumes that the revenues of a period will at least equal the expenditures of the period. This financial objective assumes that a balanced budget will be adopted. Residual equity is not related to interperiod equity.